CAPSTAR™
FINANCIAL HOLDINGS, INC.

2022
ANNUAL REPORT

Our Shareholders, Employees and Customers Keep CapStar on the Map

Anchored by four of the most prolific markets in the Southeast - **Nashville**, **Knoxville**, **Chattanooga** and **Asheville** - CapStar expanded its geographic footprint in 2022 to 24 locations across 14 counties in two states.

In addition to national recognition in the top ten for economic vitality, long-term fiscal stability and population growth, Tennessee and North Carolina consistently rank as two of the top states to live and do business in the country.

Sources: U.S. Census Bureau (2022); CNBC (2022); U.S. News and World Report (2022)

TO OUR BUSINESS PARTNERS,

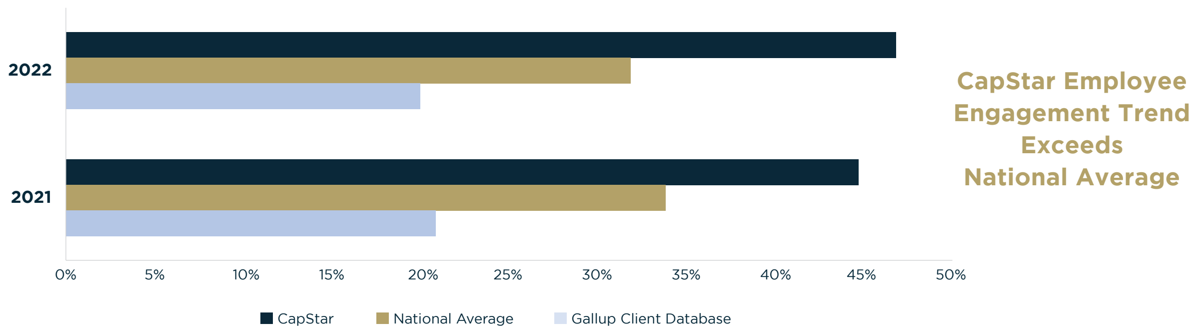
Thank you for your contribution in making CapStar a success. With your support, CapStar continues to deliver outstanding financial products and services to a growing number of businesses and individuals.

2023 marks CapStar's 15th anniversary. Founded in the summer of 2008 with the strategy of offering communities a more personalized experience at a time when banks had become bigger and relationships less meaningful, CapStar is now $3 billion in total assets. Thousands of businesses and individuals have grown and are now stronger as a result of our collective work.

Our People

No group is more important to our success than our people. Having started with approximately 30 employees, today nearly 400 hard-working, dedicated team members support their clients, communities, and families as part of CapStar. In 2022, these employees delivered a high level of service and worked tirelessly to expand existing and add new relationships that will benefit our company for many years.

Annually, the Company invests in an employee engagement survey in partnership with the Gallup organization that specifically focuses on every employee's basic needs, individual contributions, teamwork, and growth opportunities. In 2022, CapStar's percent of engaged employees increased from 45% to 47%, defying global, national and best practice organization employee engagement trends that declined following the COVID-19 pandemic in 2021 after a 10-year rise. Survey results also indicated the Bank's overall engagement mean of 3.97 (on a 5.0 scale) continues to remain above both national and global average engagement ratios.



National Recognition

Excitingly, CapStar's high commitment to service and performance earned the company national recognition as #1 in Tennessee, #5 among banks $1-5 billion in assets, and #14 among all banks nationwide in *Bank Director's* 2022 ranking of "The Best U.S. Banks."

This recognition follows CapStar's recent ranking as #18 among large community banks nationwide by S&P Global Market Intelligence, as one of 30 institutions in the U.S. selected by boutique investment bank Hovde Group as Hovde's High Performers – The Class of 2022, and as the recipient of the prestigious Raymond James Community Bankers Cup for ranking in the top 10% of community banks across the country in 2022.

Simple, Focused and Disciplined Business Model

In pursuit of our mission, we remain focused in delivering a differentiated business model. We are *simple*. We are *focused*. And, we are *disciplined* in everything we do.

Target Customer

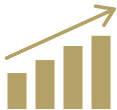
We have clearly defined the customer we are seeking to serve: small to mid-sized businesses, professionals, commercial real estate investors and relationship retail.

Strategy

Our model is different. We deliver basic banking services through a highly personalized experience supported by market-leading responsiveness, flexibility, and customer service.

Delivery

Employees are our most important asset. We work tirelessly to attract and retain highly-effective employees who are driven to provide a *Wow!* employee and customer experience.



Goals

We are a *sales organization* that happens to be in banking. Our goal is to grow meaningful relationships and operate in a manner that generates high returns on capital and stable growth in book value per share.

2022 Performance

Entering 2022, it was anticipated that the economy would begin to return to a more normalized pre-pandemic environment. The prior two years brought unprecedented challenges and produced extraordinary financial results particularly related to our mortgage and Tri-Net businesses, as well as the Small Business Administration's PPP program. However, the resulting impact of this period continued into 2022, leading to one of the most rapid and absolute increases in market interest rates in history. The impact of the movement in market rates generally benefited industry net interest income, slowed loan growth, initiated the first outflow of customer deposits in years, and significantly reduced certain fee-based businesses, including the residential mortgage industry and our Tri-Net business.

Over my nearly 25-year banking career, I have yet to see so many unique challenges be presented over a continuous, short period. I am proud of how CapStar has responded and its performance during this time. Our 2022 results remained strong.

While our net income and earnings per share declined in-line with the industry from peak levels in 2020 and 2021, our return on assets and return on equity remained strong. Our credit and capital management remained top of mind. Most asset quality measures continued to improve, many to record levels, and we returned a record amount of capital to shareholders in the form of dividends and repurchases of our common stock. This was no small feat navigating unforeseen events and continuing to serve our valued clients at a high level.

Four Strategic Objectives

Internally, we communicate and are executing four strategic objectives. While the environment has been volatile, we have made marked progress across each.

1. **Enhance profitability and earnings consistency**
2. **Accelerate organic growth**
3. **Maintain sound risk management**
4. **Execute disciplined capital allocation**

We have enhanced our profitability by improving the discipline of our pricing, redeploying excess levels of cash and securities into higher yielding loans, and working on productivity measures and operating expenses. We have improved the revenue growth capabilities of our core banking and specialty banking businesses. Strong risk management remains priority number one and is being tested every day. Lastly, we are executing a balanced capital management strategy thoughtfully weighing investments in our business, dividends, stock repurchases, with the appropriate capital level to support our business.

2022 Key Results and Accomplishments

- Revenue of $120.6 million
- Net loan charge-offs of $366 thousand
- Earnings per share of $1.77
- Return on average assets of 1.24%
- Return on average equity of 10.74%
- First cohort of **CapStar Diversity Scholarship** recipients graduated from The Southeastern School of Banking
- Recent **Chattanooga** expansion exceeded $250 million in assets; **Knoxville** expansion approaching $185 million in assets
- First expansion outside Tennessee with organic entrance into **Asheville, North Carolina**
- Revitalization of the **Government Guaranteed Lending** division with the hiring of a team of 14 dedicated and experienced professionals from top 10 SBA originators

In 3Q22, CapStar entered Asheville, North Carolina, followed by a significant investment to expand our Chattanooga team and open a full-service location in historic downtown Chattanooga.

2022 Financial Highlights

$2.3 BILLION
LOANS

$2.7 BILLION
DEPOSITS

$39.0 MILLION
NET INCOME

$1.77 EPS | **1.63%** PTPP/A | **1.24%** ROA

Looking Forward

Current Environment

The operating environment remains difficult. All indications are that 2023 will be a challenging year for banking. While elevated inflation indications remain, the Federal Reserve's actions are beginning to have major impacts. Layoffs have begun across many industries, loan demand is slowing as companies assess the economic outlook and the affordability of credit for businesses and individuals has risen, and importantly, customers have used deposits to pay down higher-cost borrowings.

The likely result of this will be near term pressure to industry net interest margins and limited balance sheet growth. Additionally, we are proactively assessing our loan portfolio for early indications of credit weakness in the event of a prolonged recession.

Looking Forward

As we work diligently to address the current environment, we remain excited about the strength of our business and markets. CapStar has a strong core banking model and many specialty businesses that are very valuable in most economic environments. We continue to serve our customers in an exemplary manner and are looking for ways to expand existing and grow new relationships. Alongside, we operate in favorable markets and are seeing the initial benefits from the recent sale of two large Tennessee-based competitors – a trend we believe is just beginning and that could continue to benefit CapStar for years to come.

Thank you for your commitment to and support of CapStar!

Timothy K. Schools
President and CEO

Our Value Proposition

Guidance - we deliver financial services to businesses across the Southeast and beyond in search of a more tailored and strategic financial partnership. Our consultative approach prioritizes solutions for our clients based on the dreams that drive them to achieve every day.

Responsiveness - we believe to win, we must act fast. We operate with a sense of urgency established by our client's timeline and needs.

Flexibility - we were created to be large enough to offer solutions for any need, but small enough to adapt to each client's unique situation.

And, we think it's important to have fun along the way, so we deliver fresh products and services through a differentiated approach.

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-K

(Mark One)

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

For the fiscal year ended December 31, 2022

OR

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

For the transition period from ________to________

Commission File Number 001-37886

CAPSTAR FINANCIAL HOLDINGS, INC.

(Exact name of Registrant as specified in its Charter)

Tennessee	**81-1527911**
(State or other jurisdiction of incorporation or organization)	**(IRS Employer Identification No.)**
1201 Demonbreun Street, Suite 700 Nashville, Tennessee	**37203**
(Address of principal executive office)	**(zip code)**

Registrant's telephone number, including area code (615) 732-6400

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

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common Stock, $1.00 par value per share	**CSTR**	**Nasdaq Global Select Market**

Securities registered pursuant to Section 12(g) of the Act:
None

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

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

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definition of "large accelerated filer," "accelerated filer" "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	☐	Accelerated filer	☒
Non-accelerated filer	☐	Small reporting company	☐
		Emerging growth company	☐

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

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

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

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

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

As of June 30, 2022, the last business day of the registrant's most recently completed second fiscal quarter, the aggregate market value of the registrant's voting and non-voting common equity held by non-affiliates of the registrant was $430,355,949 based on the closing sales price of $19.62 per share as reported on the Nasdaq Global Select Market.

Indicate the number of shares outstanding of each of the registrant's classes of common stock, as of the latest practicable date.

	Shares outstanding as of February 28, 2023
Common Stock, par value $1.00 per share	21,557,567

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's Definitive Proxy Statement relating to the 2023 Annual Meeting of Shareholders (the "2023 Proxy Statement"), which will be filed within 120 days after December 31, 2022, are incorporated by reference into Part III of this Annual Report on Form 10-K.

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CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K contains certain forward-looking statements that are included pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. These forward-looking statements reflect our current views with respect to, among other things, statements relating to the Company's assets, business, cash flows, condition (financial or otherwise), credit quality, financial performance, liquidity, short and long-term performance goals, prospects, results of operations, strategic initiatives, the benefits, cost and synergies of completed acquisitions or dispositions, and the timing, benefits, costs and synergies of future acquisitions, disposition and other growth opportunities. These statements are often, but not always, made through the use of words or phrases such as "may," "should," "could," "predict," "potential," "believe," "will likely result," "expect," "continue," "will," "anticipate," "seek," "aspire," "estimate," "intend," "plan," "project," "projection," "forecast," "roadmap," "goal," "target," "would," and "outlook," or the negative version of those words or other comparable words of a future or forward-looking nature.–Forward-looking statements express only management's beliefs regarding future results or events and are subject to inherent uncertainty, risks and changes in circumstances, many of which are outside of management's control. Uncertainty, risks, changes in circumstances and other factors could cause the Company's actual results to differ materially from those projected in the forward-looking statements. Factors that could cause actual results to differ from those discussed in such forward-looking statements include, but are not limited to: (1) difficulty attracting and retaining highly-effective employees; (2) our ability to successfully execute our business plan; (3) difficulty growing or sustaining deposit and loan balances; (4) changes in consumer preferences, spending and borrowing habits, and demand for our products and services; (5) general economic conditions, especially in the communities and markets in which we conduct our business; (6) credit risk, including the risk that negative credit quality trends may lead to a deterioration of asset quality, risk that our allowance for credit losses may not be sufficient to absorb actual losses in our loan portfolio, and risk from concentrations within our loan portfolio; (7) market risk, including interest rate and liquidity risk; (8) operational risk, including cybersecurity risk and risk of fraud, data processing system failures, and network breaches; (9) increased competition, including competition from non-bank financial institutions; (10) changes in regulations, laws, taxes, government policies, monetary policies and accounting policies affecting bank holding companies and their subsidiaries; (11) regulatory enforcement actions and adverse legal actions; and (12) other economic, competitive, technological, operational, governmental, regulatory, and market factors affecting our operations. The foregoing factors should not be construed as exhaustive and should be read in conjunction with the section entitled "Risk Factors" included in this Report. If one or more events related to these or other risks or uncertainties materialize, or if our underlying assumptions prove to be incorrect, actual results may differ materially from our forward-looking statements. Accordingly, you should not place undue reliance on any such forward-looking statements. Forward-looking statements made herein reflect management's expectations as of the date such statements are made. The Company undertakes no obligation to update any forward-looking statement to reflect events or circumstances that arise after the date such statements are made.

PART I

ITEM 1. BUSINESS

OVERVIEW

CapStar Financial Holdings, Inc., (the "Company") is a bank holding company that is headquartered in Nashville, Tennessee. The Company operates primarily through its wholly owned subsidiary, CapStar Bank (the "Bank" or "CapStar"). CapStar provides traditional banking and other financial services through its 23 bank locations and 397 associates. As of December 31, 2022, the Company had total assets of $3.1 billion, total deposits of $2.7 billion, total net loans of $2.3 billion, and shareholders' equity of $354.2 million.

The primary products and services provided by CapStar are:

- Commercial Banking – CapStar offers a full range of banking services to businesses and professionals, including deposit and savings accounts, treasury management services, as well as financing for commercial and industrial needs, owner-occupied real estate, construction and land development, and non-owner-occupied income producing real estate some of which are sold in the secondary market.
- Consumer Banking – CapStar offers a full range of banking services to individuals, including deposit and savings accounts as well as residential real estate loans, home equity loans, and other consumer loans some of which are sold in the secondary market.
- Wealth Management – CapStar specializes in helping individuals develop sound retirement strategies.

Our strategy is to maintain broadly diversified loan and deposit portfolios in terms of the type of loan product, the type of client and the industries in which our business clients are engaged.

Commercial and industrial loans consist of loans to small to mid-sized businesses and other legal entities. Commercial and industrial loans are reliant on the ability of a borrower's cash flow from operations to repay the loan. Most commercial and industrial loans are secured with the collateral securing these loans being inventory, receivables, and equipment. Lending products include commercial loans, business term loans, equipment financing and lines of credit to a diversified mix of small and medium sized businesses. As of December 31, 2022, commercial and industrial loans totaled $496.3 million or 21.5% of the Company's loan portfolio.

Commercial real estate loans consist of owner-occupied and non-owner-occupied commercial real estate loans. Owner-occupied commercial real estate loans having many of the characteristics of commercial and industrial loans with the primary source of repayment reliant on the ability of the borrower's cash flow to repay the loan. Non-owner occupied commercial real estate loans finance well-managed income producing properties supported by a history of profitable operations and cash flows, and proven operating stability. As of December 31, 2022, owner-occupied and non-owner-occupied commercial real estate loans totaled $246.1 million and $803.6 million or 10.6% and 34.7%, respectively, of the Company's loan portfolio.

Residential real estate loans consist of loans to individuals secured by first priority liens for the purchase or refinance of a residence as well as first priority lien home equity loans which allow individuals to borrow against equity in their home. Residential mortgages primarily consist of three- and five-year adjustable-rate mortgages with amortization up to 30 years as well as longer-term fixed rate loans produced by our mortgage division with the intent to sell in the secondary market. Home equity loans include lines of credit as well as amortizing term loans on which may be first or second liens. As of December 31, 2022, residential real estate loans totaled $402.6 or 17.4% of the Company's loan portfolio.

Construction and land development loans consist of loans where the repayment is dependent on the successful completion and operation and/or sale of the related real estate project. Construction and land development loans include 1-4 family construction projects and commercial construction endeavors such as warehouses, apartments, office and retail space and land acquisition and development. As of December 31, 2022, construction and land development loans totaled $230.0 million or 9.9% of the Company's loan portfolio.

Consumer loans consist of loans secured by automobiles, boats, recreational vehicles, certificates of deposit, other personal property, or in a limited case may be unsecured. As of December 31, 2022, consumer loans totaled $53.4 million or 2.3% of the Company's loan portfolio.

Other loans consists of all loans not included in the classes of loans above and leases. As of December 31, 2022, other loans totaled $80.8 million or 3.5% of the Company's loan portfolio.

CapStar's underwriting guidelines are reviewed regularly and approved annually by our Board of Directors. Our underwriting process includes:

- receipt of certain financial information, such as financial statements, tax returns and credit reports, to ensure that the potential borrower has sufficient recurring cash flow and liquidity to repay the loan;
- identifying and evaluating all significant direct and contingent liabilities;
- determination that the structure of the loan matches the underlying purpose of and repayment source for the loan, the potential borrower's creditworthiness and the depreciable life of any collateral;
- verification that the potential borrower has a demonstrated propensity to repay the loan/the borrower's indebtedness/etc.; and
- consideration of the value, liquidity and marketability of the potential borrower's collateral.

Our underwriting processes collaboratively engage our bankers and credit underwriters in the analysis of each loan request. We manage our credit risks by analyzing metrics in order to maintain a conservative and well-diversified loan portfolio reflective of our assessment of various subsets within our market. Based upon our aggregate exposure to any given borrower relationship, we employ a tiered review of loan originations that may involve joint line and credit authorization, our bank's Credit Committee or, ultimately, our full board of directors.

Our strategy for credit risk management includes the disciplined underwriting process described above and ongoing risk monitoring and review processes for all loan exposures. Our Chief Credit Officer provides bank-wide credit oversight and regularly reviews the loan portfolio to ensure that the underwriting and risk identification processes are functioning properly. We strive to identify potential problem loans early in an effort to aggressively seek resolution of these situations before the loans become delinquent or impaired, record any necessary charge-offs promptly and maintain adequate allowance levels for probable loan losses inherent in the loan portfolio. Annually, we submit ourselves to review by independent third parties to validate our internal oversight.

Market Area and Competition

CapStar operates in the community markets of Athens, Lawrenceburg/Waynesboro, and Manchester, Tennessee as well as the metropolitan markets of Asheville, North Carolina and Chattanooga, Knoxville, and Nashville, Tennessee which are included among the fastest growing nationally. The bank seeks business development and serves customers through a team of commercial relationship managers and its 23 banking locations. The financial services industry is highly competitive and each of these markets has a significant presence of other financial service providers. In particular, we estimate that, as of June 30, 2022, Tennessee included more than 80 financial institutions with over $118 billion in deposits. We compete directly with other bank and nonbank institutions located within our market area, internet-based banks, and out-of-market banks that advertise in or otherwise serve our market area, along with money market and mutual funds, brokerage houses, mortgage companies, and insurance companies or other commercial entities that offer financial services products. Competition involves efforts to retain current clients, obtain new loans and deposits, increase the scope and type of services offered, and offer competitive interest rates paid on deposits and charged on loans. Many of our competitors enjoy competitive advantages, including greater financial resources, a wider geographic presence, the ability to offer additional services, more favorable pricing alternatives, and lower origination and operating costs. Some of our competitors have been in business for a long time and have an established client base and name recognition. We expect to continue to face increasing competition.

Expansion and Acquisitions

In January of 2020, the Company announced its first out of market expansion hiring a Knoxville commercial banking team. In October of 2021, the Company announced the hiring of a Chattanooga commercial banking team. In July of 2022, the Company announced its expansion to Asheville, NC through the hiring of a commercial banking team. During this period, the Company also hired additional commercial and retail bankers within its existing markets. Additionally, during the fourth quarter of 2022, the Company announced the hiring of an experienced financial professional to expand the SBA division.

On July 1, 2020, the Company completed the acquisition of FCB Corporation ("FCB"), the bank holding company for the First National Bank of Manchester. The Company acquired all of the outstanding shares of common stock of

FCB for approximately 3.0 million shares of common stock. At the time of acquisition, Manchester had four banking locations throughout middle Tennessee. The operations of Manchester are included in our financial statements beginning July 1, 2020.

On July 1, 2020, the Company also completed the acquisition of the Bank of Waynesboro (“BOW”). The Company acquired all of the outstanding shares of common stock of BOW for approximately 0.7 million shares of common stock of our Company. At the time of acquisition, BOW had six banking locations throughout Southern Tennessee. The operations of BOW are included in our financial statements beginning July 1, 2020.

Human Capital

As of December 31, 2022, we had 397 total employees. As a service-oriented business, our long-term success depends on our people and we are committed to taking a multi-dimensional approach to talent and culture. Our people and culture are critical to the Company’s long-term success.

As such, our talent vision and strategy focus on:

- Enabling talent and performance management that generates career opportunities and creates future leaders of the organization.
- Empathy towards others that gives us a unique understanding and ability to provide internal and external service excellence.
- Supporting a healthy work-life balance by offering generous paid time off for vacation (four weeks per year), holidays (including birthday), and sick leave.
- Delivering a competitive compensation package, including medical, dental and vision benefits; life, disability, and long-term care insurance; and 401(k) employer contribution.

SUPERVISION AND REGULATION

General

Insured banks, their holding companies and their affiliates are extensively regulated under federal and state law. As a result, our growth and earnings performance and that of our subsidiaries may be affected not only by management decisions and general economic conditions, but also by the requirements of federal and state statutes and by the regulations and policies of various bank regulatory agencies, including the Tennessee Department of Financial Institutions ("TDFI"), the Board of Governors of the Federal Reserve System (the “Federal Reserve”), the Federal Deposit Insurance Corporation (“FDIC”), the Office of the Comptroller of the Currency (“OCC”) and the Consumer Financial Protection Bureau (“CFPB”). Furthermore, tax laws administered by the Internal Revenue Service (“IRS”) and state taxing authorities, accounting rules developed by the Financial Accounting Standards Board (“FASB”), securities laws administered by the Securities and Exchange Commission (“SEC”) and state securities authorities, anti-money laundering laws enforced by the U.S. Department of the Treasury and mortgage related rules, including with respect to loan securitizations and servicing by the U.S. Department of Housing and Urban Development and agencies such as Ginnie Mae and Freddie Mac, have an impact on our business. The effect of these statutes, regulations, regulatory policies and rules are significant to our operations and results and those of our bank, and the nature and extent of future legislative, regulatory or other changes affecting financial institutions are impossible to predict with any certainty.

Federal and state banking laws impose a comprehensive system of supervision, regulation and enforcement on the operations of insured banks, their holding companies and affiliates that are intended primarily for the protection of the depositors of banks, rather than their shareholders. These federal and state laws, and the regulations of the bank regulatory agencies issued under them, affect, among other things, the scope of business, the kinds and amounts of investments banks may make, reserve requirements, capital levels relative to operations, the nature and amount of collateral for loans, the establishment of branches, the ability to merge, consolidate and enter into acquisitions with other companies, dealings with insiders and affiliates and the payment of dividends.

This supervisory and regulatory framework subjects banks and bank holding companies to regular examination by their respective primary federal regulators, which results in examination reports and ratings that, while not publicly available, can impact the conduct and growth of their businesses. These examinations consider not only compliance with applicable laws and regulations, but also capital levels, asset quality and risk, management ability and

performance, earnings, liquidity, and various other factors. The regulatory agencies generally have broad discretion to impose restrictions and limitations on the operations of a regulated entity where the agencies determine, among other things, that such operations are unsafe or unsound, fail to comply with applicable law or are otherwise inconsistent with laws and regulations or with the supervisory policies of these agencies.

The following is a summary of the material elements of the supervisory and regulatory framework applicable to us and our bank. It does not describe all of the statutes, regulations and regulatory policies that apply, nor does it restate all of the requirements of those that are described. The descriptions are qualified in their entirety by reference to the particular statutory and regulatory provision.

Bank Holding Company Regulation

Since we own all of the capital stock of our bank, we are a bank holding company under the Bank Holding Company Act of 1956, as amended ("BHC Act"). As a result, we are primarily subject to the supervision, examination and reporting requirements of the BHC Act and the regulations of the Federal Reserve.

Acquisition of Banks

The BHC Act requires every bank holding company to obtain the Federal Reserve's prior approval before:

- acquiring direct or indirect ownership or control of any voting shares of any bank if, after the acquisition, the bank holding company will, directly or indirectly, own or control 5% or more of the bank's voting shares;
- acquiring all or substantially all of the assets of any bank; or
- merging or consolidating with any other bank holding company.

Additionally, the BHC Act provides that the Federal Reserve may not approve any of the above transactions if such transaction would result in or tend to create a monopoly or substantially lessen competition or otherwise function as a restraint of trade, unless the anti-competitive effects of the proposed transaction are clearly outweighed by the public interest in meeting the convenience and needs of the community to be served. The Federal Reserve is also required to consider the financial and managerial resources and future prospects of the bank holding companies and banks concerned and the convenience and needs of the community to be served. The Federal Reserve's consideration of financial resources includes a focus on capital adequacy, which is discussed in the section titled "Item 1. Business—Regulation and Supervision—Capital Adequacy." The Federal Reserve also considers the effectiveness of the institutions in combating money laundering, including a review of the anti-money laundering program of the acquiring bank holding company and the anti-money laundering compliance records of a bank to be acquired as part of the transaction. Finally, the Federal Reserve takes into consideration the extent to which the proposed transaction would result in greater or more concentrated risks to the stability of the U.S. banking or financial system.

Under the BHC Act, if well-capitalized and well-managed, we or any other bank holding company located in Tennessee may purchase a bank located outside of Tennessee without regard to whether such transaction is prohibited under state law. Conversely, a well-capitalized and well-managed bank holding company located outside of Tennessee may purchase a bank located inside Tennessee without regard to whether such transaction is prohibited under state law. In each case, however, state law may place restrictions on the acquisition of a bank that has only been in existence for a limited amount of time or will result in concentrations of deposits exceeding limits specified by statute. For example, Tennessee law currently prohibits a bank holding company from acquiring control of a Tennessee-based financial institution until the target financial institution has been in operation for at least three years.

Change in Bank Control

Subject to various exceptions, the BHC Act and the Change in Bank Control Act, together with related regulations, require Federal Reserve approval prior to any person or company acquiring "control" of a bank holding company. Under a rebuttable presumption established by the Federal Reserve pursuant to the Change in Bank Control Act, the acquisition of 10% or more of a class of voting stock of a bank holding company would constitute acquisition of "control" of the bank holding company if no other person will own, control, or hold the power to vote a greater percentage of that class of voting stock immediately after the transaction or the bank holding company has registered securities under the Exchange Act. In addition, any person or group of persons acting in concert must obtain the approval of the Federal Reserve under the BHC Act before acquiring 25% (or 5% in the case of an acquirer that is already a bank holding company) or more of the outstanding voting stock of a bank holding company, the right to

control in any manner the election of a majority of the company's directors, or otherwise obtaining control or a "controlling influence" over the bank holding company.

Permitted Activities

Under the BHC Act, a bank holding company is generally permitted to engage in or acquire direct or indirect control of the voting shares of any company engaged in the following activities:

- banking or managing or controlling banks; and
- any activity that the Federal Reserve determines to be so closely related to banking as to be a proper incident to the business of banking.

Activities that the Federal Reserve has found to be so closely related to banking as to be a proper incident to the business of banking include:

- factoring accounts receivable;
- making, acquiring, brokering or servicing loans and usual related activities in connection with the foregoing;
- leasing personal or real property under certain conditions;
- operating a non-bank depository institution, such as a savings association;
- engaging in trust company functions in a manner authorized by state law;
- financial and investment advisory activities;
- discount securities brokerage activities;
- underwriting and dealing in government obligations and money market instruments;
- providing specified management consulting and counseling activities;
- performing selected data processing services and support services;
- acting as an agent or broker in selling credit life insurance and other types of insurance in connection with credit transactions; and
- performing selected insurance underwriting activities.

The Federal Reserve may order a bank holding company or its subsidiaries to terminate any of these activities or to terminate its ownership or control of any subsidiary when it has reasonable cause to believe that the bank holding company's continued ownership, activity or control constitutes a serious risk to the financial safety, soundness, or stability of it or any of its bank subsidiaries.

Support of Subsidiary Institutions

The Federal Deposit Insurance Act and Federal Reserve policy require a bank holding company to serve as a source of financial and managerial strength to its bank subsidiaries. As a result of a bank holding company's source of strength obligation, a bank holding company may be required to provide funds to a bank subsidiary in the form of subordinate capital or other instruments which qualify as capital under bank regulatory rules. Any loans from the holding company to such subsidiary banks likely would be unsecured and subordinated to such bank's depositors and perhaps to other creditors of the bank.

Repurchase or Redemption of Securities

A bank holding company is generally required to give the Federal Reserve prior written notice of any purchase or redemption of its own then outstanding equity securities if the gross consideration for the purchase or redemption, when combined with the net consideration paid for all such purchases or redemptions during the preceding 12 months, is equal to 10% or more of the company's consolidated net worth. The Federal Reserve may disapprove such a purchase or redemption if it determines that the proposal would constitute an unsafe and unsound practice, or would violate any law, regulation, Federal Reserve order or directive, or any condition imposed by, or written agreement with, the Federal Reserve. The Federal Reserve has adopted an exception to this approval requirement for well-capitalized bank holding companies that meet certain conditions.

Bank Regulation and Supervision

Our bank is subject to extensive federal and state banking laws and regulations that impose restrictions on and provide for general regulatory oversight of the operations of our bank. These laws and regulations are generally intended to protect the safety and soundness of our bank and our bank's depositors, rather than our shareholders. The following discussion describes the material elements of the regulatory framework that applies to our bank.

Since our bank is a commercial bank chartered under the laws of the state of Tennessee and is a member of the Federal Reserve System, it is primarily subject to the supervision, examination and reporting requirements of the Federal Reserve and the TDFI. The Federal Reserve and the TDFI regularly examine our bank's operations and have the authority to approve or disapprove mergers, the establishment of branches and similar corporate actions. Both regulatory agencies have the power to take enforcement action to prevent the development or continuance of unsafe or unsound banking practices or other violations of law. Our bank's deposits are insured by the FDIC to the maximum extent provided by law. Our bank is also subject to numerous federal and state statutes and regulations that affect its business, activities and operations.

Branching

Under current Tennessee law, our bank may open branch offices throughout Tennessee with the prior approval of, or prior notice to, the TDFI and the Federal Reserve. In addition, with prior regulatory approval, our bank may acquire branches of existing banks located in Tennessee. Under federal law, our bank may establish branch offices with the prior approval of the Federal Reserve. While prior law imposed various limits on the ability of banks to establish new branches in states other than their home state, the Dodd-Frank Act allows a bank to branch into a new state by setting up a new branch if, under the laws of the state in which the branch is to be located, a state bank chartered by that state would be permitted to establish the branch. This makes it much simpler for banks to open de novo branches in other states.

FDIC Insurance and Other Assessments

The Bank pays deposit insurance assessments to the Deposit Insurance Fund, which is determined through a risk-based assessment system. The Bank's deposit accounts are currently insured by the Deposit Insurance Fund, generally up to a maximum of $250,000 per separately insured depositor, per ownership category. The Bank pays assessments to the FDIC for such deposit insurance. Under the current assessment system, the assessment rate is determined by the risk category assigned to an institution based on the institution's most recent supervisory and capital evaluations which are designed to measure risk, with riskier institutions paying a higher assessment rate. Under the Federal Deposit Insurance Act, the FDIC may terminate a bank's deposit insurance upon a finding that the institution has engaged in unsafe and unsound practices, is in an unsafe or unsound condition to continue operations, or has violated any applicable law, regulation, rule, order, agreement or condition imposed by the FDIC.

Community Reinvestment Act

The Community Reinvestment Act ("CRA") requires that, in connection with examinations of financial institutions within their respective jurisdictions, the federal banking agencies will evaluate the record of each financial institution in meeting the needs of its local community, including low- and moderate-income neighborhoods. Our bank's record of performance under the CRA is publicly available. A bank's CRA performance is also considered in evaluating applications seeking approval for mergers, acquisitions, and new offices or facilities. Failure to adequately meet these criteria could result in additional requirements and limitations being imposed on the bank. Additionally, we must publicly disclose the terms of certain CRA-related agreements. As of December 31, 2022 the Bank had a CRA rating of "Satisfactory."

Interest Rate Limitations

Interest and other charges collected or contracted for by our bank are subject to applicable state usury laws and federal laws concerning interest rates.

Federal Laws Applicable to Consumer Credit and Deposit Transactions

Our bank's loan and deposit operations are subject to a number of federal consumer protection laws, including:

- the Federal Truth in Lending Act, governing disclosures of credit terms to consumer borrowers;
- the Home Mortgage Disclosure Act, requiring financial institutions to provide information to enable the public and public officials to determine whether a financial institution is fulfilling its obligation to help meet the housing needs of the communities it serves;
- the Equal Credit Opportunity Act, prohibiting discrimination on the basis of race, color, religion, national origin, sex, marital status or certain other prohibited factors in all aspects of credit transactions;
- the Fair Credit Reporting Act, or FCRA, governing the use and provision of information to credit reporting agencies;
- the Fair Debt Collection Practices Act, governing the manner in which consumer debts may be collected by debt collectors;
- the Service Members Civil Relief Act, governing the repayment terms of, and property rights underlying, secured obligations of persons in military service;
- the Gramm-Leach-Bliley Act, governing the disclosure and safeguarding of sensitive non-public personal information of our clients;
- the Right to Financial Privacy Act, imposing a duty to maintain confidentiality of consumer financial records and prescribes procedures for complying with administrative subpoenas of financial records;
- the Electronic Funds Transfer Act governing automatic deposits to and withdrawals from deposit accounts and clients' rights and liabilities arising from the use of automated teller machines and other electronic banking services; and
- the rules and regulations of the CFPB and various federal agencies charged with the responsibility of implementing these federal laws.

Capital Adequacy

Pursuant to the Dodd-Frank Act, under the adopted regulations, the Basel member central bank and federal bank regulators approved the Basel Capital Adequacy Accord, or Basel III. The U.S. Basel III rule's minimum capital to risk-weighted assets, or RWA, requirements are as follows: (1) a common equity Tier 1 capital ratio of 4.5%, (2) a Tier 1 capital ratio of 6.0%, and (3) a total capital ratio of 8.0%. The minimum leverage ratio (Tier 1 capital to total assets) is 4.0%. The rule also changed the definition of capital, mainly by adopting stricter eligibility criteria for regulatory capital instruments, and new constraints on the inclusion of minority interests, mortgage-servicing assets, deferred tax assets, and certain investments in the capital of unconsolidated financial institutions. In addition, the U.S. Basel III rule requires that most regulatory capital deductions be made from common equity Tier 1 capital.

Under the U.S. Basel III rule, in order to avoid limitations on capital distributions, including dividend payments and certain discretionary bonus payments to executive officers, a banking organization must maintain a capital conservation buffer composed of common equity Tier 1 capital above its minimum risk-based capital requirements. The buffer is measured relative to RWA. Phase-in of the capital conservation buffer requirements began on January 1, 2016, and the requirements became fully phased in on January 1, 2019. A banking organization maintaining capital levels in excess of the fully phased-in capital conservation buffer of 2.5% would not be subject to limits on capital distributions or discretionary bonus payments; however, a banking organization with a buffer of less than 2.5% would be subject to increasingly stringent limitations as the buffer approaches zero. A banking organization also would be prohibited from making distributions or discretionary bonus payments during any quarter if its eligible retained income is negative in that quarter and its capital conservation buffer ratio was less than 2.5% at the beginning of the quarter. Effectively, the Basel III framework requires us to meet minimum risk-based capital ratios of (i) 7% for common equity Tier 1 capital, (ii) 8.5% Tier 1 capital, and (iii) 10.5% total capital. The eligible retained income of a banking organization is defined as its net income for the four calendar quarters preceding the current calendar quarter, based on the organization's quarterly regulatory reports, net of any distributions and associated tax effects not already reflected in net income. With the capital conservation buffer fully phased in, the minimum capital requirements plus the capital conservation buffer will exceed the prompt corrective action, or PCA, well-capitalized thresholds.

Failure to meet statutorily mandated capital guidelines or more restrictive ratios separately established for a banking institution could subject the institution to a variety of enforcement remedies available to federal regulatory authorities, including issuance of a capital directive, the termination of deposit insurance by the FDIC, a prohibition on accepting or renewing brokered deposits, limitations on the rates of interest that the institution may pay on its deposits, and other restrictions on its business.

Prompt Corrective Action

The Federal Deposit Insurance Corporation Improvement Act of 1991 ("FDICIA") establishes a system of "prompt corrective action" ("PCA") to resolve the problems of undercapitalized insured depository institutions. Under this system, the federal banking regulators have established five capital categories (well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized and critically undercapitalized) into which all insured depository institutions are placed. The federal banking agencies have specified by regulation the relevant capital thresholds and other qualitative requirements for each of those categories. For an insured depository institution to be "well capitalized" under the PCA framework, it must have a common equity Tier 1 capital ratio of 6.5%, Tier 1 capital ratio of 8.0%, a total capital ratio of 10.0%, and a Tier 1 leverage ratio of 5.0%, and must not be subject to any written agreement, order or capital directive, or prompt corrective action directive issued by its primary federal regulator to meet and maintain a specific capital level for any capital measure. As of December 31, 2022, our bank qualified for the "well capitalized" category.

Federal banking regulators are required to take various mandatory supervisory actions and are authorized to take other discretionary actions with respect to institutions in the three undercapitalized categories. The severity of the action depends upon the capital category in which the institution is placed. For example, institutions in all three undercapitalized categories are automatically restricted from paying distributions and management fees, whereas only an institution that is significantly undercapitalized or critically undercapitalized is restricted in its compensation paid to senior executive officers. Generally, subject to a narrow exception, the banking regulator must appoint a receiver or conservator for an institution that is critically undercapitalized.

An institution that is categorized as undercapitalized, significantly undercapitalized, or critically undercapitalized is required to submit an acceptable capital restoration plan to its appropriate federal banking agency. A bank holding company must guarantee that a subsidiary depository institution meets its capital restoration plan, subject to various limitations. The controlling holding company's obligation to fund a capital restoration plan is limited to the lesser of (i) 5% of an undercapitalized subsidiary's assets at the time it became undercapitalized and (ii) the amount required to meet regulatory capital requirements. An undercapitalized institution is also generally prohibited from increasing its average total assets, making acquisitions, establishing any branches or engaging in any new markets or product offerings, except under an accepted capital restoration plan or with Federal Reserve approval.

The regulations also establish procedures for downgrading an institution to a lower capital category based on supervisory factors other than capital.

Liquidity

Financial institutions are subject to significant regulatory scrutiny regarding their liquidity positions. This scrutiny has increased during recent years, as the economic downturn that began in the late 2000s negatively affected the liquidity of many financial institutions. Various bank regulatory publications, including Federal Reserve SR 10-6 (Funding and Liquidity Risk Management) and FDIC Financial Institution Letter FIL-84-2008 (Liquidity Risk Management), address the identification, measurement, monitoring and control of funding and liquidity risk by financial institutions.

Payment of Dividends

We are a legal entity separate and distinct from our bank. Our principal source of cash flow, including cash flow to pay dividends to our shareholders, is dividends our bank pays to us as our bank's sole shareholder. Statutory and regulatory limitations apply to our bank's payment of dividends to us as well as to our payment of dividends to our shareholders. The requirement that a bank holding company must serve as a source of strength to its subsidiary banks also results in the position of the Federal Reserve that a bank holding company should not maintain a level of cash dividends to its shareholders that places undue pressure on the capital of its bank subsidiaries or that can be funded only through additional borrowings or other arrangements that may undermine the bank holding company's ability to serve as a source of strength. Our ability to pay dividends is also subject to the provisions of Tennessee corporate law which prevents payment of dividends if, after giving effect to such payment, we would not be able to pay our debts as they become due in the usual course of business or our total assets would be less than the sum of our total liabilities plus any amounts needed to satisfy any preferential rights if we were dissolving. In addition, in deciding whether or not to declare a dividend of any particular size, our board of directors must consider our and our bank's current and prospective capital, liquidity, and other needs.

The TDFI also regulates our bank's dividend payments. Under Tennessee law, a state-chartered bank may not pay a dividend without prior approval of the Commissioner of the TDFI if the total of all dividends declared by its board of directors in any calendar year will exceed (i) the total of its retained net income for that year, plus (ii) its retained net income for the preceding two years.

Our bank's payment of dividends may also be affected or limited by other factors, such as the requirement to maintain adequate capital above regulatory guidelines. The federal banking agencies have indicated that paying dividends that deplete a depository institution's capital base to an inadequate level would be an unsafe and unsound banking practice. Under FDICIA, a depository institution may not pay any dividends if payment would cause it to become undercapitalized or if it already is undercapitalized. Moreover, the federal agencies have issued policy statements providing that bank holding companies and insured banks should generally only pay dividends out of current operating earnings.

Restrictions on Transactions with Affiliates and Insiders

Our bank is subject to Section 23A of the Federal Reserve Act, which places limits on the amount of the bank's transactions with its affiliates.

Subject to various exceptions, the total amount of the bank's transactions with affiliates is limited in amount, as to any one affiliate, to 10% of a bank's capital and surplus and, as to all affiliates combined, to 20% of a bank's capital and surplus. In addition to the limitation on the amount of these transactions, transactions with affiliates also must meet specified collateral requirements and safety and soundness requirements. Our bank must also comply with provisions prohibiting the acquisition of low-quality assets from an affiliate.

Our bank is also subject to Section 23B of the Federal Reserve Act, which, among other things, prohibits a bank from engaging in transactions with affiliates, as well as other types of transactions set forth in Section 23B, unless the transactions are on terms substantially the same, or at least as favorable to the bank, as those prevailing at the time for comparable transactions with nonaffiliated companies.

Our bank is also subject to restrictions on extensions of credit to its executive officers, directors, principal shareholders and their related interests. These extensions of credit (i) must be made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions between the bank and third parties, and (ii) must not involve more than the normal risk of repayment or present other unfavorable features. There are also individual and aggregate limitations on loans to insiders and their related interests. The aggregate amount of insider loans generally cannot exceed the institution's total unimpaired capital and surplus. Insiders and banks are subject to enforcement actions for knowingly entering into insider loans in violation of applicable restrictions.

Single Borrower Credit Limits

Under Tennessee law, total loans and extensions of credit to a borrower may not exceed 15% of our bank's capital, surplus and undivided profits. However, such loans may be in excess of that percentage, but not above 25%, if each loan in excess of 15% is first submitted to and approved in advance in writing by the board of directors and a record is kept of such written approval and reported to the board of directors quarterly.

Commercial Real Estate Concentration

In December 2006, the federal banking regulators issued guidance entitled "Concentrations in Commercial Real Estate Lending, Sound Risk Management Practices" to address increased concentrations in commercial real estate, or CRE, loans. In addition, in December 2015, the federal banking agencies issued additional guidance entitled "Statement on Prudent Risk Management for Commercial Real Estate Lending." Together, these guidelines describe the criteria the agencies will use as indicators to identify institutions potentially exposed to CRE concentration risk. An institution that has (i) experienced rapid growth in CRE lending, (ii) notable exposure to a specific type of CRE, (iii) total reported loans for construction, land development, and other land representing 100% or more of the institution's capital, or (iv) total CRE loans representing 300% or more of the institution's capital, and the outstanding balance of the institutions CRE portfolio has increased by 50% or more in the prior 36 months, may be identified for further supervisory analysis of the level and nature of its CRE concentration risk. As of December 31, 2022, our bank's total CRE loans represented 262% of total capital.

Privacy

Financial institutions are required to disclose their policies for collecting and protecting non-public personal information of their clients. Clients generally may prevent financial institutions from sharing non-public personal information with nonaffiliated third parties except under certain circumstances, such as the processing of transactions requested by the consumer or when the financial institution is jointly offering a product or service with a nonaffiliated financial institution. Additionally, financial institutions generally are prohibited from disclosing consumer account numbers to any nonaffiliated third party for use in telemarketing, direct mail marketing or other marketing to consumers.

Consumer Credit Reporting

The Fair Credit Reporting Act ("FCRA") imposes, among other things:

- requirements for financial institutions to develop policies and procedures to identify potential identity theft and, upon the request of a consumer, to place a fraud alert in the consumer's credit file stating that the consumer may be the victim of identity theft or other fraud;
- requirements for entities that furnish information to consumer reporting agencies to implement procedures and policies regarding the accuracy and integrity of the furnished information and regarding the correction of previously furnished information that is later determined to be inaccurate;
- requirements for mortgage lenders to disclose credit scores to consumers in certain circumstances; and
- limitations on the ability of a business that receives consumer information from an affiliate to use that information for marketing purposes.

Anti-Terrorism and Money Laundering Legislation

Our bank is subject to the Bank Secrecy Act and USA Patriot Act. These statutes and related rules and regulations impose requirements and limitations on specified financial transactions and accounts and other relationships intended to guard against money laundering and terrorism financing. Our bank has established an anti-money laundering program pursuant to the Bank Secrecy Act and customer identification program pursuant to the USA Patriot Act. The bank also maintains records of cash purchases of negotiable instruments, files reports of certain cash transactions exceeding $10,000 (daily aggregate amount), and reports suspicious activity that might signify money laundering, tax evasion, or other criminal activities pursuant to the Bank Secrecy Act. Our bank otherwise has implemented policies and procedures to comply with the foregoing requirements.

Overdraft Fees

Federal Reserve Regulation E restricts banks' abilities to charge overdraft fees. The rule prohibits financial institutions from charging fees for paying overdrafts on ATM and one-time debit card transactions, unless a consumer consents, or opts in, to the overdraft service for those types of transactions.

The Dodd-Frank Act

As final rules and regulations implementing the Dodd-Frank Act have been adopted, this new law has significantly changed and is significantly changing the bank regulatory framework and affected the lending, deposit, investment, trading and operating activities of banks and their holding companies. The Dodd-Frank Act requires various federal agencies to adopt a broad range of new implementing rules and regulations and to prepare numerous studies and reports for Congress. The federal agencies are given significant discretion in drafting the implementing rules and regulations, and consequently, many of the details and much of the impact of the Dodd-Frank Act will depend on the rules and regulations that implement it.

A number of the effects of the Dodd-Frank Act are described or otherwise accounted for in various parts of this "Supervision and Regulation" section. The following items provide a brief description of certain other provisions of the Dodd-Frank Act that may be relevant to us and our bank.

- The Dodd-Frank Act created the CFPB with broad powers to supervise and enforce consumer financial protection laws. The CFPB has broad rule-making authority for a wide range of consumer protection laws that apply to all banks, including the authority to prohibit "unfair, deceptive or abusive" acts and practices. The CFPB has examination and enforcement authority with respect to enumerated consumer financial protection laws over all banks with more than $10 billion in assets. Institutions with less than $10 billion in assets will continue to be examined for compliance with consumer financial protection laws by their primary federal regulator.
- The Dodd-Frank Act imposed new requirements regarding the origination and servicing of residential mortgage loans. The law created a variety of new consumer protections, including limitations, subject to exceptions, on the manner by which loan originators may be compensated and an obligation on the part of lenders to verify a borrower's "ability to repay" a residential mortgage loan. Final rules implementing these latter statutory requirements became effective in 2014.
- The Dodd-Frank Act eliminated the federal prohibitions on paying interest on demand deposits effective one year after the date of its enactment, thus allowing businesses to have interest-bearing checking accounts. Depending on competitive responses, this significant change to existing law could have an adverse impact on our interest expense.
- The Dodd-Frank Act addresses many investor protection, corporate governance and executive compensation matters that will affect most U.S. publicly traded companies. The Dodd-Frank Act (i) requires publicly traded companies to give shareholders a non-binding vote on executive compensation and golden parachute payments; (ii) enhances independence requirements for compensation committee members; (iii) requires national securities exchanges to require listed companies to adopt incentive-based compensation clawback policies for executive officers; (iv) authorizes the SEC to promulgate rules that would allow shareholders to nominate their own candidates using a company's proxy materials; and (v) directs the federal banking regulators to issue rules prohibiting incentive compensation that encourages inappropriate risks.

The Volcker Rule

On December 10, 2013, five U.S. financial regulators, including the Federal Reserve, adopted a final rule implementing the "Volcker Rule." The Volcker Rule was created by Section 619 of the Dodd-Frank Act, which generally prohibits any "banking entity" from engaging in proprietary trading or retaining an ownership interest in, sponsoring, or having certain relationships with covered funds (i.e., hedge funds or private equity funds). In addition, the Volcker Rule requires each regulated entity to establish an internal compliance program that is consistent with the extent to which it engages in activities covered by the Volcker Rule.

On October 8, 2019, the agencies finalized revisions to the Volcker Rule that, among other things, simplified and streamlined compliance requirements for banking entities that do not have significant trading activities, while banking entities with significant trading activity would become subject to more stringent compliance requirements. Further, the revisions to the Volcker Rule implemented Section 203 of the Economic Growth, Regulatory Relief, and Consumer Protection Act (EGRRCPA), which amended the definition of "banking entity" to exclude certain community banks from the definition of insured depository institution, the general result of which was to exclude such banks and their affiliates and subsidiaries from the scope of the Volcker Rule. Under EGRRCPA, a community bank and its affiliates are generally excluded from the definition of "banking entity" if the bank and all companies that control the bank have total consolidated assets equal to $10 billion or less and trading assets and liabilities equal to five percent or less of total consolidated assets. These revisions became effective on January 1, 2020, with a required compliance date of January 1, 2021.

Limitations on Incentive Compensation

In April 2016, the Federal Reserve and other federal financial agencies re-proposed restrictions on incentive-based compensation pursuant to Section 956 of the Dodd-Frank Act for financial institutions with $1 billion or more in total consolidated assets. For institutions with at least $1 billion but less than $50 billion in total consolidated assets, such as the Company and our bank, the proposal imposes principles-based restrictions that are broadly consistent with existing interagency guidance on incentive-based compensation. Such institutions are prohibited from entering into incentive compensation arrangements that encourage inappropriate risks by the institution (1) by providing an executive officer, employee, director, or principal shareholder with excessive compensation, fees, or benefits, or (2) that could lead to material financial loss to the institution. The proposal also imposes certain governance and recordkeeping requirements on institutions of the Company's and our bank's size. The Federal Reserve reserves the authority to impose more stringent requirements on institutions of the Company's and our bank's size.

Cybersecurity

Cybersecurity is a high-priority item for legislators and regulators at the federal and state levels, as well as internationally. State and federal banking regulators have issued various policy statements and, in some cases, regulations, emphasizing the importance of technology risk management and supervision. Such policy statements and regulations indicate that financial institutions should design multiple layers of security controls to establish lines of defense and to ensure that their risk management processes also address the risk posed by compromised customer credentials, including security measures to reliably authenticate customers accessing internet-based services of the financial institution. A financial institution's management is expected to maintain sufficient business continuity planning processes to ensure the rapid recovery, resumption and maintenance of the institution's operations after a cyberattack involving destructive malware. A financial institution is expected to develop appropriate processes to enable recovery of data and business operations and address rebuilding network capabilities and restoring data if the institution or its critical service providers fall victim to this type of cyberattack. These requirements, including state regulatory rules such as the detailed and extensive cybersecurity rules issued in 2016 by the New York State Department of Financial Services, may cause us to incur significant additional compliance costs and in some cases may impact our growth prospects. Additionally, if we fail to observe federal or state regulatory guidance, we could be subject to various regulatory sanctions, including financial penalties.

The Company has an Information Technology (IT) Steering Committee comprised of internal managers representing various divisions of the Company. The Committee oversees IT strategic and investment priorities and the Company's Information Security Program. The Committee regularly reports to the Risk Committee of the Board through distribution of meeting minutes and other presentations and communication, including a comprehensive overview of the Company's cyber and information security program annually.

In the ordinary course of business, we rely on electronic communications and information systems to conduct our operations and store sensitive data. We employ an in-depth, layered, defensive approach that leverages people, processes and technology to manage and maintain cybersecurity controls. We also employ a variety of preventative and detective tools to monitor, block, and provide alerts regarding suspicious activity, as well as to report on any suspected advanced persistent threats. Notwithstanding the strength of our defensive measures, the threat from cyberattacks is severe, as attacks are sophisticated and increasing in volume and complexity, and attackers respond rapidly to changes in defensive measures. Our systems and those of our customers and third-party service providers are under constant threat, and it is possible that we or they could experience a significant event in the future that could adversely affect our business or operations. As cybersecurity threats continue to evolve, we may be required to expend significant additional resources to continue to modify or enhance our protective measures or to investigate and remediate any information security vulnerabilities. Financial expenditures may also be required to meet regulatory changes in the information security and cybersecurity domains. Risks and exposures related to cybersecurity attacks

are expected to remain high for the foreseeable future due to the rapidly evolving nature and sophistication of these threats, as well as the expanding use of internet banking, mobile banking and other technology-based products and services by us and our customers. See “Item 1A. – Risk Factors” in this Annual Report for a further discussion of risks related to cybersecurity.

Federal statutes and regulations, including the Gramm-Leach-Bliley Act (“GLBA”) and the Right to Financial Privacy Act of 1978, limit our ability to disclose non-public information about consumers, customers and employees to nonaffiliated third parties. Specifically, the GLBA requires us to disclose our privacy policies and practices relating to sharing non-public information and enables retail customers to opt out of our ability to share information with unaffiliated third parties under certain circumstances. The GLBA also requires us to implement a comprehensive information security program that includes administrative, technical and physical safeguards to ensure the security and confidentiality of customer records and information and, if applicable state law is more protective of customer privacy than the GLBA, financial institutions, including our bank, will be required to comply with such state law. Other laws and regulations impact our ability to share certain information with affiliates and non-affiliates for marketing and/or non-marketing purposes. These regulations affect how consumer information is transmitted through diversified financial companies and conveyed to outside vendors. In connection with the regulations governing the privacy of consumer financial information, the federal banking agencies, including the FDIC, have adopted guidelines for establishing information security standards and programs to protect such information.

Proposed or new legislation and regulations may also significantly increase our compliance cost and impede our ability to grow into specific markets. There are a number of proposals that have either recently been adopted or are currently pending before federal, state, and foreign legislative and regulatory bodies. For example, the European Union adopted the General Data Protection Regulation (the “GDPR”), which became effective on May 25, 2018. In addition, California passed the California Consumer Privacy Act of 2018 (the “CCPA”) on June 28, 2018. Both the GDPR and the CCPA impose additional obligations on companies regarding the handling of personal data and provide certain individual privacy rights to persons whose data is stored. In the event of a data breach, there are mandatory reporting requirements that may hamper the ability to fully assess an incident prior to external reporting. We must maintain awareness of additional legal and regulatory requirements that apply to existing and future subsets of the customer base for protection against legal, reputational, and financial risk due to compliance failures.

AVAILABLE INFORMATION

We file reports with the SEC including annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and proxy statements, as well as any amendments to those reports and statements. The SEC maintains an internet site that contains reports, proxy and information statements and other information regarding issuers that file electronically with the SEC at http://www.sec.gov. Our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, proxy statements and amendments to those reports and statements filed or furnished pursuant to section 13(a) or 15(d) of the Exchange Act are also accessible at no cost on our website at http://www.ir.capstarbank.com after they are electronically filed with the SEC. Reference to our website does not constitute incorporation by reference of the information contained on the website and should not be considered part of this Report.

We have also posted our Corporate Governance Guidelines, Code of Ethics and Conflicts of Interest Policy for directors, officers and employees, and the charters of our Audit Committee, Risk Committee, Nominating and Corporate Governance Committee, and Compensation and Human Resources Committee of our board of directors on the Corporate Governance section of our website at www.ir.capstarbank.com. We will make any legally required disclosures regarding amendments to, or waivers of, provisions of our Corporate Governance Guidelines, Code of Ethics and Conflicts of Interest Policy, or current committee charters on our website. We will also provide a copy of our Corporate Governance Guidelines, Code of Ethics and Conflicts of Interest Policy, and any committee charters without charge upon written request sent to 1201 Demonbreun Street, Suite 700, Nashville, Tennessee 37203, Attention: Investor Relations.

ITEM 1A. RISK FACTORS

This Item outlines specific risks that could affect the ability of our various businesses to compete, change our risk profile or materially affect our assets, business, cash flow, condition (financial or otherwise), liquidity, prospects and results of operations. Many of these risks are beyond our control, though efforts are made to manage those risks while optimizing financial and operational results, and our operating environment continues to evolve and new risks continue to emerge. This Item highlights risks that could affect us in material ways by causing future results to differ materially from past results, by causing future results to differ materially from current expectations, or by causing material changes in our financial condition. Some of these risks are interrelated and the occurrence of one or more of them may exacerbate the effect of others. You should carefully read and consider the following risks factors, together with the other information contained in or incorporated by reference into this Report before investing in shares of our common stock.

Risks Related To Our Business

Our business, financial condition, and results of operations may be adversely affected by global pandemics, including the COVID-19 pandemic and future variants.

The COVID-19 pandemic created extensive disruptions to the global economy and to the lives of individuals throughout the world. Business and consumer customers of the Company have experienced varying degrees of financial distress as a result of the unprecedented uncertainty, volatility and disruption in the financial markets and in governmental, commercial and consumer activity caused by the COVID-19 pandemic. Even as the COVID-19 pandemic subsides, it will likely take time for the U.S. economy to recover, and the length of the recovery period is unknown. The Company's business could be materially and adversely affected during any such recovery period. To the extent the effects of COVID-19 or other global pandemics adversely impact the Company's business and financial results, it might also have a heightening effect of the other risks described in this section.

As a business operating in the financial services industry, our business and operations may be adversely affected in numerous and complex ways by weak economic conditions.

Our business and operations, which primarily consist of lending money to clients in the form of loans, borrowing money from clients in the form of deposits and investing in securities, are sensitive to general business and economic conditions in the United States. If the U.S. economy weakens, our growth and profitability from our lending, deposit and investment operations could be constrained. Uncertainty about the federal fiscal policymaking process, the medium- and long-term fiscal outlook of the federal government, and future tax rates is a concern for businesses, consumers and investors in the United States. In addition, economic and other conditions in foreign countries could affect the stability of global financial markets, which could hinder United States economic growth.

Weak economic conditions may be characterized by numerous factors; such as deflation, fluctuations in debt and equity capital markets, a lack of liquidity and/or depressed prices in the secondary market for mortgage loans, increased delinquencies on mortgage, consumer and commercial loans, residential and commercial real estate price declines and lower home sales and commercial activity. All of these factors can individually or in the aggregate be detrimental to our business, and the interplay between these factors can be complex and unpredictable. Adverse economic conditions could have a material adverse effect on our assets, business, cash flow, condition (financial or otherwise), liquidity, prospects and results of operations.

Our business and operations are concentrated in our Target Market (References herein to our "Target Market" includes the state of Tennessee, Asheville, NC, and geographical areas within a 100-mile radius of any of our banking locations), and we are more sensitive than our more geographically diversified competitors to adverse changes in the local economy.

Unlike with many of our larger competitors that maintain significant operations located outside our market area, substantially all of our clients are individuals and businesses located and doing business in our Target Market. As of December 31, 2022, approximately 92% of the loans in our loan portfolio (measured by dollar amount) were made to borrowers who live or conduct business in our Target Market. Therefore, our success will depend in large part upon the general economic conditions in this area, which we cannot predict with certainty. As a result, our operations and profitability may be more adversely affected by a local economic downturn in our Target Market than those of larger, more geographically diverse competitors. From time to time, our bank may provide financing to clients who own or have companies or properties located outside our Target Market. In such cases, we would face similar local market risk in those communities for these clients.

Competition from financial institutions and other financial service providers may adversely affect our profitability.

The banking business is highly competitive, and we experience competition in our market from many other financial institutions. We compete with commercial banks, credit unions, savings and loan associations, mortgage banking firms, internet banks, consumer finance companies, securities brokerage firms, insurance companies, money market funds, and other mutual funds, as well as other community banks and super-regional and national financial institutions that operate offices in our service area. These competitors have differing levels of marketing resources, capital, regulatory requirements, and funding.

We compete with these other financial institutions both in attracting deposits, in making loans, and in hiring staff. Our profitability depends upon our continued ability to successfully compete with an array of financial institutions in our service area.

Our reputation is critical to our business, and damage to it could have a material adverse effect on us.

The Company faces threats to its reputation from many sources, including adverse sentiment about financial institutions generally, unethical practices, employee misconduct, failure to deliver expected standards of service or quality, regulatory compliance deficiencies, and questionable or fraudulent activities of the Company’s employees and customers. Negative publicity may arise regarding the Company’s business, employees, or customers, with or without merit, and could result in the loss of customers, investors and employees, costly litigation, a decline in revenue, and increased regulatory oversight.

Credit and Interest Rate Risks

The Company is subject to lending risk, and the impacts of interest rate changes could adversely impact the Company.

There are inherent risks associated with the Company’s lending activities. These risks include, among other things, the impact of changes in interest rates and changes in the economic conditions in the markets where the Company operates. Increases in interest rates and/or weakening economic conditions could adversely impact the ability of borrowers to repay outstanding loans or the value of the collateral securing these loans. The Company is also subject to various laws and regulations that affect its lending activities. Failure to comply with applicable laws and regulations could subject the Company to regulatory enforcement action that could result in restrictions of the Company's activities or the assessment of significant civil money penalties against the Company.

As of December 31, 2022, approximately 35% of our loan portfolio was composed of non-owner occupied commercial real estate loans, 11% of owner occupied commercial real estate loans, 17% consumer real estate loans, and 10% construction and land development loans. The Company's concentration of loans secured by real estate may subject the Company to additional risk, such as fluctuations in market value of collateral, environmental liability associated with hazardous or toxic substances found on, in or around the collateral, and difficulty monitoring income-producing property serving as a source of repayment and collateral. Additionally, non-owner occupied commercial real estate loans typically involve repayment dependent upon income generated, or expected to be generated, by the property securing the loan in amounts sufficient to cover operating expenses and debt service. Weak economic conditions or other market factors can result in increased vacancy rates for retail, office and industrial property. The adequacy of such income for repayment may be adversely affected by changes in the economy or local market conditions.

Additionally, we target small and medium sized businesses as loan clients. Because of their size, these borrowers may be less able to withstand competitive, economic or financial pressures than larger borrowers in periods of economic weakness. If loan losses occur at a level where the allowance for loan losses is not sufficient to cover actual loan losses, our earnings will decrease.

We may not be able to adequately assess and limit our credit risk, which could adversely affect our profitability.

A primary component of our business involves making loans to clients. The business of lending is inherently risky because the principal of or interest on the loan may not be repaid timely or at all or the value of any collateral supporting the loan may be insufficient to cover our outstanding exposure. These risks may be affected by the strength of the borrower’s business sector and local, regional and national market and economic conditions. Our risk management practices, such as monitoring our loan applicants and the concentration of our loans and our credit approval practices, may not adequately assess credit risk, and our credit administration personnel, policies and procedures may not adequately adapt to changes in economic or any other conditions affecting clients and the quality of the loan portfolio. A failure to effectively assess and limit the credit risk associated with our loan portfolio could

have a material adverse effect on our assets, business, cash flow, condition (financial or otherwise), liquidity, prospects and results of operations.

Our allowance for loan losses may prove to be insufficient to absorb losses inherent in our loan portfolio.

We maintain an allowance for loan losses that represents management's best estimate of the loan losses and risks inherent in our loan portfolio. The level of the allowance reflects management's continuing evaluation of concentrations, specific credit risks, loan loss experience, current loan portfolio quality, present economic, political and regulatory conditions and unidentified losses inherent in the current loan portfolio. The determination of the appropriate level of the allowance for loan losses is highly subjective and requires us to make significant estimates of current credit risks and future trends, all of which may undergo material changes in a relatively short time period. Inaccurate management assumptions, continuing deterioration of economic conditions affecting borrowers, new information regarding existing loans, identification of additional problem loans and other factors, both within and outside of our control, may require us to increase our allowance for loan losses. In addition, our regulators, as an integral part of their examination process, periodically review our loan portfolio and the adequacy of our allowance for loan losses and may require adjustments based upon judgments that are different than those of management. Further, if actual charge-offs in future periods exceed the amounts allocated to the allowance for loan losses, we may need to increase our provision for loan losses to restore the adequacy of our allowance for such losses. If we are required to materially increase our level of allowance for loan losses for any reason, our assets, business, cash flow, condition (financial or otherwise), liquidity, prospects and results of operations could be materially and adversely affected.

The value of real estate collateral may fluctuate significantly resulting in an under-collateralized loan portfolio.

The market value of real estate, particularly real estate held for investment, can fluctuate significantly in a short period of time as a result of market conditions in the geographic area in which the real estate is located. If the value of the real estate serving as collateral for the Company's loan portfolio were to decline materially, a significant part of the Company's loan portfolio could become under-collateralized. If the loans that are collateralized by real estate become troubled during a time when market conditions are declining or have declined, then, in the event of foreclosure, we may not be able to realize the amount of collateral that we anticipated at the time of originating the loan. This could have a material adverse effect on the Company's provision for credit losses and the Company's operating results and financial condition.

We engage in lending secured by real estate and may be forced to foreclose on the collateral and own the underlying real estate, subjecting us to the costs and potential risks associated with the ownership of the real property.

Since we originate loans secured by real estate, we may have to foreclose on the collateral property to protect our investment and may thereafter own and operate such property, in which case we would be exposed to the risks inherent in the ownership of real estate. The amount that we, as a mortgagee, may realize after a default is dependent upon factors outside of our control, including, but not limited to general or local economic conditions, environmental cleanup liability, neighborhood assessments, interest rates, real estate tax rates, operating expenses of the mortgaged properties, supply of and demand for rental units or properties, ability to obtain and maintain adequate occupancy of the properties, zoning laws, governmental and regulatory rules, fiscal policies, and natural disasters. Our inability to manage the amount of costs or size of the risks associated with the ownership of real estate, or write-downs in the value of other real estate owned, could have a material adverse effect on our assets, business, cash flow, condition (financial or otherwise), liquidity, prospects and results of operations.

We have several large depositor relationships, the loss of which could force us to fund our business through more expensive and less stable sources.

As of December 31, 2022, our ten largest non-brokered depositors accounted for approximately 11% of our total deposits. Withdrawals of deposits by any one of our largest depositors could force us to rely more heavily on borrowings and other sources of funding for our business and withdrawal demands, adversely affecting our net interest margin and results of operations.

Liquidity risk could impair our ability to fund operations and meet our obligations as they become due, and our funding sources may be insufficient to fund our future growth.

Liquidity is essential to our business. An inability to raise funds, at competitive rates or at all, through deposits, borrowings, the sale of loans and other sources could have a substantial negative effect on our liquidity. Approximately 74% of our bank's deposits as of December 31, 2022 were checking accounts and other liquid deposits, which are payable on demand or upon several days' notice, while by comparison, 74% of the assets of our bank were loans at

December 31, 2022, which cannot be called or sold in the same time frame. Our access to funding sources in amounts adequate to finance our activities or on terms that are acceptable to us could be impaired by factors that affect us specifically or the financial services industry or economy in general.

Factors that could negatively impact our access to liquidity sources include a decrease of our business activity as a result of a downturn in the markets in which our loans are concentrated, adverse regulatory action against us, or our inability to attract and retain deposits. Market conditions or other events could also negatively affect the level or cost of funding, affecting our ongoing ability to accommodate liability maturities and deposit withdrawals, meet contractual obligations and fund asset growth and new business transactions at a reasonable cost, in a timely manner and without adverse consequences.

Additionally, secondary market residential loans may require us to repurchase or substitute mortgage loans, or indemnify buyers against losses, in the event we breach representations or warranties to purchasers, guarantors and insurers, including government-sponsored entities, about the mortgage loans and the manner in which they were originated. In addition, we may be required to repurchase mortgage loans as a result of early payment default of the borrower on a mortgage loan. If repurchase and indemnity demands increase and such demands are valid claims and are in excess of our provision for potential losses, our liquidity, results of operations and financial condition may be adversely affected.

Any substantial, unexpected or prolonged change in the level or cost of liquidity could have a material adverse effect on our ability to meet deposit withdrawals and other client needs, which could have a material adverse effect on our asset growth, new business transactions, cash flow, condition (financial or otherwise), liquidity, prospects and results of operations.

Changes to interest rates could impact the financial outcomes of the Company.

Changes in monetary policy, including changes in interest rates, could influence not only the interest income the Company receives on loans and securities and the amount of interest it pays on deposits and borrowings, but such changes could also affect (i) the Company’s ability to originate loans and obtain deposits, (ii) the fair value of the Company’s financial assets and liabilities, and (iii) the average duration of the Company’s mortgage-backed securities portfolio. The Company’s earnings and cash flows are largely dependent upon its net interest income. Net interest income is the difference between interest income earned on interest-earning assets, such as loans and securities, and interest expense paid on interest-bearing liabilities, such as deposits and borrowed funds. Interest rates are highly sensitive to many factors that are beyond the Company’s control, including general economic conditions and policies of various governmental and regulatory agencies and, in particular, the Board of Governors of the Federal Reserve System. If the interest rates paid on deposits and other borrowings increase at a faster rate than the interest rates received on loans and other investments, the Company’s net interest income, and therefore its earnings and net profit, could be adversely affected. Earnings also could be adversely affected if the interest rates received on loans and other investments fall more quickly than the interest rates paid on deposits and other borrowings. Changes in interest rates may also negatively affect the ability of the Company's borrowers to repay their loans, particularly as interest rates rise and adjustable-rate loans become more expensive.

Although management believes it has implemented effective asset and liability management strategies, including the use of derivatives as hedging instruments, to reduce the potential effects of changes in interest rates on the Company’s results of operations, any substantial, unexpected, prolonged change in market interest rates could have a material adverse effect on the Company’s financial condition and results of operations. See the section Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operations – Market and Liquidity Risk Management – Interest Rate Simulation Sensitivity Analysis" located elsewhere in this report for further discussion related to the Company’s management of interest rate risk.

The fair value of our investment securities could fluctuate because of factors outside of our control, which could have a material adverse effect on us.

Factors beyond our control could significantly affect the fair value of our investment securities. These factors include, but are not limited to, rating agency actions in respect of the securities, defaults by the issuer or with respect to the underlying securities, changes in market interest rates and instability in the capital markets. Any of these factors, among others, could cause other-than-temporary impairments ("OTTI") and realized and/or unrealized losses in future periods and declines in earnings and/or other comprehensive income (loss), which could materially and adversely affect our assets, business, cash flow, condition (financial or otherwise), liquidity, prospects and results of operations. The process for determining whether impairment of a security is OTTI usually requires complex, subjective judgments about the future financial performance and liquidity of the issuer, any collateral underlying the security as well as the Company’s intent and ability to hold the security for a sufficient period of time to allow for any anticipated recovery in fair value in order to assess the probability of receiving all contractual principal and interest payments on the

security. Our failure to assess any impairments or losses with respect to our securities could have a material adverse effect on our assets, business, cash flow, condition (financial or otherwise), liquidity, prospects and results of operations.

Strategic Risks

Acquisition and other growth opportunities may present challenges.

Any future acquisitions may result in unforeseen difficulties, which could require significant time and attention from the Company's management that would otherwise be directed at developing its existing business and managing expenses. In addition, the Company could discover undisclosed liabilities resulting from any acquisitions for which it may become responsible. Further, the benefits that the Company anticipates from these acquisitions may not develop. We may experience difficulty integrating businesses acquired through mergers and acquisitions and may fail to realize the expected revenue increases, cost savings, increases in market presence, and other projected benefits from acquisition activity. Acquisitions utilizing the Company's common stock as consideration may dilute the value of the Company's common stock, which dilution may not be recouped or recovered for a significant amount of time after the acquisition, if ever.

Any merger or acquisition opportunity that we decide to pursue will ultimately be subject to regulatory approval and other closing conditions. We may expend significant time and resources pursing potential acquisitions that are never consummated due to lack of regulatory approval or other issues. Competition for acquisition candidates in the banking industry is intense. We may expend significant time and resources evaluating acquisition candidates and conducting due diligence that does not lead to an acquisition opportunity.

The Company may implement new lines of business, enter new market areas, or offer new products and services from time to time. There can be substantial risks and uncertainties associated with these efforts. The Company may invest significant time and resources in developing and marketing new lines of business, but the benefits that the Company anticipates from these activities may not develop as expected. External factors, such as compliance with regulations, competitive alternatives, and shifting market preferences may impact the Company's ability to successfully implement organic growth strategies. Failure to successfully manage these risks could have a material adverse effect on the Company's financial condition and results of operations.

Our continued pace of growth may require us to raise additional capital in the future to fund such growth, and the unavailability of additional capital on terms acceptable to us could adversely affect us or our growth.

We believe that we have sufficient capital to meet our capital needs for our immediate growth plans. However, we will continue to need capital to support our longer-term growth plans. If capital is not available on favorable terms when we need it, we may have to either issue common stock or other securities on less than desirable terms or reduce our rate of growth until market conditions become more favorable. Either of such events could have a material adverse effect on our assets, business, cash flow, condition (financial or otherwise), liquidity, prospects and results of operations.

Operational Risks

Deterioration in the fiscal position of the U.S. federal government and downgrades in the U.S. Department of the Treasury and federal agency securities could adversely affect us and our banking operations.

In addition to causing economic and financial market disruptions, any future downgrade, failure to raise the U.S. statutory debt limit, or deterioration in the fiscal outlook of the U.S. federal government, could, among other things, materially adversely affect the market value of the U.S. and other government and governmental agency securities that we hold, the availability of those securities as collateral for borrowing, and our ability to access capital markets on favorable terms. In particular, such events could increase interest rates and disrupt payment systems, money markets, and long-term or short-term fixed income markets, adversely affecting the cost and availability of funding, which could negatively affect our profitability. Also, the adverse consequences of any downgrade could extend to those to whom we extend credit and could adversely affect their ability to repay their loans. Any of these developments could have a material adverse effect on our assets, business, cash flow, condition (financial or otherwise), liquidity, prospects and results of operations.

We are subject to losses resulting from fraudulent and negligent acts on the part of loan applicants, our borrowers, other third parties, and our employees.

When we originate loans, we rely heavily upon information supplied by third parties, including the information contained in the loan application, property appraisal, title information and employment and income documentation. If any of this information is intentionally or negligently misrepresented and such misrepresentation is not detected prior to loan funding, the fair value of the loan may be significantly lower than expected. Whether a misrepresentation is made by the loan applicant, the borrower, another third party or one of our employees, we generally bear the risk of loss associated with the misrepresentation. The persons and entities involved in such a misrepresentation are often difficult to locate, and we are often unable to collect any monetary losses that we have suffered from them.

We may bear costs associated with the proliferation of computer theft and cyber-crime.

We necessarily collect, use and hold sensitive data concerning individuals and businesses with whom we have a banking relationship. Threats to data security, including unauthorized access and cyber-attacks, rapidly emerge and change, exposing us to additional costs for protection or remediation and competing time constraints to secure our data in accordance with client expectations and statutory and regulatory requirements. Although we actively invest in the security of our technological infrastructure, it is not feasible to defend against every risk posed by rapid technological development and the increasing sophistication of cyber criminals. Patching and other measures to protect existing systems and servers could be inadequate, especially on systems that are being retired. Controls employed by our information technology department and third-party vendors could prove inadequate. We could also experience a breach by intentional or negligent conduct on the part of our employees or other internal sources, software bugs or other technical malfunctions, or other causes. As a result of any of these threats, our client accounts may become vulnerable to account takeover schemes or cyber-fraud. Our systems and those of our third-party vendors may also become vulnerable to damage or disruption due to circumstances beyond our or their control, such as from network failures, viruses and malware, power anomalies or outages, natural disasters and catastrophic events.

A breach of our security or the security of our third-party vendors that results in unauthorized access to our data could expose us to a disruption or challenges relating to our daily operations as well as to data loss, litigation, damages, fines and penalties, client notification requirements, significant increases in compliance costs, and reputational damage, any of which could individually or in the aggregate have a material adverse effect on our assets, business, cash flow, condition (financial or otherwise), liquidity, prospects and results of operations.

Our risk management framework may not be effective in mitigating risks and/or losses to us.

Our risk management framework is comprised of various processes, systems and strategies and is designed to manage the types of risk to which we are subject, including, among others, credit, liquidity, capital, financial performance, asset/liability, operational, compliance and regulatory, Community Reinvestment Act, or CRA, strategic and reputational, information technology and legal. Our framework also includes financial or other modeling methodologies that involve management assumptions and judgment. Our risk management framework may not be effective under all circumstances, including if our management fails to follow our credit policies and procedures, and thus, it may not adequately mitigate any risk or loss to us. If our framework is not effective, we could suffer unexpected losses and our assets, business, cash flow, condition (financial or otherwise), liquidity, prospects and results of operations could be materially and adversely affected. We may also be subject to potentially adverse regulatory consequences.

We depend on our information technology and telecommunications systems, and any systems failures or interruptions could adversely affect our operations and financial condition.

We rely heavily on communications and information systems to conduct our business. Any failure or interruption in the operation of these systems could impair or prevent the effective operation of our client relationship management, general ledger, deposit, lending or other functions. While we have policies and procedures designed to prevent or limit the effect of a failure or interruption in the operation of our information systems, there can be no assurance that any such failures or interruptions will not occur or, if they do occur, that they will be adequately addressed. The occurrence of any failures or interruptions impacting our information systems could damage our reputation, result in a loss of clients, and expose us to additional regulatory scrutiny, civil litigation, and possible financial liability, any of which could have a material adverse effect on our financial condition and results of operations.

We are dependent upon outside third parties for the processing and handling of our records and data.

We rely on software developed by third-party vendors to process various transactions. In some cases, we have contracted with third parties to run their proprietary software on our behalf. These systems include, but are not limited to, general ledger, payroll, employee benefits, loan and deposit processing, and securities portfolio accounting. For example, one vendor provides our core banking system through a service bureau arrangement. While we perform a review of controls instituted by the applicable vendors over these programs in accordance with industry standards and perform our own testing of user controls, we rely on the continued maintenance of controls by these third-party vendors, including safeguards over the security of client data. We may incur a temporary disruption in our ability to conduct business or process transactions, or incur damage to our reputation, if the third-party vendor fails to adequately maintain internal controls or institute necessary changes to systems. We may need to switch third-party service providers from time-to-time, which could result in disruption to our business processes, damage to our reputation and a breach of our data security measures. Such a disruption or breach of security may have a material adverse effect on our business. In addition, we may not be able to obtain or continue to obtain licenses and technologies from these third parties on reasonable terms or at all.

We encounter technological change continually and have fewer resources than certain of our competitors to invest in technological improvements.

The financial services industry is undergoing rapid technological changes, with frequent introductions of new technology-driven products and services. In addition to serving clients better, the effective use of technology increases efficiency and enables financial institutions to reduce costs. Our success will depend in part on our ability to address our clients' needs by using technology to provide products and services that will satisfy client demands for convenience, as well as to create additional efficiencies in our operations. Certain of our competitors have substantially greater resources to invest in technological improvements than us, and in the future, we may not be able to implement new technology-driven products and services timely, effectively or at all or be successful in marketing these products and services to our clients. As these technologies are improved in the future, we may, in order to remain competitive, be required to make significant capital expenditures, which may increase our overall expenses and have a material adverse effect on our net income. There is also no guarantee that any such investment in these products and services will create additional efficiencies in our operations.

We may be adversely affected by the lack of soundness of other financial institutions.

Our ability to engage in routine funding transactions could be adversely affected by the actions and soundness of other financial institutions. Financial services companies are interrelated as a result of trading, clearing, counterparty, and other relationships. We have exposure to different industries and counterparties, and through transactions with counterparties in the financial services industry, including brokers and dealers, commercial banks, investment banks, and other institutional clients. Defaults by, or even rumors or questions about, one or more financial services companies, or the financial services industry generally, have led to market-wide liquidity problems in the past and could lead to losses or defaults by us or by other institutions in the future. These losses or defaults could have a material adverse effect on our assets, business, cash flow, condition (financial or otherwise), liquidity, prospects and results of operations.

By engaging in derivative transactions, we are exposed to additional credit and market risk.

We use interest rate swaps to help manage our interest rate risk from recorded financial assets and liabilities when they can be demonstrated to effectively hedge a designated asset or liability and the asset or liability exposes us to interest rate risk. Hedging interest rate risk is a complex process, requiring sophisticated models and routine monitoring, and is not a perfect science. As a result of interest rate fluctuations, hedged assets and liabilities will appreciate or depreciate in market value. The effect of this unrealized appreciation or depreciation will generally be offset by income or loss on the derivative instruments that are linked to the hedged assets and liabilities. We also have derivatives that result from a service we provide to certain qualifying clients approved through our credit process, and therefore, are not used to manage interest rate risk in our assets or liabilities. By engaging in derivative transactions, we are exposed to credit and market risk. If the counterparty fails to perform, credit risk exists to the extent of the uncollateralized fair value gain in the derivative. Market risk exists to the extent that interest rate changes cause the value of our derivatives to decline – though to the extent the derivatives are effective hedges, changes in the value of derivative derivatives could be largely offset by changes in the fair value of the hedged item. The existence of credit and market risk associated with our derivative instruments could adversely affect our net interest income and, therefore, could have a material adverse effect on our assets, business, cash flow, condition (financial or otherwise), liquidity, prospects and results of operations.

The Company's controls and procedures may fail or be circumvented.

Any failure or circumvention of the Company's controls and procedures or failure to comply with regulations related to controls and procedures could have a material adverse effect on the Company's business, results of operations and financial condition. Management regularly reviews and updates the Company's internal controls, disclosure controls and procedures, and corporate governance policies and procedures. Any system of controls, no matter how well designed and operated, is based in part on certain assumptions and can provide only reasonable, not absolute, assurances that the objectives of the system are met.

Changes in tax law and accounting standards could materially affect the Company's operations.

Changes in tax laws, or changes in the interpretation of existing tax laws, could materially adversely affect the Company's operations. Similarly, new accounting standards, changes to existing accounting standards, and changes to the methods of preparing financial statements could impact the Company's reported financial condition and results of operations. These factors are outside the Company's control and it is impossible to predict changes that may occur and the effect of such changes.

The adoption of the Current Expected Credit Loss ("CECL") model will result in a significant change in how we recognize credit losses and may materially adversely affect our financial condition or results of operations.

In June 2016, the Financial Accounting Standards Board issued Accounting Standards Update No. 2016-13, "Financial Instruments-Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments," which replaces the current "incurred loss" model for recognizing credit losses with an "expected loss" model referred to as the CECL model. Under the CECL model, we will be required to present certain financial assets carried at amortized cost, such as loans held for investment and held-to-maturity debt securities, at the net amount expected to be collected. The measurement of expected credit losses is to be based on information about past events, including historical experience, current conditions, and reasonable and supportable forecasts that affect the collectability of the reported amount. This measurement will take place at the time the financial asset is first added to the balance sheet and periodically thereafter. This differs significantly from the "incurred loss" model required under current generally accepted accounting principles, which delays recognition until it is probable a loss has been incurred. Accordingly, we expect that the adoption of the CECL model will materially affect how we determine our allowance for loan losses and could require

us to significantly increase our allowance. Moreover, the CECL model may create more volatility in the level of our allowance for loan losses. If we are required to materially increase our level of allowance for loan losses for any reason, such increase could adversely affect our business, financial condition and results of operations.

The Company is currently finalizing its assessment of the adoption and ongoing impact, along with testing and finalization of internal controls relative to the adoption of CECL. At this time, the Company expects its allowance for credit losses related to all financial assets will increase in 2023 to approximately $28.0 to $29.0 million upon adoption compared to its allowance for loan losses at December 31, 2022 of approximately $24.1 million. The Company will initially apply the impact of the new guidance through a cumulative-effect adjustment to retained earnings as of the beginning of the year of adoption, which, for the Company, is January 1, 2023. Future adjustments to credit loss expectations will be recorded through the income statement as charges or credits to earnings.

We may be adversely impacted by the transition from LIBOR as a reference rate.

The United Kingdom's Financial Conduct Authority and the administrator of LIBOR have announced that the publication of the most commonly used U.S. dollar London Interbank Offered Rate ("LIBOR") settings will cease to be published or cease to be representative after June 30, 2023. The publication of all other LIBOR settings ceased to be published as of December 31, 2021. The Company discontinued originating LIBOR-based loans effective December 31, 2021. As described in Note One of the Notes to the Consolidated Financial Statements, management has reviewed all contracts, identified those that will be affected, and will transition the LIBOR based loans to SOFR, or another index, by June 30, 2023. Nevertheless, the transition from LIBOR has resulted in and could continue to result in added costs and employee efforts and could present additional risk.

Small Business Administration lending and other government guaranteed lending is an important part of our business. Our government guaranteed lending programs are dependent upon the U.S. federal government, and we face specific risks associated with originating SBA and other government guaranteed loans.

Our SBA lending program is dependent upon the U.S. federal government. As an approved participant in the SBA Preferred Lender's Program (an "SBA Preferred Lender"), we enable our customers to obtain SBA loans without being subject to the potentially lengthy SBA approval process necessary for lenders that are not SBA Preferred Lenders. The SBA periodically reviews the lending operations of participating lenders to assess, among other things, whether the lender exhibits prudent risk management. When weaknesses are identified, the SBA may request corrective actions or impose enforcement actions, including revocation of the lender's SBA Preferred Lender status. If we lose our status as an SBA Preferred Lender, we may lose some or all of our customers to lenders who are SBA Preferred Lenders, and as a result we could experience a material adverse effect to our financial results. Any changes to the SBA program, changes to program-specific rules impacting volume eligibility under the guaranty program, as well as changes to the program amounts authorized by Congress, may also have a material adverse effect on our business. In addition, any default by the U.S. government on its obligations or any prolonged government shutdown could impede our ability to originate SBA loans or other government guaranteed loans or sell such loans in the secondary market, which could materially adversely affect our business, results of operations, and financial condition.

Generally, we sell the guaranteed portion of our SBA 7(a) loans in the secondary market. These sales result in premium income for us at the time of sale and create a stream of future servicing income, as we retain the servicing rights to these loans. For the reasons described above, we may not be able to continue originating these loans or sell them in the secondary market. Furthermore, even if we are able to continue to originate and sell SBA 7(a) loans in the secondary market, we might not continue to realize premiums upon the sale of the guaranteed portion of these loans, or the premiums may decline due to economic and competitive factors. When we originate SBA loans, we incur credit risk on the non-guaranteed portion of the loans, and if a customer defaults on a loan, we share any loss and recovery related to the loan pro-rata with the SBA. If the SBA establishes that a loss on an SBA guaranteed loan is attributable to significant technical deficiencies in the manner in which the loan was originated, funded, or serviced by us, the SBA may seek recovery of the principal loss related to the deficiency from us. Generally, we do not maintain reserves or loss allowances for such potential claims and any such claims could materially adversely affect our business, financial condition, or results of operations.

The laws, regulations and standard operating procedures that are applicable to government guaranteed loan products may change in the future. We cannot predict the effects of these changes on our business and profitability. Because government regulation greatly affects the business and financial results of all commercial banks and bank holding companies and especially our organization, changes in the laws, regulations and procedures applicable to government guaranteed loans could adversely affect our ability to operate profitably.

The recognition of gains on the sale of loans and servicing asset valuations reflect certain assumptions.

We continue to expect that gains on the sale of U.S. government guaranteed loans will continue to comprise a significant component of our revenue. The gain on such sales recognized for year ended December 31, 2022 was $2.5 million. The determination of these gains is based on assumptions regarding the value of unguaranteed loans retained, servicing rights retained and deferred fees and costs, and net premiums paid by purchasers of the guaranteed portions of U.S. government guaranteed loans. The value of retained unguaranteed loans and servicing rights are determined based on market-derived factors such as prepayment rates, current market conditions and recent loan sales. Deferred fees and costs are determined using internal analysis of the cost to originate loans. Significant errors in assumptions used to compute gains on sale of loans or servicing asset valuations could result in material revenue misstatements, which may have a material adverse effect on our business, results of operations and profitability. In addition, while we believe these valuations reflect fair value and such valuations are subject to validation by an independent third-party, if such valuations are not reflective of fair market value then our business, results of operations and financial condition may be materially and adversely affected.

Regulatory, Compliance, and Legal Risks

We operate in an extensively regulated industry.

The Company operates in a highly regulated environment and is subject to supervision and regulation by a number of governmental regulatory agencies, including the Federal Reserve Board, the OCC, the TDFI and the FDIC. Regulations adopted by these agencies, which are generally intended to provide protection for depositors and customers rather than for the benefit of shareholders, govern a comprehensive range of matters including but not limited to (i) ownership and control of the Company's equity, (ii) acquisition of other companies and businesses, (iii) permissible activities, (iv) maintenance of adequate capital levels and (v) other operational aspects. Compliance with banking regulations is costly and restricts certain of our activities, including the payment of dividends, mergers and acquisitions, investments, loan amounts and concentrations, interest rates, opening and closing branch locations, and other activities. The bank regulatory agencies also possess broad authority to prevent or remedy unsafe or unsound practices or violations of law. These agencies have significant discretion in their ability to enforce penalties and further limit the Company's activities if the Company fails to comply with applicable regulations.

The Dodd-Frank Act instituted major changes to the bank and financial institutions regulatory regimes, and additional changes continue to be proposed and implemented by various regulatory agencies. Other changes to statutes, regulations or regulatory policies, including changes in interpretation or implementation of statutes, regulations or policies, could affect the Company in substantial and unpredictable ways. Such changes could subject the Company to reduced revenues, additional costs, limit the types of financial services and products the Company may offer and/or increase the ability of non-banks to offer competing financial services and products, among other things. The burden and expenses associated with regulatory compliance have been increasing and may continue to increase. Failure to comply with laws, regulations or policies could result in sanctions by regulatory agencies, civil money penalties and/or reputation damage, which could have a material adverse effect on the Company's business, financial condition and results of operations. Proposals to change the laws and regulations governing financial institutions are frequently raised in Congress and before bank regulatory authorities. Changes in applicable laws or regulations could materially affect the Company’s business, and the likelihood of any major changes in the future and their effects are impossible to determine. Moreover, it is impossible to predict the ultimate form any proposed legislation might take or how it might affect the Company.

We are required to act as a source of financial and managerial strength for our bank in times of stress.

Under federal law and long-standing Federal Reserve policy, we are expected to act as a source of financial and managerial strength to our bank, and to commit resources to support our bank if necessary. We may be required to commit additional resources to our bank at times when we may not be in a financial position to provide such resources or when it may not be in our, or our shareholders’ or creditors,’ best interests to do so. A requirement to provide such support is more likely during times of financial stress for us and our bank, which may make any capital we are required to raise to provide such support more expensive than it might otherwise be. In addition, any capital loans we make to our bank are subordinate in right of repayment to deposit liabilities of our bank. In the event of our bankruptcy, any commitment by us to a federal banking regulator to maintain the capital of our bank will be assumed by the bankruptcy trustee and entitled to priority of payment over general unsecured creditor claims.

We are or may become involved from time to time in suits, legal proceedings, information-gathering requests, investigations and proceedings by governmental and self-regulatory agencies that may lead to adverse consequences.

Many aspects of our business involve substantial risk of legal liability. From time to time, we are, or may become, the subject of lawsuits and related legal proceedings, governmental and self-regulatory agency information-gathering requests, reviews, investigations and proceedings and other forms of regulatory inquiry, including by bank regulatory agencies, the Securities and Exchange Commission, or SEC, and law enforcement authorities. The results of such proceedings could lead to significant civil or criminal penalties, including monetary penalties, damages, adverse judgments, settlements, fines, injunctions, restrictions on the way in which we conduct our business, or reputational harm.

Although we establish accruals for legal proceedings when information related to the loss contingencies represented by those matters indicates both that a loss is probable and that the amount of loss can be reasonably estimated, we may not have accruals for all legal proceedings where we face a risk of loss. In addition, due to the inherent subjectivity of the assessments and unpredictability of the outcome of legal proceedings, amounts accrued may not represent the ultimate loss to us from the legal proceedings or government or other inquiries. Thus, our ultimate losses may be higher, and possibly materially so, than the amounts accrued for legal loss contingencies, which could adversely affect our financial condition and results of operations.

Risks Related to Our Common Stock

Even though our common stock is currently traded on the Nasdaq Stock Market's Global Select Market, it has less liquidity than many other stocks quoted on a national securities exchange.

The trading volume in our common stock on the Nasdaq Global Select Market has been relatively low when compared with larger companies listed on the Nasdaq Global Select Market or other stock exchanges. Because of this, it may be more difficult for shareholders to sell a substantial number of shares for the same price at which shareholders could sell a smaller number of shares.

We cannot predict the effect, if any, that future sales of our common stock in the market, or the availability of shares of common stock for sale in the market, will have on the market price of our common stock. We can give no assurance that sales of substantial amounts of common stock in the market, or the potential for large amounts of sales in the market, would not cause the price of our common stock to decline or impair our future ability to raise capital through sales of our common stock.

The market price of our common stock has fluctuated significantly, and may fluctuate in the future. These fluctuations may be unrelated to our performance. General market or industry price declines or overall market volatility in the future could adversely affect the price of our common stock, and the current market price may not be indicative of future market prices.

A future issuance or future issuances of stock could dilute the value of our common stock.

Our charter permits us to issue up to an aggregate of 25 million shares of common stock. As of December 31, 2022, 21,714,380 shares of our common stock were issued and outstanding, including 170,426 shares of restricted common stock that have yet to vest. Those shares outstanding do not include the potential issuance, as of December 31, 2022, of 124,445 shares of our common stock subject to issuance upon exercise of outstanding stock options under the Stock Incentive Plan, and 1,118,225 additional shares of our common stock that were reserved for issuance under the Stock Incentive Plan. A future issuance of any new shares of our common stock would, and equity-related securities could, cause further dilution in the value of our outstanding shares of common stock.

Significant sales of our common stock by certain shareholders could affect the market value of our common stock.

Certain shares owned by larger shareholders represent a significant number of our issued and outstanding shares of common stock, and, if sold in the market all at once or at about the same time, could depress the market price of our common stock and could further affect our ability to raise equity capital. Further, we cannot predict the size or the effect, if any, that sales of these shares, or the perception that such sales could occur, may have on the market price of our shares of common stock or our ability to raise additional capital through the sale of equity securities. Any significant sales of these shares could have a materially adverse impact on our affairs, assets, business, cash flows,

condition (financial or otherwise), credit quality, financial performance, liquidity, short- and long-term performance goals, prospects and results of operations or the trading price of our common stock.

We have the ability to incur debt and pledge our assets, including our stock in our bank, to secure that debt.

We have the ability to incur debt and pledge our assets to secure that debt. Absent special and unusual circumstances, a holder of indebtedness for borrowed money has rights that are superior to those of holders of our common stock. For example, interest must be paid to a lender before dividends can be paid to our shareholders, and, in the case of liquidation, our borrowings must be repaid before we can distribute any assets to our shareholders. Furthermore, we would have to make principal and interest payments on our indebtedness, which could reduce our profitability or result in net losses on a consolidated basis even if our bank were profitable.

The rights of our common shareholders would likely be subordinate to the rights of the holders of any preferred stock that we may issue in the future.

Our charter authorizes our board of directors to issue an aggregate of up to five million shares of preferred stock without any further action on the part of our shareholders. Our board of directors also has the power, without shareholder approval, to set the terms of any series of preferred stock that may be issued, including voting rights, dividend rights, and preferences over our common stock with respect to dividends or in the event of a dissolution, liquidation or winding up and other terms. Accordingly, you should assume that any shares of preferred stock that we may issue in the future will also be senior to our common stock. In the event that we issue preferred stock in the future that has preference over our common stock with respect to payment of dividends or upon our liquidation, dissolution or winding up, or if we issue preferred stock with voting rights that dilute the voting power of our common stock, the rights of the holders of our common stock or the market price of our common stock could be adversely affected.

We and our bank are subject to capital and other legal and regulatory requirements which restrict our ability to pay dividends.

We are subject to certain restrictions on the payment of cash dividends as a result of banking laws, regulations and policies. In addition, because our bank is our only material asset, our ability to pay dividends to our shareholders depends on our receipt of dividends from the bank, which is also subject to restrictions on dividends as a result of banking laws, regulations and policies.

General Risks

We are dependent on the services of our management team and board of directors, and the unexpected loss of key personnel or directors may adversely affect our business and operations.

We are led by an experienced core management team with substantial experience in the markets that we serve, and our operating strategy focuses on providing products and services through long-term relationship managers and ensuring that our largest clients have relationships with our senior management team. Accordingly, our success depends in large part on the performance of these key personnel, as well as on our ability to attract, motivate and retain highly qualified senior and middle management. Competition for employees is intense, and the process of locating key personnel with the combination of skills and attributes required to execute our business plan may be lengthy. If any of our executive officers, other key personnel, or directors leaves us or our bank, our operations may be adversely affected. Additionally, our directors' community involvement and diverse and extensive local business relationships are important to our success.

Severe weather, natural disasters, nuclear fallout, acts of war or terrorism, and other external events could significantly impact the Company's business.

Severe weather, natural disasters, nuclear fallout, health emergencies, acts of war or terrorism, and other adverse external events, especially those that directly affect the Company's market areas, could have a significant impact on the Company's ability to conduct business. These events could adversely affect the ability of borrowers to repay outstanding loans, decrease the value of collateral securing loans, cause significant property and infrastructure damage, and affect the stability of the Company's deposit base. The Company may experience decreased revenue, increased charge-offs, and other expenses.

Climate change and societal responses to climate change could adversely affect our business and results of operations, including indirectly through impact to our customers.

The current and anticipated effects of climate change are creating an increasing level of concern for the state of the global environment. As a result, political and social attention to the issue of climate change has increased. In recent years, governments across the world have entered into international agreements to attempt to reduce global temperatures, in part by limiting greenhouse gas emissions. The United States Congress, state legislatures and federal and state regulatory agencies have continued to propose and advance numerous legislative and regulatory initiatives seeking to mitigate the effects of climate change. These agreements and measures may result in the imposition of taxes and fees, the required purchase of emission credits and the implementation of significant operational changes, each of which may require businesses to expend significant capital and incur compliance, operating, maintenance and remediation costs. Consumers and businesses also may change their behavior on their own as a result of these concerns. It is not possible to predict how climate change may impact our financial condition and operations; however, we operate in areas where our business and the activities of our customers could be impacted by the effects of climate change. The effects of climate change may include increased frequency or severity of weather-related events, such as severe storms, hurricanes, flooding and droughts and rising sea levels. These effects can disrupt business operations, damage property, devalue assets and change customer and business preferences, which may adversely affect borrowers, increase credit risk and reduce demand for our products and services. The Company and our customers will need to respond to new laws and regulations as well as consumer and business preferences resulting from climate change concerns. As a result, the Company and our customers may face cost increases, asset value reductions, operating process changes and the like. The impact to our customers will likely vary depending on their specific attributes, including reliance on or role in carbon intensive activities. In addition, we could face reductions in creditworthiness on the part of some customers or in the value of assets securing loans.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

Our headquarters and main branch office are located at 1201 Demonbreun Street, Suites 700 and 103, respectively, Nashville, Tennessee 37203. The Company owns 12 banking locations and leases 11 banking locations, pursuant to operating leases.

ITEM 3. LEGAL PROCEEDINGS

We and our subsidiaries may be involved from time to time in various routine legal proceedings incidental to our respective businesses. Neither we nor any of our subsidiaries are currently engaged in any legal proceedings that are expected to have a material adverse effect on our results of operations or financial position.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

CapStar Financial's common stock is traded on the Nasdaq Global Select Market under the symbol "CSTR" and has traded on that market since September 22, 2016. Prior to that time, there was no established public trading market for our stock.

As of February 28, 2023, there were approximately 3,759 holders of record of shares of our common stock.

Dividend Policy

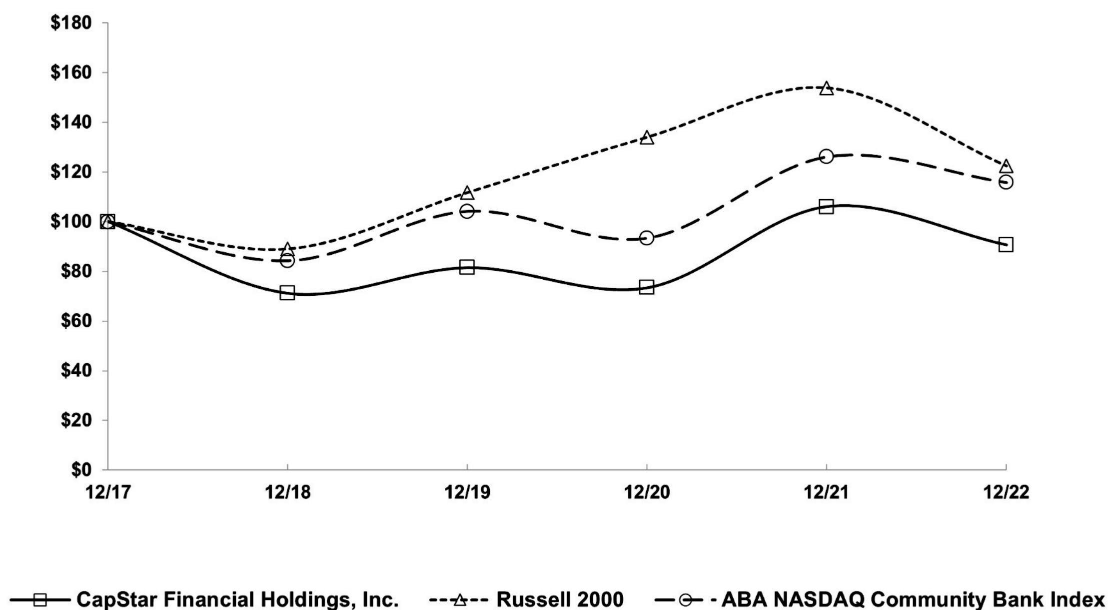
The Company generally pays dividends on a quarterly basis. As a Tennessee corporation and bank holding company, dividend payments are subject to numerous limitations. For additional information, see "Item 1. Business—Supervision and Regulation—Bank Regulation and Supervision—Payment of Dividends", "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations - Market and Liquidity Risk Management," and Note 16 of Notes to Consolidated Financial Statements.

Stock Performance Graph

The following stock performance graphs compare total shareholders' return (assuming reinvestment of dividends) on our common stock for the three year and five year periods ended December 31, 2022, as well as the Russell 2000 Index and ABA Nasdaq Community Bank Index for the same periods.

COMPARISON OF 5 YEAR CUMULATIVE TOTAL RETURN*

Among CapStar Financial Holdings, Inc., the Russell 2000 Index
and the ABA NASDAQ Community Bank Index Index



*$100 invested on 12/31/17 in stock or index, including reinvestment of dividends.
Fiscal year ending December 31.

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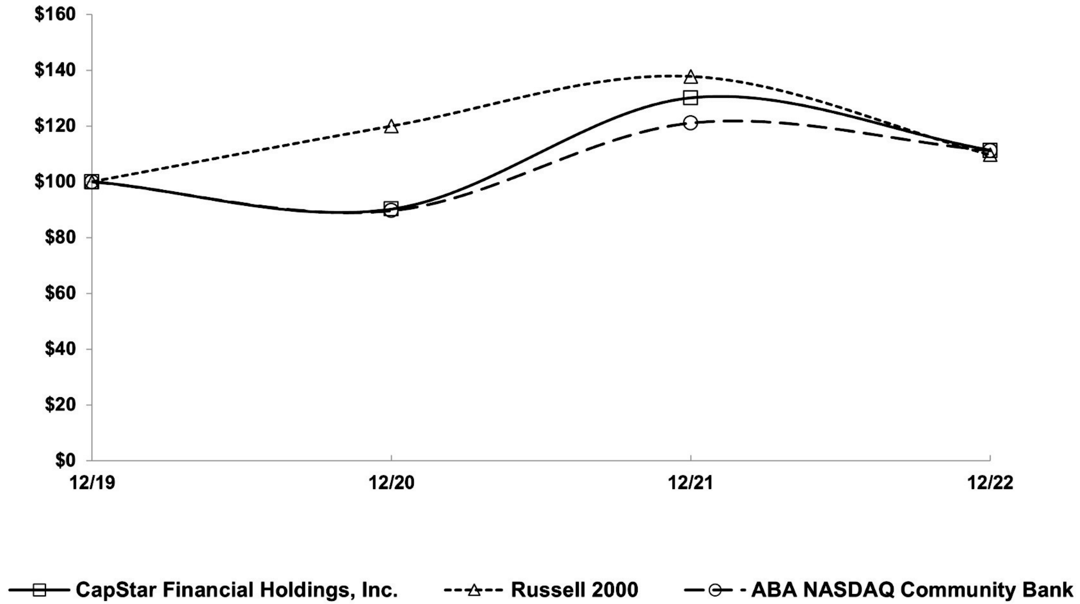
	12/31/2017	12/31/2018	12/31/2019	12/31/2020	12/31/2021	12/31/2022
CapStar Financial Holdings, Inc. (CSTR)	100	71	82	73	106	91
Russell 2000 (RUT)	100	89	112	134	154	122
ABA Nasdaq Community Bank Index (ABAQ)	100	84	104	93	126	116

COMPARISON OF 3 YEAR CUMULATIVE TOTAL RETURN*

Among CapStar Financial Holdings, Inc., the Russell 2000 Index
and the ABA NASDAQ Community Bank Index



*$100 invested on 12/31/19 in stock or index, including reinvestment of dividends.
Fiscal year ending December 31.

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	12/31/2019	12/31/2020	12/31/2021	12/31/2022
CapStar Financial Holdings, Inc. (CSTR)	100	90	130	111
Russell 2000 (RUT)	100	120	138	110
ABA Nasdaq Community Bank Index (ABAQ)	100	90	121	111

ITEM 6. [RESERVED]

ITEM 7. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following is a discussion of our financial condition and our results of operations as of and for the years ended December 31, 2022, 2021 and 2020. The purpose of this discussion is to focus on information about our financial condition and results of operations which is not otherwise apparent from the Consolidated Financial Statements appearing under the caption “Part II., Item 8—Financial Statements and Supplementary Data” in this Report. The following discussion and analysis should be read together with our Consolidated Financial Statements, the notes to our Consolidated Financial Statements and the other financial information included elsewhere in this Report. In addition to historical information, this discussion and analysis contains forward-looking statements that involve risks, uncertainties, estimates and assumptions that could cause actual results to differ materially from our current expectations. Factors that could cause such differences are discussed in the sections entitled “Risk Factors” and “Cautionary Note Regarding Forward-Looking Statements” appearing elsewhere in this Report. We assume no obligation to update any of these forward-looking statements except to the extent required by applicable law.

The following discussion and analysis pertains to our historical results on a consolidated basis. However, because we conduct all of our material business operations through our wholly-owned subsidiary, CapStar Bank, the following discussion and analysis relates to activities primarily conducted at the subsidiary level.

All dollar amounts in the tables in this section are in thousands of dollars, except per share data or when otherwise specifically noted. Unless specifically noted in this Report, all references in this section to the fiscal years 2020, 2021 and 2022 mean our fiscal years ended December 31, 2020, 2021, and 2022, respectively.

Critical Accounting Estimates

Our accounting and reporting policies are in accordance with GAAP and conform to general practices within the banking industry. Application of these policies requires management to make numerous estimates, assumptions or judgments that affect the amounts reported in the financial statements and the accompanying notes. These estimates are based on information available as of the date of the financial statements; accordingly, as this information changes, it could materially and adversely affect our reported results and financial position for the current period or future periods. The use of estimates, assumptions, and judgments are necessary when financial assets and liabilities are required to be recorded at, or adjusted to reflect, fair value. Assets carried at fair value inherently result in more financial statement volatility. Fair values and information used to record valuation adjustments for certain assets and liabilities are either based on quoted market prices or are provided by other independent third-party sources, when available. When such information is not available, management estimates valuation adjustments based upon historical experience and on various other assumptions that we believe to be reasonable under the circumstances. Management evaluates our estimates and assumptions on an ongoing basis. Changes in underlying factors, assumptions or estimates in any of these areas could have a material impact on our future financial condition and results of operations.

Our Consolidated Financial Statements are prepared based on the application of certain accounting policies, the most significant of which are described in Note 1 to our Consolidated Financial Statements for the year ended December 31, 2022, which are contained elsewhere in this Report. Certain policies inherently have a greater reliance on the use of estimates, assumptions or judgments and as such, have a greater possibility of producing results that could be materially different than originally reported. We have identified the following accounting policies and estimates that, due to the difficult, subjective or complex judgments and assumptions inherent in those policies and estimates and the potential sensitivity of our financial statements to those judgments and assumptions, are critical to an understanding of our financial condition and results of operations. We believe that the judgments, estimates and assumptions used in the preparation of our financial statements are reasonable and appropriate.

Allowance for Loan Losses

We record estimated probable inherent credit losses in the loan portfolio as an allowance for loan losses. The methodologies and assumptions for determining the adequacy of the overall allowance for loan losses involve significant judgments to be made by management. Some of the more critical judgments supporting our allowance for loan losses include judgments about the credit-worthiness of borrowers, estimated value of underlying collateral, assumptions about cash flow, determination of loss factors for estimating credit losses, and the impact of current events, conditions, and other factors impacting the level of inherent losses, including any remaining impact from the COVID-19 pandemic and its variants. Under different conditions or using different assumptions, the actual credit losses ultimately realized by us may be different from our estimates. On a quarterly basis, we assess the risk inherent in our loan portfolio based on qualitative and quantitative trends in the portfolio, including the internal risk

classification of loans, historical loss rates, changes in the nature and volume of the loan portfolio, industry or borrower concentrations, delinquency trends, detailed reviews of significant loans with identified weaknesses, and the impacts of local, regional, and national economic factors on the quality of the loan portfolio. Based on this analysis, we may record a provision for loan losses in order to maintain the allowance at appropriate levels. For a more complete discussion of the methodology employed to calculate the allowance for loan losses, see Note 1 to our Consolidated Financial Statements for the year ended December 31, 2022, which is included elsewhere in this Report.

Investment Securities Impairment

We assess on a quarterly basis whether there have been any events or economic circumstances to indicate that a security in an unrealized loss position is impaired on an other-than-temporary basis. In any instance, we would consider many factors, including the severity and duration of the impairment, our intent and ability to hold the security for a period of time sufficient for a recovery in value, recent events specific to the issuer or industry, and, for debt securities, external credit ratings and recent downgrades. Securities with respect to which there is an unrealized loss that is deemed to be other-than-temporary are written down to fair value with the write-down recorded in earnings.

Income Taxes

Deferred income tax assets and liabilities are computed using the asset and liability method, which recognizes a liability or asset representing the tax effects, based on current tax law, of future deductible or taxable amounts attributable to events recognized in the financial statements. A valuation allowance may be established to the extent necessary to reduce the deferred tax asset to a level at which it is “more likely than not” that the tax asset or benefit will be realized. Realization of tax benefits depends on having sufficient taxable income, available tax loss carrybacks or credits, the reversal of taxable temporary differences and/or tax planning strategies within the reversal period, and that current tax law allows for the realization of recorded tax benefits.

Business Combinations

Assets purchased and liabilities assumed in a business combination are recorded at their fair value. The fair value of a loan portfolio acquired in a business combination requires greater levels of management estimates and judgment than the remainder of purchased assets or assumed liabilities. When the loans have evidence of credit deterioration since origination and it is probable at the date of acquisition that the Company will not collect all contractually required principal and interest payments, the loans are considered impaired, and the expected cash flows in excess of the amount paid are recorded as interest income over the remaining life of the loan. The excess of the loan’s contractual principal and interest over expected cash flows is not recorded. We must estimate expected cash flows at each reporting date. Subsequent decreases to the expected cash flows will generally result in a provision for loan losses. Subsequent increases in cash flows result in a reversal of the provision for loan losses to the extent of prior charges and adjusted accretable yield which will have a positive impact on interest income. Purchased loans without evidence of credit deterioration are recorded at their initial fair value and adjusted as necessary for subsequent advances, pay downs, amortization or accretion of any premium or discount on purchase, charge-offs and additional provisions that may be required.

Results of Operations

The following is a summary of our results of operations:

	Year ended December 31, 2022	Year ended December 31, 2021	2022-2021 Percent Increase (Decrease)	Year ended December 31, 2020	2021-2020 Percent Increase (Decrease)
Interest income	$ 113,533	$ 98,459	*15.3%*	$ 91,852	*7.2%*
Interest expense	17,441	7,289	*139.3%*	15,529	*(53.1)%*
Net interest income	96,092	91,170	*5.4%*	76,323	*19.5%*
Provision for loan losses	2,474	(1,066)	*332.1%*	11,479	*(109.3)%*
Net interest income after provision for loan losses	93,618	92,236	*1.5%*	64,844	*42.2%*
Noninterest income	24,522	42,681	*(42.5)%*	43,248	*(1.3)%*
Noninterest expense	69,370	73,541	*(5.7)%*	77,361	*(4.9)%*
Net income before income taxes	48,770	61,376	*(20.5)%*	30,731	*99.7%*
Income tax expense	9,753	12,699	*(23.2)%*	6,035	*110.4%*
Net income	$ 39,017	$ 48,677	*(19.8)%*	$ 24,696	*97.1%*
Basic net income per share of common stock	$ 1.77	$ 2.20	*(19.5)%*	$ 1.22	*80.3%*
Diluted net income per share of common stock	$ 1.77	$ 2.19	*(19.2)%*	$ 1.22	*79.5%*

The following sections provide a more detailed analysis of significant factors affecting our operating results.

Net Interest Income

The largest component of our net income is net interest income – the difference between the interest income earned on loans, investment securities and other interest earning assets and interest expense on deposit accounts and other interest-bearing liabilities. Net interest income calculated on a tax-equivalent basis divided by total average interest-earning assets represents our net interest margin. The major factors that affect net interest income and net interest margin are changes in volumes, mix, the yield on interest-earning assets and the cost of interest-bearing liabilities. Our margin can also be affected by economic conditions, the competitive environment, loan demand and deposit flow. Our ability to respond to changes in these factors by using effective asset-liability management techniques is critical to maintaining the stability of the net interest margin and our net interest income.

The following table sets forth the average balances, interest income or interest expense for each category of interest-earning assets and interest-bearing liabilities and the average interest rate for interest-earning assets and interest-bearing liabilities, net interest spread and net interest margin for the years ended December 31, 2022, 2021 and 2020:

	For the Year Ended December 31,								
	2022			2021			2020		
	Average Outstanding Balance	Interest Income/ Expense	Average Yield/ Rate	Average Outstanding Balance	Interest Income/ Expense	Average Yield/ Rate	Average Outstanding Balance	Interest Income/ Expense	Average Yield/ Rate
Interest-Earning Assets									
Loans (1)	$ 2,176,073	$ 97,759	4.49%	$ 1,910,115	$ 84,368	4.42%	$ 1,690,179	$ 78,180	4.63%
Loans held for sale	84,171	3,742	4.45%	152,482	4,851	3.18%	175,311	6,092	3.47%
Securities:									
Taxable investment securities (2)	400,204	8,427	2.11%	441,495	7,213	1.63%	250,042	5,455	2.18%
Investment securities exempt from federal income tax (3)	55,310	1,267	2.90%	61,438	1,408	2.90%	49,474	1,326	3.39%
Total securities	455,514	9,694	2.20%	502,933	8,621	1.79%	299,516	6,781	2.38%
Cash balances in other banks	172,746	2,262	1.31%	317,406	598	0.19%	307,852	799	0.26%
Funds sold	7,546	76	1.01%	14,640	21	0.14%	18	—	2.77%
Total interest-earning assets	2,896,050	113,533	3.93%	2,897,576	98,459	3.41%	2,472,876	91,852	3.73%
Noninterest-earning assets	242,384			224,776			149,760		
Total assets	$ 3,138,434			$ 3,122,352			$ 2,622,636		
Interest-Bearing Liabilities									
Interest bearing deposits:									
Interest-bearing transaction accounts	$ 856,344	4,479	0.52%	$ 955,553	1,626	0.17%	$ 744,144	3,868	0.52%
Savings and money market deposits	689,825	5,102	0.74%	594,652	1,203	0.20%	549,533	5,196	0.95%
Time deposits	450,005	5,421	1.20%	417,770	2,873	0.69%	407,224	5,317	1.31%
Total interest-bearing deposits	1,996,174	15,002	0.75%	1,967,975	5,702	0.29%	1,700,901	14,381	0.85%
Borrowings and repurchase agreements	66,051	2,439	3.69%	30,574	1,587	5.19%	27,809	1,148	4.13%
Total interest-bearing liabilities	2,062,225	17,441	0.85%	1,998,549	7,289	0.36%	1,728,710	15,529	0.90%
Noninterest-bearing deposits	676,617			725,075			558,416		
Total funding sources	2,738,842			2,723,624			2,287,126		
Noninterest-bearing liabilities	36,339			34,969			29,762		
Shareholders' equity	363,253			363,759			305,748		
Total liabilities and shareholders' equity	$ 3,138,434			$ 3,122,352			$ 2,622,636		
Net interest spread (4)			3.09%			3.05%			2.83%
Net interest income/margin (5)		$ 96,092	3.33%		$ 91,170	3.16%		$ 76,323	3.10%

(1) Average loan balances include non-accrual loans. Interest income on loans includes amortization of deferred loan fees, net of deferred loan costs.

(2) Taxable investment securities include restricted equity securities.

(3) Yields on tax exempt securities are shown on a tax equivalent basis.

(4) Net interest spread is the average yield on total interest-earning assets minus the average rate on total interest-bearing liabilities.

(5) Net interest margin is net interest income calculated on a tax equivalent basis divided by total average interest-earning assets.

The following table reflects, for the periods indicated, the changes in our net interest income due to changes in the volume of interest-earning assets and interest-bearing liabilities and the associated rates earned or paid on these assets and liabilities.

	2022 Compared to 2021 Increase (decrease) due to			2021 Compared to 2020 Increase (decrease) due to		
	Volume	Rate	Net	Volume	Rate	Net
Interest-Earning Assets						
Loans	$ 11,747	$ 1,644	$ 13,391	$ 10,173	$ (3,985)	$ 6,188
Loans held for sale	(2,173)	1,064	(1,109)	(793)	(448)	(1,241)
Securities:						
Taxable investment securities	(675)	1,889	1,214	4,148	(2,390)	1,758
Investment securities exempt from federal income tax	(140)	(1)	(141)	379	(297)	82
Total securities	(815)	1,888	1,073	4,527	(2,687)	1,840
Cash balances in other banks	(273)	1,937	1,664	25	(226)	(201)
Funds Sold	(10)	65	55	405	(384)	21
Total interest-earning assets	8,476	6,598	15,074	14,337	(7,730)	6,607
Interest-Bearing Liabilities						
Interest-bearing transaction accounts	(169)	3,022	2,853	1,099	(3,341)	(2,242)
Savings and money market deposits	192	3,707	3,899	427	(4,420)	(3,993)
Time deposits	222	2,326	2,548	138	(2,582)	(2,444)
Borrowings and repurchase agreements	1,841	(989)	852	114	325	439
Total interest-bearing liabilities	2,086	8,066	10,152	1,778	(10,018)	(8,240)
Net Interest Income	$ 6,390	$ (1,468)	$ 4,922	$ 12,559	$ 2,288	$ 14,847

2022 compared to 2021

Our net interest income increased $4.9 million, or 5.4%, from 2021 to 2022 primarily due to a 13.9% increase in average loans held for investment partially offset by a 46 basis point increase in the average cost of interest-bearing deposits as market rates increased sharply throughout 2022 and customers shifted into higher cost deposit categories.

The $266.0 million increase in average loans held for investment is primarily attributable to the recent expansion into the Asheville, Chattanooga, and Knoxville markets, and the transfer of Tri-Net loans held for sale to loans held for investment offset by PPP loan forgiveness and paydowns. Our expansion into these new markets contributed $236.4 million to the increase in average loans while loans transferred from held for sale contributed $66.4 million to the increase. The transfer of Tri-Net loans held for sale to loans held for investment was due to the adverse impact of rapidly rising interest rates on pricing and investor demand. Average PPP loans decreased $123.7 million in 2022 when compared to 2021. PPP fees recognized as income totaled $0.7 million and $7.2 million for the years ended December 31, 2022 and 2021, respectively.

Net interest margin for the year ended December 31, 2022 also benefited from a 76 basis point or 80.0% increase in yields on average cash balances in other banks, federal funds sold, and investment securities which was offset by a decrease in their average balances of $199.2 million, or 23.9% as the Federal Reserve increased interest rates over the year ended December 31, 2022 compared to historically low levels experienced in the year ended December 31, 2021.

2021 compared to 2020

Our net interest income increased $14.8 million, or 19.5%, from 2020 to 2021 primarily due to a 13.0% increase in average loans held for investment and a 54 basis point or 60.0% decline in the average yield on interest-bearing liabilities as we worked to lower our cost of deposits across all categories.

The loan balance increase is primarily attributable to a combination of the FCB and BOW acquisitions and expansions into new markets. Fee income associated with PPP loan forgiveness and paydowns also contributed to net interest income. PPP fees recognized as income totaled $7.2 million and $3.6 million for the years ended December 31 2021 and 2020, respectively.

Net interest margin for the year ended December 31, 2021 also benefited from a 67.9% increase in average securities offset by a 59 basis point or 24.8% decrease in average security yield as yields on investments purchased were depressed by a sharp decline in market interest rates as the Federal Reserve lowered short-term rates to historically low levels in response to the pandemic.

Provision for Loan losses

Our policy is to maintain an allowance for loan losses at a level sufficient to absorb estimated probable losses inherent in the loan portfolio. The allowance is increased by a provision for loan losses, which is a charge to earnings, and is decreased by charge-offs and increased by loan recoveries. While our policies and procedures used to estimate the allowance for loan losses, as well as the resultant provision for loan losses charged to operations, are considered adequate by management, they are necessarily approximate and imprecise. There are factors beyond our control, such as conditions in the local and national economy, local real estate markets, or particular industry or borrower-specific conditions, which may materially and negatively impact our asset quality and the adequacy of our allowance for loan losses and, thus, the resulting provision for loan losses. Provision expense is impacted by macroeconomic factors, the absolute level of loans, loan growth, the credit quality of the loan portfolio and the amount of net charge-offs.

Our allowance for loan losses as a percentage of total loans held for investment was 1.03%, 1.10% and 1.23% at December 31, 2022, 2021 and 2020, respectively. Our allowance for loan losses plus fair value purchase accounting marks to non-PPP loans was 1.13%, 1.27%, and 1.58% at December 31, 2022, 2021 and 2020, respectively. See “Non-GAAP Financial Measures” for a discussion of and reconciliation to the most directly comparable U.S. GAAP measure.

2022 compared to 2021

The year ended December 31, 2022 yielded a $2.5 million provision compared to a ($1.1) million release of loan loss reserves in 2021. This increase was primarily attributable to an increase in loans during the year ended December 31, 2022 and other qualitative factors offset by a release of pandemic-related reserves.

Net charge-offs for 2022 were $0.4 million compared to $0.5 million for 2021, while our allowance for loan losses as a percentage of total loans held for investment decreased from 1.10% at December 31, 2021 to 1.03% at December 31, 2022. Similarly, these decreases were attributable to an increase in loan balances during the year ended December 31, 2022 and a release of pandemic-related reserves offset by an increase in other qualitative factors.

Based upon our evaluation of the loan portfolio, we believe the allowance for loan losses to be adequate to absorb our estimate of probable losses existing in the loan portfolio at December 31, 2022.

2021 compared to 2020

The year ended December 31, 2021 yielded a ($1.1) million release of loan loss reserves compared to a $11.5 million provision in 2020. This decrease was primarily attributable to improved asset quality trends, significant improvement in specific classified loans and improvement in COVID-19 qualitative factors within our allowance for loan losses methodology. While the pandemic and its variants are still considered within the Company's current allowance for loan losses, the release in 2021 is a reflection of credit quality metrics returning to pre-pandemic levels.

Net charge-offs for 2021 were $0.5 million compared to $0.9 million for 2020, while our allowance for loan losses as a percentage of total loans held for investment decreased from 1.23% at December 31, 2020 to 1.10% at December 31, 2021. Similarly, these decreases were attributable to improvements in economic conditions through December 31, 2021, as compared to the economic deterioration that occurred or was anticipated during 2020 as a result of COVID-19 and its variants.

Noninterest Income

In addition to net interest income, we generate recurring noninterest income. Our banking operations generate revenue from service charges on deposit accounts, interchange and debit card transaction fees, originating and selling mortgage, commercial real estate and SBA loans, wealth management and gains (losses) on sales of securities. In addition to these types of recurring noninterest income, we own insurance on several key employees and record income within "Other noninterest income" based upon the increase in the cash surrender value of these policies.

The following table sets forth the principal components of noninterest income for the periods indicated.

	Year Ended December 31, 2022	Year Ended December 31, 2021	2022-2021 Percent Increase (Decrease)	Year Ended December 31, 2020	2021-2020 Percent Increase (Decrease)
Noninterest income:					
Deposit service charges	$ 4,781	$ 4,515	*5.9%*	$ 3,494	*29.2%*
Interchange and debit card transaction fees	5,053	4,816	*4.9%*	3,172	*51.8%*
Mortgage banking	5,073	16,058	*(68.4)%*	25,034	*(35.9)%*
Tri-Net	78	8,613	*(99.1)%*	3,693	*133.2%*
Wealth management	1,687	1,850	*(8.8)%*	1,573	*17.6%*
SBA lending	2,501	2,060	*21.4%*	1,440	*43.1%*
Net gain on sale of securities	8	28	*(71.4)%*	125	*(77.6)%*
Bank owned life insurance	2,996	1,829	*63.8%*	887	*106.2%*
Other noninterest income	2,345	2,912	*(19.5)%*	3,830	*(24.0)%*
Total noninterest income	$ 24,522	$ 42,681	*(42.5)%*	$ 43,248	*(1.3)%*

2022 compared to 2021

A decrease in mortgage banking and Tri-Net income drove a decrease in total noninterest income of $18.2 million to $24.5 million, or 17.8% of total revenue, for the year ended December 31, 2022 compared to $42.7 million, or 30.3% of total revenue, for the year ended December 31, 2021.

Mortgage banking income consists of mortgage fee income from the origination and sale of mortgage loans. These mortgage fees are for loans originated in our markets that are subsequently sold to third-party investors. Generally, mortgage origination fees increase in lower interest rate environments and more robust housing markets and decrease in rising interest rate environments and more challenging housing markets. Mortgage origination fees will fluctuate from period to period as the rate environment changes. Mortgage banking income decreased 68.4% from 2021 to 2022 primarily due to the Federal Reserve rate increases over 2022, and corresponding increases in mortgage rates, resulting in fewer lending transactions.

Revenue for Tri-Net, a business launched in the fourth quarter of 2016, is derived from the origination and sale of commercial real estate loans to third-party investors. All such sales transfer servicing rights to the buyer. Income from Tri-Net sales decreased significantly compared to the prior year primarily due to the adverse impact of rapidly rising interest rates on pricing and investor demand. As a result of this impact, the Company transferred $105.5 million of Tri-Net loans from loans held for sale to loans held for investment. Tri-Net results include a $1.3 million realized loss on sale of loans and a $2.4 million unrealized loss on loans transferred to held for investment, partially offset by a $1.6 million gain on related hedge instruments. Similar to the Company's mortgage division, the Company anticipates continued near-term challenges in the Tri-Net division in a volatile rate environment. The Company paused any further commitments to originate such loans early in the third quarter, noting that originations would restart only when clear indications of market stabilization and liquidity normalization are observed. The Company announced plans to test a limited pool of Tri-Net originations in the 1st half of 2023.

SBA loan sales revenue also increased $0.4 million, or 21.4%, when compared to the prior year due to increased volumes and premiums as we continue to invest in and grow our government guaranteed lending division. As announced in the first quarter of 2023, we have hired a team of experienced SBA professionals to expand our SBA division and expect increased activity into 2023.

Income on bank owned life insurance increased $1.2 million, or 63.8%, in the year ended December 31, 2022 when compared to the year ended December 31, 2021 primarily due to the gain on death benefits.

Other noninterest income primarily consists of loan related fees and other service-related fees.

2021 compared to 2020

The increase in interchange and debit card transaction fees and other deposit service charges for 2021 were driven by the incremental increase in transaction volume related to our acquisitions of FCB and BOW, an emphasis on electronic banking and continued growth in deposits and volume of our commercial and consumer deposit account.

Mortgage banking income decreased 35.9% from 2020 to 2021. In 2020, we experienced an increase in mortgage lending transactions as a result of the sharp decline in mortgage interest rates at the start of the COVID-19 pandemic. However, volumes declined in 2021 as mortgage interest rates began to rise from 2020 levels.

Revenue for Tri-Net increased through continued growth and development as one the Company's key unique fee businesses.

SBA loan sales revenue also increased when compared to the prior year comparable period due to increased volumes and premiums as we continue to invest in and grow our government guaranteed lending division.

Noninterest Expense

The following table presents the primary components of noninterest expense for the periods indicated.

	Year Ended December 31,		2022-2021 Percent Increase (Decrease)	Year Ended December 31,	2021-2020 Percent Increase (Decrease)
	2022	**2021**		**2020**	
Noninterest expense:					
Salaries and employee benefits	$ 38,065	$ 41,758	*(8.8)%*	$ 45,252	*(7.7)%*
Data processing and software	11,152	11,248	*(0.9)%*	8,865	*26.9%*
Occupancy	4,299	4,205	*2.2%*	3,590	*17.1%*
Equipment	2,988	3,507	*(14.8)%*	3,195	*9.8%*
Professional services	2,175	2,155	*0.9%*	2,224	*(3.1)%*
Regulatory fees	1,080	1,031	*4.8%*	1,261	*(18.2)%*
Acquisition related expenses	—	323	*(100.0)%*	5,390	*(94.0)%*
Amortization of intangibles	1,690	1,939	*(12.8)%*	1,824	*6.3%*
Other noninterest expense	7,921	7,375	*7.4%*	5,760	*28.0%*
Total noninterest expense	$ 69,370	$ 73,541	*(5.7)%*	$ 77,361	*(4.9)%*

2022 compared to 2021

Total noninterest expense for 2022 decreased $4.2 million, or 5.7%, to $69.4 million compared to $73.5 million for 2021 primarily due to a decrease in salaries and employee benefits of $3.7 million, or 8.8%. While our base employee count stayed consistent at 397, our incentive compensation decreased in 2022 in relation to net income, Tri-Net activity, and mortgage banking activities. Additionally, in 2022, our executives elected to voluntarily forego their annual bonuses which totaled $0.9 million in an effort to establish a culture of operational excellence following two operational losses and losses in the Company's Tri-Net division.

Other noninterest expense in 2022 includes $1.5 million in operational losses for which the bank is seeking recovery.

Our efficiency ratio was 57.51% and 54.94% for 2022 and 2021, respectively. The efficiency ratio is the ratio of noninterest expense to the sum of net interest income and noninterest income and measures the amount of expense that is incurred to generate a dollar of revenue. When the efficiency ratio is adjusted for the Tri-Net losses, operational losses net of recoveries, and reversal of executive incentives the efficiency ratio for the year ended December 31, 2022 was 56.13%. See “Non-GAAP Financial Measures” for a discussion of and reconciliation to the most directly comparable U.S. GAAP measure.

2021 compared to 2020

Despite the impact of the FCB and BOW acquisitions, salaries and employee benefits expense decreased primarily due to lower incentive compensation as mortgage banking results declined compared to 2020, as well as a decrease in severance expense. At December 31, 2021, our associate base increased to 397 employees compared to 380 at December 31, 2020.

Data processing and software expense increased from 2020 to 2021 primarily due to an increase in the volume of transactions from organic growth, a full year of our FCB and BOW operations and services related to the processing of PPP loans.

Our acquisition-related expenses decreased $5.1 million from 2020 to 2021 following the 2020 FCB and BOW acquisitions, and thereby, lower integration-related expenses.

Our efficiency ratio was 54.94% and 67.40% for 2021 and 2020, respectively. The improvement in efficiency ratio for 2021 is primarily attributable to greater expense discipline in accordance with the Company's core strategy.

Income Taxes

2022 compared to 2021

We recorded income tax expense of $9.8 million and $12.7 million in 2022 and 2021, respectively. Our effective income tax rate for 2022 and 2021 was 20.0% and 20.7%, respectively. Our effective tax rate differs from the statutory tax rate due to our investments in qualified municipal securities, tax benefits from our real estate investment trust, company owned life insurance, state tax credits, net of the effect of certain non-deductible expenses and the recognition of excess tax benefits related to stock compensation. The lower effective tax rate in 2022 compared to 2021 is mainly the result of higher income on bank owned life insurance contracts and an increase in Tennessee state tax credits offset by fewer adjustments related to excess stock compensation expense.

2021 compared to 2020

We recorded income tax expense of $12.7 million and $6.0 million in 2021 and 2020, respectively. Our effective income tax rate for 2021 and 2020 was 20.7% and 19.6%, respectively. Our effective tax rate differs from the statutory tax rate due to our investments in qualified municipal securities, tax benefits from our real estate investment trust, company owned life insurance, state tax credits, net of the effect of certain non-deductible expenses and the recognition of excess tax benefits related to stock compensation. The higher effective tax rate in 2021 compared to 2020 is mainly the result of net operating loss carryback provisions associated with the CARES Act in 2020.

Financial Condition

2022 compared to 2021

Total assets decreased from $3,133.0 million at December 31, 2021 to $3,117.2 million at December 31, 2022. Loans held for investment grew from $1,965.8 million at December 31, 2021 to $2,312.8 million at December 31, 2022, a 17.7% increase. The increase was supported by organic loan growth as well as transfers of loans from held for sale. Loans held for sale decreased $39.0 million or 46.6%, during 2022 which is primarily related to the pausing of Tri-Net originations and declines in mortgage banking volumes. Cash and cash equivalents decreased $279.8 million or 67.4% as the Company deployed its excess liquidity experienced in 2021 to fund loan originations, the repurchase of common stock, and dividends in 2022.

Total liabilities increased from $2,753.0 million at December 31, 2021 to $2,763.0 million at December 31, 2022. Deposits decreased $4.5 million to $2,679.8 million at December 31, 2022 compared to $2,684.2 billion at December 31, 2021. While in the short-term the Company is experiencing a period of increased competition for deposits driven by high interest rates, a key longer-term strategic initiative is to create a stronger deposit-led culture with an emphasis on lower cost relationship-based deposits. As of December 31, 2022, the Company's lowest cost deposit category, noninterest bearing, decreased $213.1 million from December 31, 2021 to December 31, 2022, while higher cost time deposits increased $335.6 million or 90.0%. Other changes in deposits from 2021 to 2022 included a $194.7 million decrease or 20.6% in interest-bearing transaction deposits and a $67.7 million or 10.6% increase in savings and money market accounts.

2021 compared to 2020

Total assets increased $146.0 million or 4.9%, from December 31, 2020 to December 31, 2021. Loans held for investment grew from $1,883.7 million at December 31, 2020 to $1,965.8 million at December 31, 2021, a 4.4% increase. The increase was supported by organic loan growth partially offset by approximately $159.5 million in net paydowns of forgiven PPP loans. Loans held for sale decreased $103.3 million or 55.2%, during 2021 which is primarily related to the timing of selling residential and commercial real estate loans. Cash and cash equivalents increased $137.7 million or 49.6% as the Company continued to experience excess liquidity and grow deposits.

Total liabilities increased $109.4 million or 4.1% from December 31, 2020 to December 31, 2021. Deposits increased $116.3 million to $2.684 billion at December 31, 2021, a 4.5% increase. While in the short-term the Company is experiencing a period of excess liquidity, a key longer-term strategic initiative is to create a stronger deposit-led culture with an emphasis on lower cost relationship-based deposits. As of December 31, 2021, the Company's lowest cost deposit category, noninterest bearing, increased $62.2 million December 31, 2020 to December 31, 2021, while higher cost time deposits decreased $96.5 million or 20.5%. Other changes in deposits from 2020 to 2021 included a $100.5 million increase or 11.9% in interest-bearing transaction deposits and a $50.0 million or 8.5% increase in savings and money market accounts.

Investment Securities

The investment portfolio plays a key role in the management of liquidity and interest rate risk and provides another source of interest income. In managing the composition of the balance sheet, we seek a balance between earnings sources and credit and liquidity considerations. We manage our investment portfolio according to a written investment policy approved by our board of directors. Balances in our investment portfolio are subject to change over time based on our funding needs and interest rate risk management objectives. Our liquidity levels take into account anticipated future cash flows and all available sources of funds and are maintained at levels we believe are appropriate to assure future flexibility in meeting our anticipated funding needs.

Our investment portfolio consists primarily of securities issued by U.S. government-sponsored agencies, agency mortgage-backed securities, obligations of states and political subdivisions, asset-backed securities and other debt securities, all with varying contractual maturities. However, these maturities do not necessarily represent the expected life of the securities as some of these securities may be called or paid down without penalty prior to their stated maturities. The investment portfolio is regularly reviewed by the Asset Liability Management committee, or ALCO, of the bank to ensure an appropriate risk and return profile as well as for adherence to the investment policy.

Our investment portfolio totaled $397.7 million, $461.2 million, and $488.6 million at December 31, 2022, 2021 and 2020, respectively. Decreases in our investment portfolio over 2022 are related to the unrealized losses experienced in response to the rising rate environment. See "Note 3 to our Consolidated Financial Statements" for additional information on our investment securities.

The following table presents the fair value of our securities as of December 31, 2022 by their stated maturities (this maturity schedule excludes security prepayment and call features), as well as the weighted average yields for each maturity range.

	Due in one year or less		Due in one year to five years		Due in five years to ten years		Due after ten years	
	Fair Value	Weighted Average Yield	Fair Value	Weighted Average Yield	Fair Value	Weighted Average Yield	Fair Value	Weighted Average Yield
Securities available for sale:								
U. S. government agency securities	$ —	—	$ 1,888	2.2%	$ 11,014	2.1%	$ —	—
State and municipal securities	4,139	4.0%	20,694	3.3%	26,660	2.0%	16,819	2.4%
Mortgage-backed securities	57	4.1%	60,270	2.1%	147,494	1.4%	37,007	1.3%
Asset-backed securities	—	—	3,270	5.4%	—	—	—	—
Other debt securities	2,003	8.5%	5,036	4.8%	60,065	3.8%	—	—
Total securities available for sale	$ 6,199	5.5%	$ 91,158	2.7%	$ 245,233	2.1%	$ 53,826	1.7%
Securities held to maturity:								
State and municipal securities	$ 1,240	3.1%	$ —	—	$ —	—	$ —	—
Total securities held to maturity	$ 1,240	3.1%	$ —	—	$ —	—	$ —	—

Loans and Leases

Loans and leases are our largest category of earning assets and typically provide higher yields than other types of earning assets. Associated with the higher loan yields are the inherent credit and liquidity risks that we attempt to control and counterbalance.

The composition of gross loans and leases at December 31 for each of the past three years and the percentage of each classification to total loans are summarized as follows:

	December 31, 2022		December 31, 2021		December 31, 2020	
	Amount	Percent	Amount	Percent	Amount	Percent
Commercial real estate - owner occupied	$ 246,109	*10.6%*	$ 209,261	*10.6%*	$ 162,603	*8.6%*
Commercial real estate - non-owner occupied	803,611	*34.7%*	616,023	*31.3%*	481,229	*25.5%*
Consumer real estate	402,615	*17.4%*	326,412	*16.6%*	343,791	*18.3%*
Construction and land development	229,972	*9.9%*	214,310	*10.9%*	174,859	*9.3%*
Commercial and industrial	496,347	*21.5%*	497,615	*25.3%*	623,446	*33.1%*
Consumer	53,382	*2.3%*	46,811	*2.4%*	44,279	*2.4%*
Other	80,762	*3.5%*	55,337	*2.8%*	53,483	*2.8%*
Total gross loans held for investment	$ 2,312,798	*100.0%*	$ 1,965,769	*100.0%*	$ 1,883,690	*100.0%*

Over the past three years, we have continued to experience growth in our loan portfolio, especially in the commercial real estate loan classifications reflecting the development of the Target Market in which we operate along with our expansion into Chattanooga in 2021 and Asheville in 2022.

Our primary focus has been on commercial and industrial and commercial real estate lending, which constituted 67% of our loan portfolio as of December 31, 2022. Although we expect continued growth with respect to our loan portfolio, we do not expect any significant changes over the foreseeable future in our emphasis on commercial lending.

The repayment of loans is a source of additional liquidity for us. The following table details maturities and sensitivity to interest rate changes for our loan portfolio at December 31, 2022.

	December 31, 2022				
	Due in 1 year or less	**Due in 1-5 years**	**Due after 5-15 years**	**Due after 15 years**	**Total**
Commercial real estate	$ 98,699	$ 526,417	$ 395,590	$ 29,014	$ 1,049,720
Consumer real estate	15,837	93,867	214,429	78,482	402,615
Construction and land development	60,450	134,413	24,258	10,851	229,972
Commercial and industrial	150,788	198,933	122,687	23,939	496,347
Consumer	13,018	34,437	5,898	29	53,382
Other	17,775	29,666	32,677	644	80,762
Gross loans	$ 356,567	$ 1,017,733	$ 795,539	$ 142,959	$ 2,312,798
Interest rate sensitivity					
Fixed interest rates	114,963	750,096	500,589	12,308	1,377,956
Floating or adjustable interest rates	241,604	267,637	294,950	130,651	934,842
Total gross loans	$ 356,567	$ 1,017,733	$ 795,539	$ 142,959	$ 2,312,798

The information presented in the table above is based upon the contractual maturities of the individual loans, which may be renewed at their contractual maturity. Renewal of such loans is subject to review and credit approval, as well as modification of terms at their maturity. Consequently, we believe that this treatment presents fairly the maturity structure of the loan portfolio.

Asset Quality

One of our key objectives is to maintain a high level of asset quality in our loan portfolio. We utilize disciplined and thorough underwriting processes that collaboratively engage our seasoned and experienced business bankers and credit underwriters in the analysis of each loan request. Based upon our aggregate exposure to any given borrower relationship, we employ scaled review of loan originations that may involve senior credit officers, our Chief Credit Officer, our Chief Credit Policy Officer, our bank's Credit Committee or, ultimately, our full board of directors. In addition, we have adopted underwriting guidelines to be followed by our lending officers that require senior management review of proposed extensions of credit exceeding certain thresholds. When delinquencies exist, we monitor the levels of such delinquencies for any negative or adverse trends. Our loan review procedures include approval of lending policies and underwriting guidelines by the board of directors of our bank, an independent loan review, approval of larger credit relationships by our bank's Credit Committee and loan quality documentation procedures. Like other financial institutions, we are subject to the risk that our loan portfolio will be subject to increasing pressures from deteriorating borrower credit due to general economic conditions.

We target small and medium sized businesses, the owners and operators of such businesses and other consumers and high net worth individuals as loan clients. Because of their size, these borrowers may be less able to withstand competitive or economic pressures than larger borrowers in periods of economic weakness. If loan losses occur at a level where the allowance for loan losses is not sufficient to cover actual loan losses, our earnings will decrease. We use an independent consulting firm to review our loans for quality in addition to the reviews that may be conducted internally and by bank regulatory agencies as part of their examination process. Our bank has procedures and processes in place intended to assess whether losses exceed the potential amounts documented in our bank's impairment analyses and to reduce potential losses in the remaining performing loans within our loan portfolio. These procedures and processes include the following:

- we monitor the past due and overdraft reports on a weekly basis to identify deterioration as early as possible and the placement of identified loans on the watch list;
- we perform quarterly credit reviews for all watch list/classified loans, including formulation of action plans. When a workout is not achievable, we move to collection/foreclosure proceedings to obtain control of the underlying collateral as rapidly as possible to minimize the deterioration of collateral and/or the loss of its value;

- we require updated financial information, global inventory aging and interest carry analysis where appropriate for existing borrowers to help identify potential future loan payment problems; and
- we generally limit loans for new construction to established builders and developers that have an established record of turning their inventories, and we restrict our funding of undeveloped lots and land.

Our bank categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. Our bank analyzes loans individually by classifying each loan as to credit risk. This analysis includes all commercial loans and consumer relationships with an outstanding balance greater than $500,000, individually. This analysis is performed on a regular basis by the relationship managers and credit department personnel. On at least an annual basis an independent party performs a formal credit risk review of a sample of the loan portfolio. Among other things, this review assesses the appropriateness of the risk rating of each loan in the sample. See "Note 4 to our Consolidated Financial Statements" for a table that provides the risk category of loans by applicable class of loans.

Non-Performing Loans and Assets

Information summarizing non-performing assets, including non-accrual loans follows.

	December 31,		
	2022	2021	2020
Non-accrual loans	$ 10,714	$ 3,258	$ 4,817
Troubled debt restructurings	344	1,832	1,928
Loans past due greater than 90 days and still accruing	1,025	1,380	3,296
Non-performing loans	10,714	3,258	4,817
Foreclosed real estate	—	266	523
Non-performing assets	$ 10,714	$ 3,524	$ 5,340
Non-accrual loans as a percentage of total loans	0.46%	0.17%	0.25%
Non-performing assets as a percentage of total assets	0.34%	0.11%	0.18%
Allowance for loan losses to nonaccrual loans	222.20%	665.99%	482.56%

Non-accrual loans to total loans increased to 0.46% at December 31, 2022 compared to 0.17% at December 31, 2022. The increase in non-accrual loans is principally related to two relationships that total $8.4 million. These loans are made up of one loan totaling $3.4 million which has a 90% SBA guaranty of $3.0 million and a specific reserve of $0.3 million as well as a relationship of $5.0 million which is adequately secured with no loss expected.

We have established a policy to discontinue accruing interest on loans (that is, place the loans on non-accrual status) after they have become 90 days delinquent as to payment of principal or interest, unless the loans are considered to be well-collateralized and are in the process of collection. Consumer loans and any accrued interest are typically charged off no later than 180 days past due. In addition, a loan will not be placed on non-accrual status before it becomes 90 days delinquent unless management believes that the collection of all principal and interest is not expected in a timely manner. Interest previously accrued but uncollected on such loans is reversed and charged against interest income when the receivable is determined to be uncollectible. If we believe that a loan will not be collected in full, we will increase the allowance for loan losses to reflect management's estimate of any potential exposure or loss. Generally, payments received on non-accrual loans are applied directly to principal. As of December 31, 2022, there were not any loans, outside of those included in the table above, that cause management to have serious doubts as to the ability of borrowers to comply with present repayment terms.

Due to the weakening credit status of a borrower, we may elect to formally restructure certain loans to facilitate a repayment plan that seeks to minimize the potential losses, if any, that we might incur. The effect of these changes is assessed to determine if the loan should be classified as a Troubled Debt Restructure. Loans that have been restructured that are on non-accruing status as of the date of restructuring, are included in the nonperforming loan balances as discussed above and are classified as impaired loans. Loans that have been restructured that are on accrual status as of the restructure date are not included in nonperforming loans; however, such loans are still considered impaired.

Allowance for Loan Losses (allowance)

Our allowance for loan losses represents our estimate of probable inherent credit losses in the loan portfolio. We determine the allowance based on an ongoing evaluation of risk as it correlates to potential losses within the portfolio. Increases in the allowance are made by charges to the provision for loan losses. Loans deemed to be uncollectible are charged against the allowance. Recoveries of previously charged-off amounts are credited to our allowance. The judgments and estimates associated with our allowance determination are described under "Critical Accounting Policies and Estimates" above and in Notes 1 and 4 to the "Notes to Consolidated Financial Statements."

While no portion of our allowance is in any way restricted to any individual loan or group of loans and the entire allowance is available to absorb losses from any and all loans, the following tables represent management's allocation of our allowance to specific loan categories for the periods indicated.

	December 31, 2022		December 31, 2021		December 31, 2020	
	Amount	Percent	Amount	Percent	Amount	Percent
Commercial real estate	$ 7,934	*33.3%*	$ 7,124	*32.8%*	$ 7,349	*31.6%*
Consumer real estate	3,153	*13.2%*	2,412	*11.1%*	1,831	*7.9%*
Construction and land development	3,830	*16.1%*	3,769	*17.4%*	3,476	*15.0%*
Commercial and industrial	7,654	*32.2%*	7,441	*34.3%*	9,708	*41.8%*
Consumer	430	*1.8%*	397	*1.8%*	305	*1.3%*
Other	805	*3.4%*	555	*2.6%*	576	*2.5%*
Total allowance for loan and lease losses	$ 23,806	*100.0%*	$ 21,698	*100.0%*	$ 23,245	*100.0%*

	December 31, 2022			December 31, 2021			December 31, 2020		
	Net Charge-Offs (Recoveries)	Average Loans	Ratio	Net Charge-Offs (Recoveries)	Average Loans	Ratio	Net Charge-Offs (Recoveries)	Average Loans	Ratio
Commercial real estate	$ 213	$ 978,074	*0.02%*	$ —	$ 727,102	*0.00%*	$ 10	$ 597,175	*0.00%*
Consumer real estate	(2)	358,201	*(0.00)%*	17	331,274	*0.01%*	(35)	296,610	*(0.01)%*
Construction and land development	—	208,385	*0.00%*	—	196,098	*0.00%*	—	150,038	*0.00%*
Commercial and industrial	(172)	501,132	*(0.03)%*	(189)	552,561	*(0.03)%*	(493)	555,024	*(0.09)%*
Consumer	(220)	50,945	*(0.43)%*	(123)	45,263	*(0.27)%*	(96)	35,630	*(0.27)%*
Other	(185)	79,336	*(0.23)%*	(186)	57,817	*(0.32)%*	(224)	55,702	*(0.40)%*
Total allowance for loan and lease losses	$ (366)	$2,176,073	*(0.02)%*	$ (481)	$1,910,115	*(0.03)%*	$ (838)	$1,690,179	*(0.05)%*

Changes in the allocation of the allowance from year to year in various categories are influenced by the level of net charge-offs in respective categories and other factors including, but not limited to, an evaluation of the impact of current economic conditions and trends, risk allocations tied to specific loans or groups of loans and changes in qualitative allocations. Management believes that allocations for each loan category are reasonable and reflective of risk inherent in the portfolio.

Deposits

Client deposits are the primary funding source for our loan growth. The following table presents the average balance and average rate paid on deposits for each of the following categories for the periods indicated.

	Year ended December 31,					
	2022		2021		2020	
	Average Balance	Average Rate Paid	Average Balance	Average Rate Paid	Average Balance	Average Rate Paid
Types of Deposits:						
Noninterest-bearing demand deposits	$ 676,617	0.00%	$ 725,075	0.00%	$ 558,416	0.00%
Interest-bearing transaction accounts	856,344	0.52%	955,553	0.17%	744,144	0.52%
Money market accounts	524,661	0.93%	451,947	0.23%	463,183	1.10%
Savings accounts	165,164	0.13%	142,705	0.11%	86,350	0.11%
Time deposits	450,005	1.20%	417,770	0.69%	407,224	1.31%
Total deposits	$ 2,672,791	0.56%	$ 2,693,050	0.21%	$ 2,259,317	0.64%

Total average deposits remained relatively stable in 2022 compared to 2021 and increased 19.2% in 2021 compared to 2020. Increased pricing pressure during the year ended December 31, 2022 resulted in a shift to higher cost deposit

categories during the year but the Company continues to focus on building and expanding client relationships to deliver on our core deposit-led strategy.

The maturities of time deposits that exceed the FDIC insurance limit of $250 thousand at December 31, 2022 are as follows ($ in thousands):

	December 31, 2022				
	Three months or less	Over three through six months	Over six through twelve months	Over twelve months	Total
Time deposits in excess of FDIC insurance limit	$ 181,317	$ 102,306	$ 85,864	$ 10,401	$ 379,888

Capital Adequacy

As of December 31, 2022, CapStar Financial's capital ratios were as follows.

	Well Capitalized Guidelines	December 31, 2022
Total risk-based capital	10.00%	14.51%
Tier 1 risk-based capital	8.00%	12.61%
Common equity tier 1 capital	6.50%	12.61%
Tier 1 leverage	5.00%	11.40%

See Note 16 to the "Notes to Consolidated Financial Statements" for additional information related to our capital position.

Market and Liquidity Risk Management

Our objective is to manage assets and liabilities to provide a satisfactory, consistent level of profitability within the framework of our established liquidity, loan, investment, borrowing, and capital policies. Our ALCO is charged with the responsibility of monitoring these policies, which are designed to ensure an acceptable composition of asset/liability mix. Two critical areas of focus for ALCO are interest rate sensitivity and liquidity risk management.

Interest Rate Simulation Sensitivity Analysis

Managing interest rate risk is fundamental for the financial services industry. By considering both on and off-balance sheet financial instruments, management evaluates interest rate sensitivity while attempting to optimize net interest income within the constraints of prudent capital adequacy, liquidity needs, market opportunities and customer requirements.

We use earnings at risk, or EAR, simulations to assess the impact of changing rates on earnings under a variety of scenarios and time horizons. The simulation model is designed to reflect the dynamics of interest earning assets, interest bearing liabilities and off-balance sheet financial instruments. These simulations utilize both instantaneous and parallel changes in the level of interest rates, as well as gradual and non-parallel changes such as changing slopes and twists of the yield curve. Static simulation models are based on current exposures and assume a constant balance sheet with no growth. By estimating the effects of interest rate increases and decreases, the model can reveal approximate interest rate risk exposure. The simulation model is used by management to gauge approximate results given a specific change in interest rates at a given point in time. The model is therefore a tool to indicate earnings trends in given interest rate scenarios and does not indicate actual expected results.

At December 31, 2022, our net interest income over the next year is estimated to be fairly neutral at a 100 basis point market rate increase while being adversely impacted by falling interest rates or by larger rate increases. Many assumptions are used to calculate the impact of interest rate fluctuations on our net interest income, such as asset prepayments, non-maturity deposit price sensitivity, and key rate drivers. Because of the inherent use of these estimates and assumptions in the model, our actual results may, and most likely will, differ from our static EAR results. In addition, static EAR results do not include actions that our management may undertake to manage the risks in response to anticipated changes in interest rates or client behavior. For example, as part of our asset/liability management strategy, management has the ability to increase asset duration and/or decrease liability duration in order to reduce asset sensitivity, or to decrease asset duration and/or increase liability duration in order to increase asset sensitivity.

The following table illustrates our model's estimates of net interest income changes over the next 12 months in response to market interest rate changes.

	Net interest income change
Increase 200bp	(1.3)%
Increase 100bp	0.1
Decrease 100bp	(2.7)
Decrease 200bp	(6.6)

Liquidity Risk Management

Liquidity risk is the risk that we will be unable to meet our obligations as they become due because of an inability to liquidate assets or obtain adequate funding. Management has established a comprehensive management process for identifying, measuring, monitoring and controlling liquidity risk. Because of its critical importance to the viability of the Bank, liquidity risk management is fully integrated into our risk management processes. Critical elements of our liquidity risk management include: effective corporate governance consisting of oversight by the board of directors and active involvement by management; appropriate strategies, policies, procedures, and limits used to manage and mitigate liquidity risk; comprehensive liquidity risk measurement and monitoring systems (including assessments of the current and prospective cash flows or sources and uses of funds) that are commensurate with the complexity and business activities of the Bank; active management of intraday liquidity and collateral; an appropriately diverse mix of existing and potential future funding sources; adequate levels of highly liquid marketable securities free of legal, regulatory, or operational impediments, that can be used to meet liquidity needs in stressful situations; comprehensive contingency funding plans that sufficiently address potential adverse liquidity events and emergency cash flow requirements; and internal controls and internal audit processes sufficient to determine the adequacy of the institution’s liquidity risk management process.

The role of liquidity management is to ensure funds are available to meet depositors’ withdrawal and borrowers’ credit demands while at the same time optimizing financial results within our corporate guidelines. This is accomplished by balancing changes in demand for funds with changes in the supply of those funds. Liquidity is provided by short-term liquid assets that can be converted to cash, investment securities available-for-sale, various lines of credit available to us, and the ability to attract funds from external sources, principally deposits.

Our most liquid assets are comprised of cash and due from banks, available-for-sale marketable investment securities and federal funds sold. The fair value of the available-for-sale investment portfolio was $396.4 million at December 31, 2022. We pledge portions of our investment securities portfolio to secure public fund deposits, derivative positions and Federal Home Loan Bank (“FHLB”) advances. At December 31, 2022, total investment securities pledged for these purposes comprised 55% of the estimated fair value of the entire investment portfolio, leaving $180.4 million of unpledged securities.

We have a large base of non-maturity customer deposits, defined as demand, savings, and money market deposit accounts. At December 31, 2022, such deposits totaled $2.0 billion and represented 74% of our total deposits.

Other sources of funds available to meet daily needs include FHLB advances. As a member of the FHLB of Cincinnati, the Company has access to credit products offered by the FHLB. At December 31, 2022, available credit from the FHLB totaled $509.4 million. Additionally, we had available credit from the Federal Reserve of $322.6 million and available federal funds purchased lines with correspondent banks totaling $145.0 million at December 31, 2022.

The principal source of cash for CapStar Financial is dividends paid to it as the sole shareholder of the Bank. At December 31, 2022, the Bank was able to pay up to $89.9 million in dividends to CapStar Financial without regulatory approval subject to the ongoing capital requirements of the Bank.

Accordingly, management believes that our funding sources are at sufficient levels to satisfy our short-term and long-term liquidity needs.

Contractual Obligations

The following provides an overview of the Company's significant contractual obligations as of December 31, 2022.

Short-term borrowings and long-term debt - The Company issued $30.0 million of fixed-to-floating rate subordinated notes during the third quarter of 2020, which were recorded net of issuance costs of $0.6 million, that mature June 30, 2030. Beginning on or after June 30, 2025, the Company may redeem the notes, in whole or in part, at their principal amount plus any accrued and unpaid interest. The carrying value of subordinated notes was $29.7 million at December 31, 2022. The Company had FHLB advances of $15.0 million which matured in January of 2023.

Operating Lease Obligations - We are party to operating lease agreements for many of our branch locations, ATMs, loan production offices and operation centers. For qualifying leases with a term exceeding one year we record a lease liability and right-of-use ("ROU") asset on our balance sheet. As of December 31, 2022, the lease liability and ROU asset totaled $11.0 million and $10.1 million, respectively.

As of December 31, 2022 the remaining terms of our leases ranged from one to 9 years. Certain of our leases contain options to renew the lease at the end of the current term. Unless we have determined we are reasonably likely to renew the lease, these options have been excluded from the calculation of our lease liability and ROU asset. Additional information regarding operating leases is provided in Note 7 to the consolidated financial statements.

Off-Balance Sheet Arrangements

In the normal course of business, we enter into various transactions that, in accordance with GAAP, are not included in our consolidated balance sheets. We enter into these transactions to meet the financing needs of our clients. These transactions include commitments to extend credit and standby letters of credit, which involve, to varying degrees, elements of credit risk and interest rate risk in excess of the amounts recognized in our consolidated balance sheets. Most of these commitments mature within two years and are expected to expire without being drawn upon. Standby letters of credit as well as commitments to extend credit are included in the determination of the amount of risk-based capital that the Company and the Bank are required to hold.

We enter into contractual loan commitments to extend credit, normally with fixed expiration dates or termination clauses, at specified rates and for specific purposes. Substantially all of our commitments to extend credit are contingent upon clients maintaining specific credit standards until the time of loan funding.

Standby letters of credit are written conditional commitments issued by us to guarantee the performance of a client to a third party. In the event that the client does not perform in accordance with the terms of the agreement with the third party, we would be required to fund the commitment. The maximum potential amount of future payments we could be required to make is represented by the contractual amount of the commitment. If the commitment is funded, we would be entitled to seek recovery from the client. Our policies generally require that standby letter of credit arrangements contain security and debt covenants similar to those contained in loan agreements.

We minimize our exposure to loss under loan commitments and standby letters of credit by subjecting them to the same credit approval and monitoring procedures as we do for on-balance sheet instruments. We assess the credit risk associated with certain commitments to extend credit and establish a liability for probable credit losses. The effect on our revenue, expenses, cash flows and liquidity of the unused portions of these commitments cannot be reasonably predicted because there is no guarantee that the lines of credit will be used.

Our off-balance sheet arrangements are summarized in the following table for the periods indicated.

	Contract or notional amount		
	December 31, 2022	**December 31, 2021**	**December 31, 2020**
Financial instruments whose contract amounts represent credit risk:			
Unused commitments to extend credit	$ 1,112,950	$ 831,075	$ 804,520
Standby letters of credit	7,288	10,623	10,403
Total	$ 1,120,238	$ 841,698	$ 814,923

Non-GAAP Financial Measures

This Report includes the following financial measures that have been prepared other than in accordance with generally accepted accounting principles in the United States ("non-GAAP financial measures"): tangible common equity, tangible book value per share of common stock, tangible book value per share of common stock plus after-tax unrealized available for sale investment (gains) losses, tangible common equity to tangible assets, tangible common equity to tangible assets plus after-tax unrealized available for sale investment (gains) losses, the allowance for loan losses plus fair value purchase accounting marks to non-PPP loans, and the efficiency ratio excluding Tri-Net losses, operational losses, and executive incentive reversal. The Company believes that these non-GAAP financial measures (i) provide useful information to management and investors that is supplementary to its financial condition, results of operations and cash flows computed in accordance with GAAP, (ii) enable a more complete understanding of factors and trends affecting the Company's business, and (iii) allow investors to evaluate the Company's performance in a manner similar to management, the financial services industry, bank stock analysts and bank regulators; however, the Company acknowledges that its non-GAAP financial measures have a number of limitations. As such, you should not view these disclosures as a substitute for results determined in accordance with GAAP, and they are not necessarily comparable to non-GAAP financial measures that other companies use.

The following table presents a reconciliation of these measures to the most directly comparable GAAP financial measures.

	December 31, 2022	December 31, 2021	December 31, 2020
Tangible Equity:			
Total shareholders' equity	$ 354,182	$ 380,094	$ 343,486
Less: intangible assets	(46,069)	(47,759)	(49,698)
Tangible equity	$ 308,113	$ 332,335	$ 293,788
Tangible book value per share of common stock:			
Tangible equity	$ 308,113	$ 332,335	$ 293,788
Total shares of stock outstanding	21,714,380	22,166,129	21,988,803
Tangible book value per share of common stock	$ 14.19	$ 14.99	$ 13.36
Tangible book value per share of common stock plus after-tax unrealized available for sale investment losses:			
Total shareholders' equity	$ 354,182	$ 380,094	$ 343,486
Less: intangible assets	(46,069)	(47,759)	(49,698)
Add: after-tax unrealized available for sale investment (gains) losses	51,760	2,978	(6,020)
Tangible equity plus after-tax unrealized available for sale investment (gains) losses	$ 359,873	$ 335,313	$ 287,768
Total shares of common stock outstanding	21,714,380	22,166,129	21,988,803
Tangible book value per share of common stock plus after-tax unrealized available for sale investment losses	$ 16.57	$ 15.13	$ 13.09
Tangible common equity to tangible assets:			
Tangible equity	$ 308,113	$ 332,335	$ 293,788
Assets	$ 3,117,169	$ 3,133,046	$ 2,987,006
Less: intangible assets	(46,069)	(47,759)	(49,698)
Tangible assets	$ 3,071,100	$ 3,085,287	$ 2,937,308
Tangible common equity to tangible assets	10.03%	10.77%	10.00%
Tangible common equity to tangible assets plus after-tax unrealized available for sale investment losses:			
Tangible equity plus after-tax unrealized available for sale investment losses	$ 359,873	$ 335,313	$ 287,768
Tangible assets	$ 3,071,100	$ 3,085,287	$ 2,937,308
Add: after-tax unrealized available for sale investment losses	51,760	2,978	(6,020)
Tangible assets plus after-tax unrealized available for sale investment losses	$ 3,122,860	$ 3,088,265	$ 2,931,288
Tangible common equity to tangible assets plus after-tax unrealized available for sale investment losses	11.52%	10.86%	9.82%

The following table presents a reconciliation of allowance for loan losses plus fair value purchase accounting marks to non-PPP loans for the most directly comparable GAAP financial measures.

	December 31, 2022	December 31, 2021	December 31, 2020
Allowance for loan losses	$ 23,806	$ 21,698	$ 23,245
Purchase accounting marks	2,438	3,003	3,663
Allowance for loan losses and purchase accounting fair value marks	26,244	24,701	26,908
Loans held for investment	2,312,798	1,965,769	1,883,690
Less: PPP Loans net of deferred fees	221	26,539	181,601
Non-PPP Loans	2,312,577	1,939,230	1,702,089
Allowance for loan losses plus fair value marks / Non-PPP Loans	1.13%	1.27%	1.58%

The following table presents a reconciliation of the efficiency ratio adjusted for 2022 Tri-Net and operational losses for the most directly comparable GAAP financial measures.

	December 31, 2022	December 31, 2021	December 31, 2020
Net interest income	$ 96,092	$ 91,170	$ 76,323
Noninterest income	24,522	42,681	43,248
Less: Tri-Net losses	2,059	—	—
Noninterest income excluding Tri-Net losses	26,581	42,681	43,248
Total income excluding Tri-Net losses	122,673	133,851	119,571
Noninterest expense	69,370	73,541	77,361
Less: Operational losses	(1,463)	—	—
Less: Executive incentive reversal	947	—	—
Noninterest expense excluding operational losses and incentive reversal	68,854	73,541	77,361
Efficiency ratio excluding Tri-Net losses, operational losses, and executive incentive reversal	56.13%	54.94%	64.70%

Impact of Inflation

The consolidated financial statements and related consolidated financial data presented herein have been prepared in accordance with U.S. GAAP and practices within the banking industry which require the measurement of financial position and operating results in terms of historical dollars without considering the changes in the relative purchasing power of money over time due to inflation. Unlike most industrial companies, virtually all the assets and liabilities of a financial institution are monetary in nature. As a result, interest rates have a more significant impact on a financial institution's performance than the effects of general levels of inflation.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Information required by this item is included in Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operations – Market and Liquidity Risk Management – Interest Rate Simulation Sensitivity Analysis” and is incorporated herein by reference.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

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Report of Independent Registered Public Accounting Firm

To the Shareholders and the Board of Directors of CapStar Financial Holdings, Inc.:

Opinion on the Financial Statements

We have audited the accompanying consolidated balance sheets of CapStar Financial Holdings, Inc. and its subsidiary (the "Company") as of December 31, 2022 and 2021 and the related consolidated statements of income, comprehensive income, changes in shareholders' equity and cash flows for each of the three years in the period ended December 31, 2022, and the related notes to the consolidated financial statements (collectively, the financial statements). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2022 and 2021, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2022, in conformity with accounting principles generally accepted in the United States of America.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the Company's internal control over financial reporting as of December 31, 2022, based on criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission in 2013, and our report dated March 3, 2023 expressed an unqualified opinion on the effectiveness of the Company's internal control over financial reporting.

Basis for Opinion

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

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

Critical Audit Matters

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

Allowance for Loan Losses

As described in Note 4 to the Company's financial statements, the Company has a gross loan portfolio of approximately $2.31 billion and related allowance for loan losses of approximately $23.8 million as of December 31, 2022. As described by the Company in Note 1, the evaluation of the allowance for loan losses is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available. The allowance for loan losses is evaluated on a regular basis and is based upon the Company's review of the collectability of the loans in light of peer group historical loss experience, the nature and volume of the loan portfolio, information about specific borrower situations and estimated collateral values, economic conditions, and other factors.

We identified the Company's estimate of the allowance for loan losses as a critical audit matter. The principal considerations for our determination of the allowance for loan losses as a critical audit matter related to the high degree of subjectivity in the Company's judgments in determining the qualitative factors. Auditing these complex judgments and assumptions by the Company involves especially challenging auditor judgment due to the nature and extent of audit evidence and effort required to address these matters, including the extent of specialized skill or knowledge needed.

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

- We tested the design and operating effectiveness of controls relating to the Company's determination of the allowance for loan losses, including controls over the qualitative factors.
- We evaluated the relevance and the reasonableness of assumptions related to evaluation of the loan portfolio, current economic conditions, and other risk factors used in development of the qualitative factors for collectively evaluated loans.
- We validated the completeness and accuracy of the underlying data used to develop the factors.
- We validated the mathematical accuracy of the calculation.
- We evaluated the reasonableness of assumptions and data used by the Company in developing the qualitative factors by comparing these data points to internally developed and third-party sources, as well as other audit evidence gathered.
- Analytical procedures were performed to evaluate the directional consistency of changes that occurred in the allowance for loan losses for loans collectively evaluated for impairment.

We have served as the Company's auditor since 2017.

/s/ Elliott Davis, LLC

Franklin, Tennessee
March 3, 2023

Report of Independent Registered Public Accounting Firm

To the Shareholders and Board of Directors of CapStar Financial Holdings, Inc.:

Opinion on the Internal Control Over Financial Reporting

We have audited CapStar Financial Holdings, Inc. and Subsidiary's (the "Company") internal control over financial reporting as of December 31, 2022, based on criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission in 2013.In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2022, based on criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission in 2013.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the consolidated balance sheets of the Company as of December 31, 2022 and 2021 and the related consolidated statements of income, comprehensive income, changes in shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2022 of the Company and our report dated March 3, 2023 expressed an unqualified opinion.

Basis for Opinion

The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting in the accompanying Management's Annual Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audit in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

Definition and Limitations of Internal Control Over Financial Reporting

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ Elliott Davis, LLC

Franklin, Tennessee
March 3, 2023

CAPSTAR FINANCIAL HOLDINGS INC. & SUBSIDIARY
Consolidated Balance Sheets
(Dollars in thousands, except share and per share data)

	December 31, 2022	December 31, 2021
Assets		
Cash and due from banks	$ 25,280	$ 48,202
Interest-bearing deposits in financial institutions	105,558	347,023
Federal funds sold	4,467	19,900
Total cash and cash equivalents	135,305	415,125
Securities available-for-sale, at fair value	396,416	459,396
Securities held-to-maturity, fair value of $1,240 and $1,830 at December 31, 2022 and 2021, respectively	1,240	1,782
Loans held for sale (includes $12,636 and $37,306 measured at fair value at December 31, 2022 and 2021, respectively)	44,708	83,715
Loans held for investment	2,312,798	1,965,769
Less allowance for loan losses	(23,806)	(21,698)
Loans, net	2,288,992	1,944,071
Premises and equipment, net	24,855	25,727
Restricted equity securities	16,632	14,453
Accrued interest receivable	10,511	7,376
Goodwill	41,068	41,068
Core deposit intangible, net	5,001	6,691
Other real estate owned, net	—	266
Other assets	152,441	133,376
Total assets	$ 3,117,169	$ 3,133,046
Liabilities and Shareholders' Equity		
Deposits:		
Noninterest-bearing	$ 512,076	$ 725,171
Interest-bearing	749,857	944,605
Savings and money market accounts	709,190	641,456
Time	708,696	373,049
Total deposits	2,679,819	2,684,281
Federal Home Loan Bank advances	15,000	—
Subordinated debt	29,666	29,532
Other liabilities	38,502	39,139
Total liabilities	2,762,987	2,752,952
Shareholders' equity:		
Common stock, voting, $1 par value; 25,000,000 shares authorized; 21,714,380 and 22,166,129 shares issued and outstanding at December 31, 2022 and 2021, respectively	21,714	22,166
Additional paid-in capital	240,863	248,709
Retained earnings	141,657	110,489
Accumulated other comprehensive loss, net of income tax	(50,052)	(1,270)
Total shareholders' equity	354,182	380,094
Total liabilities and shareholders' equity	$ 3,117,169	$ 3,133,046

See accompanying notes to consolidated financial statements.

CAPSTAR FINANCIAL HOLDINGS INC. & SUBSIDIARY
Consolidated Statements of Income
(Dollars in thousands, except share and per share data)

	Year Ended December 31,		
	2022	2021	2020
Interest income:			
Loans, including fees	$ 101,501	$ 89,219	$ 84,272
Securities:			
Taxable	7,642	6,573	4,863
Tax-exempt	1,268	1,408	1,342
Federal funds sold	76	21	—
Restricted equity securities	784	640	576
Interest-bearing deposits in financial institutions	2,262	598	799
Total interest income	113,533	98,459	91,852
Interest expense:			
Interest-bearing deposits	4,479	1,626	3,868
Savings and money market accounts	5,102	1,203	5,196
Time deposits	5,421	2,873	5,317
Federal funds purchased	2	—	—
Federal Home Loan Bank advances	862	12	356
Subordinated notes	1,575	1,575	792
Total interest expense	17,441	7,289	15,529
Net interest income	96,092	91,170	76,323
Provision for loan losses	2,474	(1,066)	11,479
Net interest income after provision for loan losses	93,618	92,236	64,844
Noninterest income:			
Deposit service charges	4,781	4,515	3,494
Interchange and debit card transaction fees	5,053	4,816	3,172
Mortgage banking	5,073	16,058	25,034
Tri-Net	78	8,613	3,693
Wealth management	1,687	1,850	1,573
SBA lending	2,501	2,060	1,440
Net gain on sale of securities	8	28	125
Bank owned life insurance	2,996	1,829	887
Other noninterest income	2,345	2,912	3,830
Total noninterest income	24,522	42,681	43,248
Noninterest expense:			
Salaries and employee benefits	38,065	41,758	45,252
Data processing and software	11,152	11,248	8,865
Occupancy	4,299	4,205	3,590
Equipment	2,988	3,507	3,195
Professional services	2,175	2,155	2,224
Regulatory fees	1,080	1,031	1,261
Acquisition related expenses	—	323	5,390
Amortization of intangibles	1,690	1,939	1,824
Other noninterest expense	7,921	7,375	5,760
Total noninterest expense	69,370	73,541	77,361
Income before income taxes	48,770	61,376	30,731
Income tax expense	9,753	12,699	6,035
Net income	$ 39,017	$ 48,677	$ 24,696
Per share information:			
Basic net income per share of common stock	$ 1.77	$ 2.20	$ 1.22
Diluted net income per share of common stock	$ 1.77	$ 2.19	$ 1.22
Weighted average shares outstanding:			
Basic	22,010,462	22,127,919	20,162,038
Diluted	22,059,855	22,179,461	20,185,589

See accompanying notes to consolidated financial statements.

CAPSTAR FINANCIAL HOLDINGS INC. & SUBSIDIARY
Consolidated Statements of Comprehensive Income
(Dollars in thousands)

	Year Ended December 31,		
	2022	2021	2020
Net income	$ 39,017	$ 48,677	$ 24,696
Other comprehensive income (loss):			
Unrealized (losses) gains on securities available-for-sale:			
Unrealized holding (losses) gains arising during the period	(65,897)	(12,141)	4,968
Reclassification adjustment for gains included in net income	(8)	(28)	(125)
Tax effect	17,123	3,171	(1,177)
Net of tax	$ (48,782)	(8,998)	3,666
Unrealized losses on cash flow hedges:			
Reclassification adjustment for losses included in net income	—	—	2,679
Tax effect	—	—	—
Net of tax	—	—	2,679
Other comprehensive (loss) income	(48,782)	(8,998)	6,345
Comprehensive (loss) income	$ (9,765)	$ 39,679	$ 31,041

See accompanying notes to consolidated financial statements.

CAPSTAR FINANCIAL HOLDINGS INC. & SUBSIDIARY
Consolidated Statements of Changes in Shareholders' Equity
(Dollars in thousands, except share and per share data)

	Common stock, voting		Additional paid-in capital	Retained earnings	Accumulated other comprehensive (loss) income	Total shareholders' equity
	Shares	Amount				
Balance December 31, 2019	18,361,922	$ 18,362	$ 207,083	$ 46,218	$ 1,383	$ 273,046
Net issuance of restricted common stock	122,381	122	(165)	—	—	(43)
Stock-based compensation expense	—	—	1,223	—	—	1,223
Net exercise of common stock options	20,582	21	85	—	—	106
Repurchase of common stock	(147,800)	(148)	(1,289)	—	—	(1,437)
Issuance of common stock in conjunction with acquisitions	3,631,718	3,632	39,953	—	—	43,585
Common stock dividends declared ($0.20 per share)	—	—	—	(4,035)	—	(4,035)
Net income	—	—	—	24,696	—	24,696
Other comprehensive income	—	—	—	—	6,345	6,345
Balance December 31, 2020	21,988,803	$ 21,989	$ 246,890	$ 66,879	$ 7,728	$ 343,486
Net issuance of restricted common stock	110,103	110	(329)	—	—	(219)
Stock-based compensation expense	—	—	1,600	—	—	1,600
Net exercise of common stock options	94,483	94	983	—	—	1,077
Repurchase of common stock	(27,260)	(27)	(435)	—	—	(462)
Common stock dividends declared ($0.23 per share)	—	—	—	(5,067)	—	(5,067)
Net income	—	—	—	48,677	—	48,677
Other comprehensive loss	—	—	—	—	(8,998)	(8,998)
Balance December 31, 2021	22,166,129	$ 22,166	$ 248,709	$ 110,489	$ (1,270)	$ 380,094
Net issuance of restricted common stock	40,267	40	(170)	-	-	(130)
Stock-based compensation expense	—	—	1,355	—	—	1,355
Net exercise of common stock options	5,800	6	45	—	—	51
Repurchase of common stock	(497,816)	(498)	(9,076)	—	—	(9,574)
Common stock dividends declared ($0.36 per share)	—	—	—	(7,849)	—	(7,849)
Net income	—	—	—	39,017	—	39,017
Other comprehensive loss	—	—	—	—	(48,782)	(48,782)
Balance December 31, 2022	21,714,380	$ 21,714	$ 240,863	$ 141,657	$ (50,052)	$ 354,182

See accompanying notes to consolidated financial statements.

CAPSTAR FINANCIAL HOLDINGS INC. & SUBSIDIARY
Consolidated Statements of Cash Flows
(Dollars in thousands)

	Year Ended December 31,		
	2022	2021	2020
Cash flows from operating activities:			
Net income	$ 39,017	$ 48,677	$ 24,696
Adjustments to reconcile net income to net cash (used in) provided by operating activities:			
Provision for loan losses	2,474	(1,066)	11,479
Amortization (accretion) of discounts on acquired loan and deferred fees, net	681	(7,016)	(5,290)
Depreciation and amortization	3,174	3,452	3,201
Net amortization of premiums on investment securities	1,828	2,435	1,563
Net gain on sale of securities	(8)	(28)	(125)
Mortgage banking income	(5,073)	(16,058)	(25,034)
Tri-Net fees	(78)	(8,613)	(3,693)
Net gain on sale of SBA loans	(2,501)	(2,060)	(1,440)
Net gain on disposal of premises and equipment	(14)	(21)	(303)
Net gain on sale of other real estate owned	(102)	(49)	(273)
Stock-based compensation	1,355	1,600	1,223
Deferred income tax expense (benefit)	470	(207)	(4,339)
Origination of loans held for sale	(685,622)	(1,288,434)	(1,355,961)
Proceeds from loans held for sale	626,778	1,397,992	1,365,568
Cash payments arising from operating leases	(2,194)	(2,074)	(1,814)
Amortization of debt issuance expense	134	109	36
Net (increase) decrease in accrued interest receivable and other assets	(2,829)	(15,318)	2,894
Net (decrease) increase in accrued interest payable and other liabilities	(1,207)	3,043	6,790
Net cash (used in) provided by operating activities	(23,717)	116,364	19,178
Cash flows from investing activities:			
Activities in securities available-for-sale:			
Purchases	(68,895)	(92,465)	(340,962)
Sales	—	—	78,385
Maturities, prepayments and calls	64,177	104,733	91,616
Activities in securities held-to-maturity:			
Maturities, prepayments and calls	515	600	881
(Purchase) redemption of restricted equity securities	(2,179)	1,109	(783)
Net increase in loans	(242,573)	(57,110)	(162,843)
Purchase of premises and equipment	(981)	(503)	(417)
Proceeds from sale of premises and equipment	429	21	3,286
Purchases of bank owned life insurance	—	(39,000)	—
Proceeds from sale of other real estate	368	2,328	1,817
Cash paid for acquisitions	—	—	(27,278)
Cash received from acquisitions	—	—	90,760
Net cash used in investing activities	(249,139)	(80,287)	(265,538)
Cash flows from financing activities:			
Net (decrease) increase in deposits	(4,462)	116,280	395,873
Proceeds from Federal Home Loan Bank advances	395,000	—	680,000
Payments on Federal Home Loan Bank advances	(380,000)	(10,000)	(680,000)
Proceeds from issuance of subordinated notes, net of debt issuance expense	—	—	29,387
Repurchase of common stock	(9,574)	(462)	(1,437)
Exercise of common stock options and warrants, net of repurchase of restricted shares	(79)	858	63
Common stock dividends paid	(7,849)	(5,067)	(4,035)
Termination of interest rate swap agreement and related reclassification adjustment for unrealized losses included in income	—	—	2,679
Net cash (used in) provided by financing activities	(6,964)	101,609	422,530
Net (decrease) increase in cash and cash equivalents	(279,820)	137,686	176,170
Cash and cash equivalents at beginning of period	415,125	277,439	101,269
Cash and cash equivalents at end of period	$ 135,305	$ 415,125	$ 277,439
Supplemental disclosures of cash paid:			
Interest paid	$ 15,427	$ 8,075	$ 15,551
Income taxes	8,860	16,045	10,353
Supplemental disclosures of noncash transactions:			
Transfer of loans to other real estate	—	2,022	452
Loans charged off to the allowance for loan losses	756	647	1,226
Lease liabilities arising from obtaining right-of-use assets	570	—	668
Unrealized (losses) gains on securities available for sale	(48,782)	(8,998)	3,666
Loans transferred from held-for-sale to held-for-investment, net of loans from held-for-investment transferred to held-for-sale	105,503	18,396	2,800
Assets acquired, net of cash	—	—	423,983
Liabilities assumed	—	—	447,412
Goodwill	—	—	3,558

See accompanying notes to consolidated financial statements.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The consolidated financial statements as of December 31, 2022 and 2021 and for each of the three years in the period ended December 31, 2022 include CapStar Financial Holdings, Inc. and it's wholly owned subsidiary, CapStar Bank (the "Bank", together referred to as the "Company"). Significant intercompany transactions and accounts are eliminated in consolidation.

The consolidated financial statements of the Company have been prepared in conformity with U.S. generally accepted accounting principles ("GAAP") and conform to general practices within the banking industry.

Business Combinations

The Company accounts for business combinations using the acquisition method of accounting. The accounts of an acquired entity are included as of the date of acquisition, and any excess of purchase price over the fair value of the net assets acquired is capitalized as goodwill. Under this method, all identifiable assets acquired, including purchased loans, and liabilities assumed are recorded at fair value.

The Company typically issues common stock and/or pays cash for an acquisition, depending on the terms of the acquisition agreement. The value of shares of common stock issued is determined based on the market price of the stock as of the closing of the acquisition.

Nature of Operations

Through the Bank, the Company provides full banking services to consumer and corporate customers located primarily in Tennessee. The Bank operates under a state bank charter and is a member of the Federal Reserve System. As a state member bank, the Bank is subject to regulations of the Tennessee Department of Financial Institutions, the Board of Governors of the Federal Reserve System (the "Federal Reserve"), and the Federal Deposit Insurance Corporation.

Reclassifications

Certain amounts, previously reported, have been reclassified to state all periods on a comparable basis and had no effect on shareholders' equity or net income.

Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change relate to the determination of the allowance for loan losses, determination of impairment of intangible assets, including goodwill, the valuation of our investment portfolio, the valuation of loans held for sale, and deferred tax assets.

Cash and Cash Equivalents

For purposes of reporting cash flows, cash and cash equivalents include cash on hand, amounts due from banks, interest-bearing deposits in financial institutions and federal funds sold. Generally, federal funds are purchased and sold for one-day periods. The Company maintains deposits in excess of the federal insurance amounts with other financial institutions. Management makes deposits only with financial institutions it considers to be financially sound.

Securities

The Bank accounts for securities under the provisions of Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") 320, *Investments – Debt and Equity Securities*. Under the provisions of FASB ASC 320, securities are to be classified in three categories and accounted for as follows:

Securities Held-to-Maturity - Debt securities are classified as held-to-maturity securities when the Bank has the positive intent and ability to hold the securities to maturity. Securities held to maturity are carried at amortized cost.

Trading Securities - Debt and equity securities that are bought and held principally for the purpose of selling them in the near term are classified as trading securities and reported at fair value, with unrealized gains and losses included in earnings. No securities have been classified as trading securities.

Securities Available-for-Sale - Debt securities not classified as either held-to-maturity securities or trading securities are classified as available for sale securities. Securities available for sale are carried at estimated fair value with unrealized gains and losses excluded from earnings and reported as a separate component of shareholders' equity in other comprehensive income (loss).

Interest income includes amortization of purchase premiums or discounts. Premiums and discounts on securities are amortized on the level-yield method without anticipating prepayments, except for mortgage-backed securities where prepayments are anticipated. Realized gains and losses from the sales of securities are recorded on the trade date and determined using the specific-identification method.

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

Loans Held For Sale and Fair Value Option

The Company classifies loans as loans held for sale when originated with the intent to sell. As of April 1, 2019, the Company elected the fair value option for all residential mortgage loans originated with the intent to sell. This election allows for a more effective offset of the changes in fair values of the loans and the derivative instruments used to economically hedge them without the burden of complying with the requirements for hedge accounting. The Company has not elected the fair value option for other loans held for sale primarily because they are not economically hedged using derivative instruments. The fair value of residential mortgage loans originated with the intent to sell is based on traded market prices of similar assets. Other loans held for sale, such as SBA loans or Tri-Net loans, that are recorded at lower of cost or fair value may be carried at fair value on a nonrecurring basis when the fair value is less than cost. No SBA loans or Tri-Net loans were measured at fair value as of December 31, 2022. For further information, see Note 22 - Fair Value. The Company does not securitize mortgage loans. If the Company sells loans with servicing rights retained, the carrying value of the mortgage loan sold is reduced by the amount allocated to the servicing right. The changes in fair value are recorded as a component of mortgage banking income and included gains (losses) of ($0.5) million, ($2.5) million, and $2.5 million for the years ended December 31, 2022, 2021, and 2020, respectively.

The following table summarizes the difference between the fair value and the aggregate unpaid principal balance for residential real estate loans held for sale as of December 31, 2022 and 2021 (dollars in thousands):

	Fair Value	Aggregate Unpaid Principal Balance	Difference
December 31, 2022			
Residential mortgage loans held for sale	$ 12,636	$ 12,582	$ 54
December 31, 2021			
Residential mortgage loans held for sale	37,306	36,755	551

Tri-Net Fees

Tri-Net fees are derived from the origination of commercial real estate loans with the intent to sell to third-party investors. All of these loan sales transfer servicing rights to the buyer. Realized gains and losses are recognized when legal title of the loan has transferred to the investor and sales proceeds have been received and are reflected in the accompanying statements of income in Tri-Net fees, net of related costs such as commission expenses. Loans that have not been sold at period end are classified as held for sale on the balance sheet and recorded at the lower of aggregate cost or fair value. Net unrealized losses, if any, are recorded as a valuation allowance and charged to earnings.

Loans

The Company has seven classes of loans held for investment: commercial real estate, consumer real estate, construction and land development, commercial and industrial, consumer, PPP, and other. The appropriate classification is determined based on the underlying collateral utilized to secure each loan.

Commercial real estate includes both owner-occupied and non-owner occupied properties. The repayment of owner-occupied properties is largely dependent on the operations of the tenant, while non-owner occupied properties is dependent upon the refinance or sale of the underlying real estate.

Consumer real estate consists primarily of 1-4 family residential properties including home equity lines of credit.

Construction and land development loans include loans where the repayment is dependent on the successful completion and operation and/or sale of the related real estate project. Construction and land development loans include 1-4 family construction projects and commercial construction endeavors such as warehouses, apartments, office and retail space and land acquisition and development.

Commercial and industrial loans include loans to business enterprises issued for commercial, industrial and/or other professional purposes.

Consumer loans include all loans issued to individuals not included in the consumer real estate class.

PPP loans originated through the CARES act and include partially, or fully forgivable loans used to cover payroll costs, rent, interest, utilities, and other qualifiable expenses.

Other loans include all loans not included in the classes of loans above and leases.

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 purchase premiums and discounts, deferred loan fees and costs, and an allowance for loan losses. Interest income is accrued on the unpaid principal balance. Loan origination fees, net of certain direct origination costs, are deferred and recognized in interest income using the level-yield method without anticipating prepayments.

The accrual of interest on loans is discontinued at the time the loan is 90 days past due unless the credit is well secured and in process of collection. Consumer loans and any accrued interest are typically charged off no later than 180 days past due. Past due status is based on contractual terms of the loan. In all cases, loans are placed on non-accrual or charged off at an earlier date if collection of principal or interest is considered doubtful and collection is highly questionable. Amortization of deferred loan fees is discontinued when a loan is placed on non-accrual status.

All interest accrued but not received for loans placed on non-accrual is reversed against interest income. Interest received on such loans is accounted for on the cash-basis or cost-recovery method, until qualifying for return to accrual status. Under the cost-recovery method, interest income is not recognized until the loan balance is reduced to zero. Under the cash-basis method, interest income is recorded when the payment is received in cash. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured. Loans can also be returned to accrual status when they become well secured and in the process of collection.

Acquired Loans

Acquired loans are accounted for under the acquisition method of accounting. The acquired loans are recorded at their estimated fair values as of the acquisition date. Fair value of acquired loans is determined using a discounted cash flow model based on assumptions regarding the amount and timing of principal and interest payments, estimated prepayments, estimated default rates, estimated loss severity in the event of defaults, and current market rates. Estimated credit losses are included in the determination of fair value; therefore, an allowance for loan losses is not recorded on the acquisition date.

An acquired loan is considered purchased credit impaired when there is evidence of credit deterioration since origination and it is probable at the date of acquisition that the Bank will be unable to collect all contractually required payments.

Purchased credit impaired loans are accounted for individually or aggregated into pools of loans based on common risk characteristics such as loan type and risk rating. The Company estimates the amount and timing of expected cash flows for each loan or pool, and the expected cash flows in excess of amount paid (fair value) is recorded as interest income over the remaining life of the loan or pool (accretable yield). The excess of the loan's or pool's contractual principal and interest over expected cash flows is not recorded (nonaccretable difference). Over the life of the loan or pool, expected cash flows continue to be estimated. If the present value of expected cash flows is less than the carrying amount, a loss is recorded as a provision for loan losses. If the present value of expected cash flows is greater than the carrying amount, it is recognized as part of future interest income.

Acquired non-impaired loans are recorded at their initial fair value and adjusted for subsequent advances, pay downs, amortization or accretion of any premium or discount on purchase, charge-offs and additional provisioning that may be required.

Allowance for Loan Losses

The allowance for loan losses ("ALL") is maintained at a level that management believes to be adequate to absorb expected loan losses inherent in the loan portfolio as of the balance sheet date. The allowance for loan losses is a valuation allowance for estimated credit losses inherent in the loan and lease portfolio, increased by the provision for loan losses and decreased by charge-offs, net of recoveries. Quarterly, the Company estimates the allowance required using peer group loss experience, the nature and volume of the portfolio, information about specific borrower situations and estimated collateral values, economic conditions, and other factors. The Company's historical loss experience is based on the actual loss history by class of loan for comparable peer institutions due to the Company's

limited loss history. 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. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries are credited to the allowance for loan losses.

The Company also considers the results of the external independent loan review when assessing the adequacy of the allowance and incorporates relevant loan review results in the loan impairment and overall adequacy of allowance determinations. Furthermore, regulatory agencies periodically review the Company's allowance for loan losses and may require the Company to record adjustments to the allowance based on their judgment of information available to them at the time of their examinations.

Additional considerations are included in the determination of the adequacy of the allowance based on the continuous review conducted by relationship managers and credit department personnel. The Company's loan policy requires that each customer relationship wherein total exposure exceeds $1.5 million be subject to a formal credit review at least annually. Should these reviews identify potential collection concerns, appropriate adjustments to the allowance may be made.

The allowance consists of specific and general components as discussed below. While the allowance consists of separate components, these terms are primarily used to describe a process. Both portions of the allowance are available to provide for inherent losses in the entire portfolio.

Specific Component

The specific component relates to loans that are individually determined to be impaired when, based on current information and events, it is probable that the Company will be unable to collect all amounts due according to the contractual terms of the loan agreement. Loans for which the terms have been modified resulting in a concession, and for which the borrower is experiencing financial difficulties, are considered troubled debt restructurings ("TDRs") and classified as impaired.

Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed.

Loans meeting any of the following criteria are individually evaluated for impairment: risk rated substandard (as defined in Note 4), on non-accrual status or past due greater than 90 days. If a loan is impaired, a portion of the allowance is allocated based on the present value of estimated future cash flows using the loan's existing rate or at the fair value of collateral less costs to sell if repayment is expected solely from the collateral. Changes to the valuation allowance are recorded as a component of the provision for loan losses.

TDRs are individually evaluated for impairment and included in the separately identified impairment disclosures. TDRs are measured at the present value of estimated future cash flows using the loan's effective rate at inception. If a TDR is considered to be a collateral dependent loan, the loan is reported, net, at the fair value of the collateral less costs to sell.

General Component

The general component of the allowance for loan losses covers loans that are collectively evaluated for impairment. Large groups of homogeneous loans are collectively evaluated for impairment, and accordingly, they are not included in the separately identified impairment disclosures. The general allowance component also includes loans that are individually identified for impairment evaluation but are not considered impaired. The general component is based on historical loss experience adjusted for current factors. Due to the Company's limited loss history, the historical loss experience is based on the actual loss history by class of loan for comparable peer institutions.

The Company utilized a look-back period of 53 quarters, 49 quarters, and 45 quarters as of December 31, 2022, 2021, and 2020, respectively. In the current economic environment, management believes the extension of the look-back period was necessary in order to capture sufficient loss observations to develop a reliable loss estimate of credit losses. This extension of the historical look-back period to capture the historical loss experience of peer banks was applied to all classes and segments of our loan portfolio.

The actual loss experience is supplemented with other environmental factors that capture changes in trends, conditions, and other relevant factors that may cause estimated credit losses as of the evaluation date to differ from historical loss experience. The allocation for environmental factors is by nature subjective. These amounts represent estimated probable inherent credit losses, which exist but have not been captured in the historical loss experience. The environmental factors include consideration of the following: changes in lending policies and procedures, economic conditions, nature and volume of the portfolio, experience of lending management, volume and severity of past due loans, quality of the loan review system, value of underlying collateral for collateral dependent loans, concentrations, and other external factors.

Servicing Rights

When mortgage loans are sold with servicing retained, servicing rights are initially recorded at fair value with the income statement effect recorded in other noninterest income. Fair value is based on market prices for comparable mortgage servicing contracts, when available or alternatively, is based on a valuation model that calculates the present value of estimated future net servicing income. All classes of servicing assets are subsequently measured using the amortization method which requires servicing rights to be amortized into noninterest income in proportion to, and over the period of, the estimated future net servicing income of the underlying loans.

Servicing rights are evaluated for impairment based upon the fair value of the rights as compared to carrying amount. Impairment is determined by stratifying rights into groupings based on predominant risk characteristics, such as interest rate, loan type and investor type. Impairment is recognized through a valuation allowance for an individual grouping, to the extent that fair value is less than the carrying amount. If the Company later determines that all or a portion of the impairment no longer exists for a particular grouping, a reduction of the allowance may be recorded as an increase to income. Changes in valuation allowances are reported with other noninterest income on the income statement and the associated asset is included in other assets on the Consolidated Balance Sheet. The fair values of servicing rights are subject to significant fluctuations as a result of changes in estimated and actual prepayment speeds and default rates and losses.

Servicing fee income, which is reported on the income statement within other noninterest income, is recorded for fees earned for servicing loans. The fees are based on a contractual percentage of the outstanding principal or a fixed amount per loan and are recorded as income when earned. The amortization of mortgage servicing rights is netted against loan servicing fee income. Net servicing fees totaled $0.4 million, $0.6 million, and $0.7 million for the years ended December 31, 2022, 2021, and 2020 respectively. Valuation adjustments associated with these servicing rights amounted to $47 thousand, $77 thousand and ($238) thousand for the years ended December 31, 2022, 2021 and 2020, respectively. Late fees and ancillary fees related to loan servicing are not material.

Premises and Equipment

Premises and equipment are stated at cost less accumulated depreciation and amortization. Depreciation is computed principally by the straight-line method over the estimated useful lives of the assets. Leasehold improvements are amortized by the straight-line method based on the shorter of the asset lives or the expected lease terms. Useful lives for premises and equipment range from one to thirty-nine years.

These assets are reviewed for impairment when events indicate their carrying amount may not be recoverable from future undiscounted cash flows. If impaired, the assets are recorded at fair value.

Leases

In February 2016, the FASB issued a new accounting standard update (Accounting Standards Update ("ASU") 2016-02, Leases (Topic 842)), which requires for all operating leases the recognition of a ROU asset and a corresponding lease liability, in the Consolidated Balance Sheet. For short term leases (term of 12 months or less), a lessee is permitted to make an accounting election not to recognize lease assets and lease liabilities. The lease cost will be allocated over the lease term on a straight-line basis. There were further amendments, including practical expedients, with the issuance of ASU 2018-01, “Leases (Topic 842): Land Easement Practical Expedient for Transition to Topic 842” in January 2018. In July 2018, the FASB issued ASU No. 2018-11, "Leases (Topic 842): Targeted Improvements", which provides for the option to apply the new leasing standard to all open leases as of the adoption date, on a prospective basis.

Bank Owned Life Insurance

The Bank has purchased life insurance policies on certain key executives. Bank owned life insurance is recorded at the amount that can be realized under the insurance contract at the balance sheet date, which is the cash surrender value adjusted for other charges or other amounts due that are probable at settlement. Bank owned life insurance is included in other assets on the Consolidated Balance Sheet.

Securities Sold under Agreements to Repurchase

The Bank enters into sales of securities under agreements to repurchase at a specified future date. Such repurchase agreements are considered financing arrangements and, accordingly, the obligation to repurchase assets sold is reflected as a liability in the balance sheets of the Bank. Repurchase agreements are collateralized by debt securities which are owned and under the control of the Bank and are included in other liabilities on the Consolidated Balance Sheet.

Goodwill and Other Intangible Assets

Goodwill resulting from business combinations is generally determined as the excess of the fair value of the consideration transferred, plus the fair value of any noncontrolling interests in the acquiree, over the fair value of the net assets acquired and liabilities assumed as of the acquisition date. Goodwill and intangible assets acquired in a business combination and determined to have an indefinite useful life are not amortized, but tested for impairment at least annually or more frequently if events and circumstances exists that indicate that a goodwill impairment test should be performed. Qualitative factors are assessed to first determine if it is more likely than not (more than 50%) that the carrying value of goodwill is less than fair value.

During the year ended December 31, 2022 and 2021, qualitative factors indicated it was more likely than not that the carrying value of goodwill was less than fair value, thus there were no indicators of impairment and no quantitative testing was performed.

Intangible assets with definite useful lives are amortized over their estimated useful lives to their estimated residual values. Goodwill is the only intangible asset with an indefinite life on the balance sheet.

Other intangible assets consist of core deposit intangible assets arising from whole bank acquisitions and are amortized on an accelerated method over their estimated useful lives, which range from six to ten years.

Other Real Estate Owned

Other real estate owned ("OREO") includes assets that have been acquired in satisfaction of debt through foreclosure and are recorded at estimated fair value less the estimated cost of disposition. Fair value is based on independent appraisals and other relevant factors. Valuation adjustments required at foreclosure are charged to the allowance for loan losses. Subsequent to foreclosure, additional losses resulting from the periodic revaluation of the property are charged to other real estate expense. Costs of operating and maintaining the properties and any gains or losses recognized on disposition are also included in other real estate expense. Improvements made to properties are capitalized if the expenditures are expected to be recovered upon the sale of the properties.

Restricted Equity Securities

The Bank is a member of the FHLB system. Members are required to own a certain amount of stock based upon the level of borrowings and other factors, and may invest additional amounts. FHLB stock is carried at cost, classified as a restricted equity security, and periodically evaluated for impairment based on an assessment of the ultimate recovery of par value. Both cash and stock dividends are reported as interest income on the Consolidated Statements of Income.

The Bank is also a member of the Federal Reserve System, and as such, holds stock of the Federal Reserve Bank of Atlanta ("Federal Reserve Bank"). Federal Reserve Bank stock is carried at cost, classified as a restricted equity security, and periodically evaluated for impairment based on ultimate recovery of par value. Both cash and stock dividends are reported as interest income on the Consolidated Statements of Income.

Income Taxes

Income tax expense is the total of the current year income tax due or refundable and the change in deferred tax assets and liabilities. Deferred tax assets and liabilities are the expected future tax amounts for the temporary differences between carrying amounts and tax bases of assets and liabilities, computed using enacted tax rates. A valuation allowance, if needed, reduces deferred tax assets to the amount expected to be realized.

A tax position is recognized as a benefit only if it is "more likely than not" that the tax position would be sustained in a tax examination, with a tax examination being presumed to occur. The amount recognized is the largest amount of tax benefit that is greater than 50% likely of being realized on examination. For tax positions not meeting the "more likely than not" test, no tax benefit is recorded. The Company's tax returns remain open to audit under the statute of limitations by the IRS and various states for the years ended December 31, 2019 through 2022. It is the Company's policy to recognize interest and/or penalties related to income tax matters in income tax expense on the Consolidated Statements of Income.

Stock-Based Compensation

Stock-based compensation expense is recognized based on the fair value of the portion of stock-based payment awards that are ultimately expected to vest, reduced for estimated forfeitures. Forfeitures are estimated at the time of grant and revised, if necessary, in subsequent periods, if actual forfeitures differ from those estimates. A Black-Scholes model is utilized to estimate the fair value of stock options, while the market price of the Company's common stock at the date of grant is used for restricted stock awards. Compensation expense is recognized over the required service period, generally defined as the vesting period. For awards with graded vesting, compensation expense is recognized on a straight-line basis over the requisite service period for the entire award. For awards with performance vesting criteria, anticipated performance is projected to determine the number of awards expected to vest, and the corresponding aggregate expense is adjusted to reflect the elapsed portion of the performance period.

Advertising Costs

Advertising costs are expensed as incurred. Advertising expense was approximately $0.9 million, $0.8 million, $0.4 million for the years ended December 31, 2022, 2021 and 2020, respectively and is included in other operating expenses on the Consolidated Statements of Income.

Off-Balance Sheet Financial Instruments

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

Derivative Instruments

Derivative instruments are recorded on the balance sheet at their respective fair values. The accounting for changes in fair value (i.e., gains or losses) of a derivative instrument depends on whether it has been designated and qualifies as part of a hedging relationship. If the derivative instrument is not designated as a hedge, the gain or loss on the derivative instrument is recognized in earnings in the period of change.

The Bank enters into interest rate swaps ("swaps") to facilitate customer transactions and meet their financing needs. Upon entering into these arrangements to meet customer needs, the Bank enters into offsetting positions with large U.S. financial institutions in order to minimize market risk to the Bank. These swaps are derivatives, but are not designated as hedging instruments.

The Bank may also utilize cash flow hedges to manage its future interest rate exposure. These derivative contracts are designated as hedges and, as such, changes in the fair value of these derivative instruments are recorded in other comprehensive income (loss) on the Consolidated Statements of Comprehensive Income. The Bank prepares written hedge documentation for all derivatives which are designated as hedges. The written hedge documentation includes identification of, among other items, the risk management objective, hedging instrument, hedged item and methodologies for assessing and measuring hedge effectiveness and ineffectiveness, along with support for management's assertion that the hedge will be highly effective.

The effective portion of the changes in the fair value of a derivative that is highly effective and that has been designated and qualifies as a cash flow hedge are initially recorded in accumulated other comprehensive income (loss) and subsequently reclassified into earnings in the same period during which the hedged item affects earnings. The ineffective portion, if any, would be recognized in current period earnings.

The Bank discontinues hedge accounting when it determines that the derivative is no longer effective in offsetting changes in the cash flows of the hedged item, the derivative is settled or terminates, or treatment of the derivative as a hedge is no longer appropriate or intended. When hedge accounting is discontinued, subsequent changes in fair value of the derivative are recorded as noninterest income. When a cash flow hedge is discontinued but the hedged cash flows or forecasted transactions are still expected to occur, gains or losses that were accumulated in other

comprehensive income (loss) are amortized into earnings over the same periods which the hedged transactions will affect earnings.

Cash flows resulting from the derivative financial instruments that are accounted for as hedges are classified in the cash flow statement in the same category as the cash flows of the items being hedged.

Commitments to fund mortgage loans to be sold into the secondary market, “interest rate locks”, and forward commitments for the sale of mortgage-backed securities are accounted for as free standing derivatives. The fair value of the interest rate lock is recorded at the time the commitment to fund the mortgage loan is executed and is adjusted for the expected exercise of the commitment before the loan is funded. Fair values of these mortgage derivatives are estimated based on changes in mortgage interest rates from the date the interest rate on the loan is locked. The Company enters into forward commitments for the sale of mortgage-backed securities when interest rate locks are entered into, in order to hedge the change in interest rates resulting from its commitments to fund the loans. Changes in the fair values of these derivatives are included in mortgage banking income on the Consolidated Statements of Income.

Comprehensive Income

Comprehensive income consists of net income and other comprehensive income (loss). Other comprehensive income includes unrealized gains and losses on securities available for sale, unrealized gains and losses on securities transferred to held to maturity and unrealized gains and losses on cash flow hedges which are also recognized as separate components of equity. The Bank’s policy is to release the income tax effects of items in accumulated other comprehensive income (loss) when the item is realized.

Fair Value Measurements

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

Restriction on Cash Balances

Regulation D of the Federal Reserve Act requires that banks maintain reserve balances with their applicable Federal Reserve Bank based principally on the type and amount of their deposits. On March 15, 2020, the Board of the Federal Reserve reduced reserve requirement ratios to zero percent effective March 26, 2020. This action eliminated reserve requirements for all depository institutions.

Subsequent Events

The Company has evaluated subsequent events for recognition and disclosure through March 3, 2023, which is the date the financial statements were available to be issued.

Income Per Common Share

Basic net income per share available to common stockholders ("EPS") is computed by dividing net income available to common stockholders by the weighted average shares of common stock outstanding for the period. Diluted EPS reflects the dilution that could occur if securities or other contracts to issue common stock were exercised or converted. The difference between basic and diluted weighted average shares outstanding is attributable to convertible preferred stock, common stock options and warrants. The dilutive effect of outstanding convertible preferred stock, common stock options and warrants is reflected in diluted EPS by application of the treasury stock method.

No antidilutive stock options were excluded from calculation for the years ended December 31, 2022, 2021 or 2020.

The following is a summary of the basic and diluted earnings per share calculation for each of the following years (in thousands except share data):

	Year Ended December 31,		
	2022	2021	2020
Basic net income per share calculation:			
Numerator – Net income	$ 39,017	$ 48,677	$ 24,696
Denominator – Average common shares outstanding	22,010,462	22,127,919	20,162,038
Basic net income per share	$ 1.77	$ 2.20	$ 1.22
Diluted net income per share calculation:			
Numerator – Net income	$ 39,017	$ 48,677	$ 24,696
Denominator – Average common shares outstanding	22,010,462	22,127,919	20,162,038
Dilutive shares contingently issuable	49,393	51,542	23,551
Average diluted common shares outstanding	22,059,855	22,179,461	20,185,589
Diluted net income per share	$ 1.77	$ 2.19	$ 1.22

Recently Issued Accounting Pronouncements

ASU 2016-13, Financial Instruments – Credit Losses (Topic326) and related amendments

In June 2016, the FASB issued guidance to change the accounting for credit losses and modify the impairment model for certain debt securities. The guidance requires an entity to utilize a new impairment model known as the current expected credit loss ("CECL") model to estimate its lifetime "expected credit losses" and record an allowance that, when deducted from the amortized cost basis of the financial assets, presents the net amount expected to be collected on the financial assets. Purchased credit deteriorated ("PCD") loans will receive an initial allowance at the acquisition date that represents an adjustment to the amortized cost basis of the loan, with no impact to earnings. Credit losses relating to available-for-sale debt securities will be recorded through an allowance for credit losses prospectively, with such allowance limited to the amount by which fair value is below amortized cost. The CECL framework is expected to result in earlier recognition of credit losses and is expected to be significantly influenced by the composition, characteristics and quality of the Company's loan portfolio, as well as the prevailing economic conditions and forecasts.

In April 2019, the FASB issued ASU 2019-04, *Codification Improvements to Topic 326, Financial Instruments-Credit Losses, Topic 815, Derivatives and Hedging, and Topic 825, Financial Instruments,* which clarifies the scope of the credit losses standard and addresses issues related to accrued interest receivable balances and recoveries, among other things. In May 2019, the FASB issued ASU 2019-05, *Financial Instruments-Credit Losses (Topic 326): Targeted Transition Relief.* The amendments provide entities with an option to irrevocably elect the fair value option for certain financial assets previously measured at amortized cost basis, upon adoption of Topic 326. In November 2019, the FASB issued ASU 2019-10, *Financial Instruments-Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842): Effective Dates*. This update deferred the effective dates of Topic 326 to January 1, 2023 for certain entities including smaller reporting companies as defined by the SEC. The Company, as a smaller reporting company as of the relevant measuring period, qualified for this extension.

In March 2022, the FASB issued ASU 2022-02, *Financial Instruments – Credit Losses (Topic 326): Troubled Debt Restructurings and Vintage Disclosures,* which eliminates the accounting guidance for troubled debt restructurings by creditors in ASC 310-40, Receivables – Troubled Debt Restructurings by Creditors, while enhancing disclosure requirements for certain loan refinancings and restructurings involving borrowings that are experiencing financial difficulty. Specifically, rather than applying the troubled debt restructuring recognition and measurement guidance, creditors will evaluate all loan modifications to determine if they result in a new loan or a continuation of the existing

loan. Losses associated with troubled debt restructurings should be incorporated in a creditor's estimate of its allowance for credit losses. Additionally, public business entities are required to disclose current-period gross write-offs by year of origination for loan financing receivables and net investment in leases.

The Company is currently finalizing its assessment of the adoption and ongoing impact, along with testing and finalization of internal controls relative to the adoption of CECL. At this time, the Company expects its allowance for credit losses related to all financial assets will increase in 2023 to approximately $24.5 to $26.0 million upon adoption compared to its allowance for loan losses at December 31, 2022 of approximately $24.1 million. Additionally, a reserve on unfunded commitments of $3.0 to $4.0 million will be established as a liability on the Consolidated Balance Sheet, a reserve that was previously not required. The Company will initially apply the impact of the new guidance through a cumulative-effect adjustment to retained earnings as of the beginning of the year of adoption, which, for the Company, is January 1, 2023. Future adjustments to credit loss expectations will be recorded through the income statement as charges or credits to earnings.

ASU 2020-04 — Applicable to entities within the scope of Topic 848, Reference Rate Reform:

In March 2020, the FASB issued guidance which provides temporary optional guidance to ease the potential burden in accounting for reference rate reform. The ASU provides optional expedients and exceptions for applying generally accepted accounting principles to contract modifications and hedging relationships, subject to meeting certain criteria, that reference LIBOR or another reference rate expected to be discontinued. It is intended to help stakeholders during the global market-wide reference rate transition period. In January 2021, the FASB issued ASU 2021-01 which clarifies that certain optional expedients and exceptions in Topic 848 for contract modifications and hedge accounting apply to derivatives that are affected by the discounting transition. The guidance was effective for all entities as of March 12, 2020 through December 31, 2022. The Company continues to implement its transition plan towards cessation of LIBOR and the modification of its outstanding financial instruments with attributes that are either directly or indirectly influenced by LIBOR. The Company expects to utilize the LIBOR transition relief allowed under ASU 2020-04, as applicable, and does not expect such adoption to have a material impact on its accounting and disclosures. The Company will continue to assess the impact as the reference rate transition approaches June 30, 2023.

NOTE 2 – ACQUISITIONS

FCB Acquisition

Effective July 1, 2020, pursuant to the Agreement and Plan of Acquisition dated as of January 23, 2020 (the "FCB Acquisition Agreement"), by and between the Company and FCB Corporation, a Tennessee corporation ("FCB"), FCB was acquired by CapStar, with CapStar continuing as the surviving entity (the "FCB Acquisition"). Immediately following the FCB Acquisition, The First National Bank of Manchester, a national banking association and a wholly owned subsidiary of FCB, was acquired by CapStar Bank, a Tennessee chartered bank and a wholly owned subsidiary of CapStar (the "FNBM Acquisition"), with CapStar Bank continuing as the surviving entity in the FNBM Acquisition.

Subject to the terms and conditions set forth in the FCB Acquisition Agreement, at the effective time of the FCB Acquisition, shares of common stock, par value $10.00 per share, of FCB ("FCB Common Stock") issued and outstanding immediately prior to the completion of the FCB Acquisition (other than shares of FCB Common Stock owned or held by FCB, CapStar and their subsidiaries (in each case, other than shares of FCB Common Stock held in a fiduciary or agency capacity or in satisfaction of debts previously contracted) were collectively converted into the right to receive in the aggregate 2,966,918 shares of common stock, par value $1.00 per share, of CapStar ("CapStar Common Stock"), with cash (without interest) in lieu of fractional shares, and $22.2 million in cash, without interest.

BOW Acquisition

Effective July 1, 2020, following the FCB Acquisition, pursuant to the Plan of Bank Acquisition, dated as of January 23, 2020 (the "BOW Acquisition Agreement," and together with the FCB Acquisition Agreement, the "Acquisition Agreements"), by and among CapStar, CapStar Bank and The Bank of Waynesboro, a Tennessee chartered bank ("BOW"), BOW was acquired by CapStar Bank, with CapStar Bank continuing as the surviving entity (the "BOW Acquisition," and together with the FCB Acquisition, the "Acquisitions").

On the terms and subject to the conditions set forth in the BOW Acquisition Agreement, at the effective time of the BOW Acquisition, shares of common stock, par value $10.00 per share, of BOW ("BOW Common Stock") issued and outstanding immediately prior to the completion of the BOW Acquisition (other than shares of BOW Common Stock owned or held by CapStar, CapStar Bank, BOW and their subsidiaries (in each case, other than shares of BOW Common Stock held in a fiduciary or agency capacity or in satisfaction of debts previously contracted)) were collectively converted into the right to receive in the aggregate 664,800 shares of CapStar Common Stock, with cash (without interest) in lieu of fractional shares, and $5.1 million in cash, without interest.

Total acquisition consideration amounted to approximately $70.9 million.

With the acquisitions, the Company further expanded its franchise in the Middle Tennessee market. FCB's and BOW's results of operations were included in the Company's results beginning July 1, 2020. Acquisition related costs of $5.4 million are included in the Company's consolidated statements of income for the year ended December 31, 2020. The fair value of the common shares issued as part of the consideration paid for the Acquisitions was determined by the closing price of the Company's common shares immediately preceding the acquisition date.

Goodwill of $3.6 million associated with the Acquisitions is not amortizable for book or tax purposes. The following table summarizes the consideration paid for the Acquisitions and the amounts of the assets acquired and liabilities assumed recognized at the acquisition date (in thousands).

	As recorded by FCB Corporation and BOW	Initial fair value adjustments		Measurement period adjustments	As recorded by CapStar Financial Holdings
Assets:					
Cash and cash equivalents	$ 90,760	$ —		$ —	$ 90,760
Securities	98,536	159	(a)	—	98,695
Loans, gross	296,992	(2,318)	(b)	—	294,674
Allowance for loan losses	(4,544)	4,544	(c)	—	—
Premises and equipment, net	9,907	1,540	(d)	—	11,447
Core deposit intangible	—	3,570	(e)	—	3,570
Other	16,514	(917)	(f)	—	15,597
Total	$ 508,165	$ 6,578		$ —	$ 514,743
Liabilities:					
Deposits	$ 440,025	$ 2,652	(g)	$ —	$ 442,677
Other	4,735	—		—	4,735
Total	$ 444,760	$ 2,652		$ —	$ 447,412
Net identifiable assets acquired					$ 67,331
Total cost of acquisition:					
Value of stock issued					$ 43,611
Cash consideration paid					27,278
Total cost of acquisition					$ 70,889
Goodwill recorded related to acquisition					$ 3,558

(a) The amount represents the fair value adjustment of securities that were subsequently sold.
(b) The amount represents the adjustment of the net book value of the acquired loans to their estimated fair value based on interest rates and expected cash flows at the date of acquisition.
(c) The amount represents the removal of FCB and BOW’s existing allowance for loan losses.
(d) The amount represents the adjustment of the net book value of acquired premises and equipment to their estimated fair value.
(e) The amount represents the adjustment of recording the fair value of the core deposit intangible representing the intangible value of the deposit base acquired and the fair value of the customer relationship.
(f) The amount represents the net adjustment of the deferred tax asset recognized on the fair value adjustments on acquired assets and assumed liabilities.
(g) The amount represents the adjustment necessary because the weighted average interest rate of acquired time deposits exceeded the cost of similar funding at the time of acquisition. The fair value adjustment will be amortized to reduce future interest expense over the life of the portfolio.

The following unaudited pro forma financial information presents the combined results of the Company, FCB and BOW as if the acquisition had occurred as of January 1, 2019, after giving effect to certain adjustments, including amortization of the core deposit intangible, and related income tax effects. The pro forma financial information does not necessarily reflect the results of operations that would have occurred had the Company, FCB and BOW constituted a single entity during such periods (in thousands, except share data):

	Pro forma combined twelve months ended December 31, 2020	Pro forma combined twelve months ended December 31, 2019
Net interest income	$ 73,571	$ 87,523
Noninterest income	44,453	27,375
Total revenue	118,024	114,898
Net income	25,927	28,989
Per share information:		
Basic net income per share of common stock	$ 1.29	$ 1.35
Diluted net income per share of common stock	$ 1.28	$ 1.30

NOTE 3 – INVESTMENT SECURITIES

Investment securities have been classified in the balance sheet according to management's intent. The Company's classification of securities at December 31, 2022 and 2021 was as follows (in thousands):

	December 31, 2022				December 31, 2021			
	Amortized Cost	Gross unrealized gains	Gross unrealized (losses)	Estimated fair value	Amortized Cost	Gross unrealized gains	Gross unrealized (losses)	Estimated fair value
Securities available-for-sale:								
U. S. government agency securities	$ 14,537	$ —	$ (1,635)	$ 12,902	$ 11,550	$ 47	$ (94)	$ 11,503
State and municipal securities	77,562	129	(9,379)	68,312	81,158	2,107	(705)	82,560
Mortgage-backed securities	300,488	—	(55,660)	244,828	300,398	2,008	(8,799)	293,607
Asset-backed securities	3,332	—	(62)	3,270	3,326	13	—	3,339
Other debt securities	70,542	3	(3,441)	67,104	67,104	1,514	(231)	68,387
Total	$ 466,461	$ 132	$ (70,177)	$ 396,416	$ 463,536	$ 5,689	$ (9,829)	$ 459,396
Securities held-to-maturity:								
State and municipal securities	$ 1,240	$ —	$ —	$ 1,240	$ 1,782	$ 48	$ —	$ 1,830
Total	$ 1,240	$ —	$ —	$ 1,240	$ 1,782	$ 48	$ —	$ 1,830

The amortized cost and fair value of debt and equity securities at December 31, 2022, by contractual maturity, are shown below (in thousands). Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. Securities not due at a single maturity date are shown separately.

	Available-for-sale		Held-to-maturity	
	Amortized cost	Estimated fair value	Amortized cost	Estimated fair value
Due in less than one year	$ 6,132	$ 6,142	$ 1,240	$ 1,240
Due one to five years	28,750	27,618	—	—
Due five to ten years	106,544	97,739	—	—
Due beyond ten years	21,215	16,819	—	—
Mortgage-backed securities	300,488	244,828	—	—
Asset-backed securities	3,332	3,270	—	—
	$ 466,461	$ 396,416	$ 1,240	$ 1,240

Results from sales, maturities, prepayments and calls of securities available for sale were as follows (in thousands):

	Year ended December 31		
	2022	2021	2020
Proceeds	$ 64,177	$ 104,733	$ 170,001
Gross gains	8	45	148
Gross losses	—	(17)	(23)

Securities with a market value of $217.3 million and $188.8 million at December 31, 2022 and 2021, respectively, were pledged to collateralize public deposits, derivative positions and Federal Home Loan Bank advances.

At December 31, 2022 and 2021 there were no holdings of securities of any one issuer, other than the U.S. Government and its agencies, in an amount greater than 10% of shareholders' equity.

The following tables show the Company's securities with unrealized losses, aggregated by major security type and length of time in a continuous unrealized loss position (in thousands):

	Less than 12 months		12 months or more		Total	
December 31, 2022	Estimated fair value	Gross unrealized losses	Estimated fair value	Gross unrealized losses	Estimated fair value	Gross unrealized losses
U. S. government agency securities	$ 6,243	$ (836)	$ 6,659	$ (799)	$ 12,902	$ (1,635)
State and municipal securities	12,952	(422)	41,779	(8,957)	54,731	(9,379)
Mortgage-backed securities	81,751	(7,647)	161,708	(48,013)	243,459	(55,660)
Asset-backed securities	3,270	(62)	—	—	3,270	(62)
Other debt securities	41,018	(2,028)	24,084	(1,413)	65,102	(3,441)
Total temporarily impaired securities	$ 145,234	$ (10,995)	$ 234,230	$ (59,182)	$ 379,464	$ (70,177)
December 31, 2021						
U. S. government agency securities	$ 2,560	$ (20)	$ 2,737	$ (74)	$ 5,297	$ (94)
State and municipal securities	15,309	(279)	12,768	(426)	28,077	(705)
Mortgage-backed securities	155,805	(5,291)	75,934	(3,508)	231,739	(8,799)
Asset-backed securities	—	—	—	—	—	—
Other debt securities	30,375	(231)	—	—	30,375	(231)
Total temporarily impaired securities	$ 204,049	$ (5,821)	$ 91,439	$ (4,008)	$ 295,488	$ (9,829)

Declines in the fair value of securities below their cost that are deemed to be other-than-temporary are reflected in earnings as realized losses to the extent the impairment is related to credit losses. The amount of the impairment of available for sale securities related to other factors is recognized in other comprehensive income (loss). In estimating other-than-temporary impairment losses, management considers, among other things, the length of time and the extent to which the fair value has been less than cost, the financial condition and near-term prospects of the issuer and the intent and ability of the Company to hold the security for a period of time sufficient to allow for any anticipated recovery in fair value. The unrealized losses shown above are primarily due to increases in market rates over the yields available at the time of purchase of the underlying securities and not credit quality. Because the Company does not intend to sell these securities and it is more likely than not that the Company will not be required to sell the securities before recovery of their amortized cost bases, which may be maturity, the Company does not consider these securities to be other than temporarily impaired at December 31, 2022. There were no other-than-temporary impairments for the years ended December 31, 2022, 2021 or 2020.

NOTE 4 – LOANS AND ALLOWANCE FOR LOAN LOSSES

Loans at December 31, 2022 and 2021 were as follows (in thousands):

	December 31, 2022	December 31, 2021
Commercial real estate	$ 1,049,720	$ 825,284
Consumer real estate	402,615	326,412
Construction and land development	229,972	214,310
Commercial and industrial	496,347	497,615
Consumer	53,382	46,811
Other	80,762	55,337
Total	2,312,798	1,965,769
Allowance for loan losses	(23,806)	(21,698)
Total loans, net	$ 2,288,992	$ 1,944,071

Payroll Protection Program Loans

The CARES Act created a new guaranteed, unsecured loan program under the SBA called the Payroll Protection Program (“PPP”), which the Company participates in, to fund operational costs of eligible businesses, organizations and self-employed persons during the pandemic period. The SBA has guaranteed 100% of the amounts loaned under the PPP by lenders to eligible small businesses. One of the notable features of the PPP is that borrowers are eligible for loan forgiveness if certain conditions are met related to retaining staff and if loan amounts are used to cover eligible expenses, such as payroll, mortgage interest, rents and utilities payments. These loans have a two-year term and will earn interest at a rate of 1%. The outstanding balances of loans originated under the PPP as of December 31, 2022 and 2021 totaled $0.2 million and $26.5 million, respectively, and were included in commercial and industrial loans.

Additionally, PPP borrowers are not required to pay any fees to the government or the lender and the loans may be repaid by the borrower at any time. The SBA, however, will pay lenders a processing fee based on the size of the PPP loan, ranging from 1% to 5% of the loan. These fees are deferred and amortized over the life of the loan. PPP fees recognized as income totaled $0.7 million, $7.2 million, and $3.6 million for the years ended December 31, 2022, 2021, and 2020, respectively.

Loans Held for Sale

Included within the balance sheet as of December 31, 2022 the Company had $44.7 million in loans held for sale, which was comprised of $12.6 million in residential mortgage loans and $32.1 million in the guaranteed portion of SBA loans. At December 31, 2021, the Company had $83.7 million in loans held for sale, which was comprised of $40.9 million in Tri-Net commercial real estate loans, $37.3 million in residential mortgage loans, and $7.4 million in the guaranteed portion of SBA loans.

Allowance for Loan Losses

The adequacy of the allowance for loan losses ("ALL") is assessed at the end of each quarter. The ALL includes a specific component related to loans that are individually evaluated for impairment and a general component related to loans that are segregated into homogenous pools and collectively evaluated for impairment. The ALL factors applied to these pools are an estimate of probable incurred losses based on management's evaluation of historical net losses from loans with similar characteristics, which are adjusted by management to reflect current events, trends, and conditions. The adjustments include consideration of the following: changes in lending policies and procedures, economic conditions, nature and volume of the portfolio, experience of lending management, volume and severity of past due loans, quality of the loan review system, value of underlying collateral for collateral dependent loans, concentrations, and other external factors. The Company's evaluation of other external factors included consideration of the novel coronavirus ("COVID-19") global pandemic (including the effects of COVID-19 variants) and the resulting impact on the Company's loan portfolio as of December 31, 2022, which has been uncertain due to evolving conditions and unforeseen new variants. Such factors do not have material impact to our allowance as of December 31, 2022.

At December 31, 2022, variable-rate and fixed-rate loans totaled $934.9 million and $1,377.9 million, respectively. At December 31, 2021, variable-rate and fixed-rate loans totaled $881.1 million and $1,084.7 million, respectively.

The Company categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. The Company analyzes all commercial loans, and consumer relationships with an outstanding balance greater than $500,000, individually and assigns each loan a risk rating. This analysis is performed on a continual basis by the relationship managers and credit department personnel. On at least an annual basis an independent party performs a formal credit risk review of a sample of the loan portfolio. Among other things, this review assesses the appropriateness of the loan's risk rating. The Company uses the following definitions for risk ratings:

Special Mention – A special mention asset possesses deficiencies or potential weaknesses deserving of management's attention. If uncorrected, such weaknesses or deficiencies may expose the Company to an increased risk of loss in the future.

Substandard – A substandard asset is inadequately protected by the current sound net worth and paying capacity of the obligor or of the collateral pledged, if any. Assets so classified must have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the Company will sustain some loss if deficiencies are not corrected. Loss potential, while existing in the aggregate amount of substandard assets, does not have to exist in individual assets classified substandard.

Doubtful – A doubtful asset has all weaknesses inherent in one classified substandard, with the added characteristic that weaknesses make collection or liquidation in full, on the basis of existing facts, conditions, and values, highly questionable and improbable. The probability of loss is extremely high, but certain important and reasonable specific pending factors which may work to the advantage and strengthening of the asset exist, therefore, its classification as an estimated loss is deferred until a more exact status may be determined. Pending factors include proposed merger, acquisition or liquidation procedures, capital injection, perfecting liens on additional collateral, and refinancing plans.

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

Loans not falling into the criteria above are considered to be pass-rated loans. The Company utilizes six loan grades within the pass risk rating.

The following table provides the risk category of loans by applicable class of loans as of December 31, 2022 and 2021 (in thousands):

	Non-impaired Loans					
December 31, 2022	Pass	Special Mention	Substandard	Doubtful	Total Impaired Loans	Total
Commercial real estate	$ 1,036,726	$ 4,731	$ 440	$ —	$ 4,543	$ 1,046,440
Consumer real estate	393,734	555	467	—	367	395,123
Construction and land development	229,897	—	—	—	7	229,904
Commercial and industrial	477,081	516	12,751	127	4,305	494,780
Consumer	52,911	—	84	2	19	53,016
Other	80,504	—	68	—	—	80,572
Purchased Credit Impaired	11,595	68	1,259	41	—	12,963
Total	$ 2,282,448	$ 5,870	$ 15,069	$ 170	$ 9,241	$ 2,312,798
December 31, 2021						
Commercial real estate	$ 802,562	$ 12,921	$ 4,721	$ —	$ 1,151	$ 821,355
Consumer real estate	312,662	475	712	—	909	314,758
Construction and land development	214,209	—	—	—	10	214,219
Commercial and industrial	468,278	9,811	16,952	73	250	495,364
Consumer	45,695	—	56	3	23	45,777
Other	54,959	—	76	—	—	55,035
Purchased Credit Impaired	15,416	—	3,585	260	—	19,261
Total	$ 1,913,781	$ 23,207	$ 26,102	$ 336	$ 2,343	$ 1,965,769

The following tables detail the changes in the ALL for the years ending December 31, 2022, 2021 and 2020 by loan classification (in thousands):

	Commercial real estate	Consumer real estate	Construction and land development	Commercial and industrial	Consumer	Other	Total
Year ended December 31, 2022							
Balance, beginning of period	$ 7,124	$ 2,412	$ 3,769	$ 7,441	$ 397	$ 555	$ 21,698
Charged-off loans	(12)	(8)	—	(205)	(330)	(201)	(756)
Recoveries	225	6	—	33	110	16	390
Provision for loan losses	597	743	61	385	253	435	2,474
Balance, end of period	$ 7,934	$ 3,153	$ 3,830	$ 7,654	$ 430	$ 805	$ 23,806
Year ended December 31, 2021							
Balance, beginning of period	$ 7,349	$ 1,831	$ 3,476	$ 9,708	$ 305	$ 576	$ 23,245
Charged-off loans	(10)	(1)	—	(199)	(210)	(227)	(647)
Recoveries	10	18	—	10	87	41	166
Provision for loan losses	(225)	564	293	(2,078)	215	165	(1,066)
Balance, end of period	$ 7,124	$ 2,412	$ 3,769	$ 7,441	$ 397	$ 555	$ 21,698
Year ended December 31, 2020							
Balance, beginning of period	$ 3,599	$ 1,231	$ 2,058	$ 5,074	$ 222	$ 420	$ 12,604
Charged-off loans	—	(49)	—	(728)	(172)	(277)	(1,226)
Recoveries	10	14	—	235	76	53	388
Provision for loan losses	3,740	635	1,418	5,127	179	380	11,479
Balance, end of period	$ 7,349	$ 1,831	$ 3,476	$ 9,708	$ 305	$ 576	$ 23,245

A breakdown of the ALL and the loan portfolio by loan category at December 31, 2022 and 2021 follows (in thousands):

	Commercial real estate	Consumer real estate	Construction and land development	Commercial and industrial	Consumer	Other	Total
December 31, 2022							
Allowance for Loan Losses:							
Collectively evaluated for impairment	$ 7,934	$ 3,153	$ 3,830	$ 6,909	$ 378	$ 805	$ 23,009
Individually evaluated for impairment	—	—	—	716	—	—	716
Purchased credit impaired	—	—	—	29	52	—	81
Balances, end of period	$ 7,934	$ 3,153	$ 3,830	$ 7,654	$ 430	$ 805	$ 23,806
Loans:							
Collectively evaluated for impairment	$ 1,041,897	$ 394,756	$ 229,897	$ 490,475	$ 52,997	$ 80,572	$2,290,594
Individually evaluated for impairment	4,543	367	7	4,305	19	—	9,241
Purchased credit impaired	3,280	7,492	68	1,567	366	190	12,963
Balances, end of period	$ 1,049,720	$ 402,615	$ 229,972	$ 496,347	$ 53,382	$ 80,762	$2,312,798
December 31, 2021							
Allowance for Loan Losses:							
Collectively evaluated for impairment	$ 7,075	$ 2,211	$ 3,769	$ 7,376	$ 321	$ 555	$ 21,307
Individually evaluated for impairment	—	200	—	—	—	—	200
Purchased credit impaired	49	1	—	65	76	—	191
Balances, end of period	$ 7,124	$ 2,412	$ 3,769	$ 7,441	$ 397	$ 555	$ 21,698
Loans:							
Collectively evaluated for impairment	$ 820,204	$ 313,849	$ 214,209	$ 495,114	$ 45,754	$ 55,035	$1,944,165
Individually evaluated for impairment	1,151	909	10	250	23	—	2,343
Purchased credit impaired	3,929	11,654	91	2,251	1,034	302	19,261
Balances, end of period	$ 825,284	$ 326,412	$ 214,310	$ 497,615	$ 46,811	$ 55,337	$1,965,769

The following table presents the allocation of the ALL for each respective loan category with the corresponding percentage of loans in each category to total loans, net of deferred fees as of December 31, 2022 and 2021. PPP loans included in commercial and industrial loans in the below table do not have a corresponding ALL as they are fully guaranteed by the SBA (dollars in thousands):

	December 31, 2022		December 31, 2021	
	Amount	Percent of total loans	Amount	Percent of total loans
Commercial real estate	$ 7,934	0.34%	$ 7,124	0.36%
Consumer real estate	3,153	0.14%	2,412	0.12%
Construction and land development	3,830	0.17%	3,769	0.19%
Commercial and industrial	7,654	0.33%	7,441	0.38%
Consumer	430	0.02%	397	0.02%
Other	805	0.03%	555	0.03%
Total allowance for loan and lease losses	$ 23,806	1.03%	$ 21,698	1.10%

The following table presents information related to impaired loans, excluding purchased credit impaired ("PCI") loans, for the years ended December 31, 2022 and 2021 (in thousands):

	December 31, 2022			December 31, 2021		
	Recorded investment	Unpaid principal balance	Related allowance	Recorded investment	Unpaid principal balance	Related allowance
With no related allowance recorded:						
Commercial real estate	$ 4,543	$ 4,551	$ —	$ 1,151	$ 1,115	$ —
Consumer real estate	367	393	—	255	281	—
Construction and land development	7	8	—	10	11	—
Commercial and industrial	420	412	—	250	298	—
Consumer	19	19	—	23	23	—
Other	—	—	—	—	—	—
Subtotal	5,356	5,383	—	1,689	1,728	—
With an allowance recorded:						
Commercial real estate	—	—	—	—	—	—
Consumer real estate	—	—	—	654	654	200
Construction and land development	—	—	—	—	—	—
Commercial and industrial	3,885	4,061	716	—	—	—
Consumer	—	—	—	—	—	—
Other	—	—	—	—	—	—
Subtotal	3,885	4,061	716	654	654	200
Total	$ 9,241	$ 9,444	$ 716	$ 2,343	$ 2,382	$ 200

The recorded investment in loans excludes accrued interest receivable and loan origination fees, net due to immateriality. For purposes of this disclosure, the unpaid principal balance is not reduced for partial charge-offs.

The following table presents information related to the average recorded investment and interest income recognized on impaired loans, excluding PCI loans, for the years ended December 31, 2022, 2021 and 2020 (in thousands):

	Year Ended December 31, 2022		Year Ended December 31, 2021		Year Ended December 31, 2019	
	Average recorded investment	Interest income recognized	Average recorded investment	Interest income recognized	Average recorded investment	Interest income recognized
With no related allowance recorded:						
Commercial real estate	$ 4,612	$ 210	$ 1,169	$ 64	$ 1,198	$ 66
Consumer real estate	387	9	577	3	1,975	66
Construction and land development	8	—	12	1	—	—
Commercial and industrial	228	17	263	13	121	1
Consumer	21	1	35	3	8	—
Other	—	—	—	—	—	—
Subtotal	5,256	237	2,056	84	3,302	133
With an allowance recorded:						
Commercial real estate	—	—	—	—	—	—
Consumer real estate	—	—	665	—	—	—
Construction and land development	—	—	—	—	107	—
Commercial and industrial	4,189	422	—	—	—	—
Consumer	—	—	—	—	—	—
Other	—	—	—	—	—	—
Subtotal	4,189	422	665	—	107	—
Total	$ 9,445	$ 659	$ 2,721	$ 84	$ 3,409	$ 133

There was no interest income recognized on a cash basis for impaired loans for the years ended December 31, 2022, 2021 or 2020.

Non-accrual loans and loans past due 90 days still on accrual include both smaller balance homogeneous loans that are collectively evaluated for impairment and individually classified impaired loans. Impaired loans include commercial loans that are individually evaluated for impairment and deemed impaired (i.e., individually classified impaired loans) as well as TDRs for all loan classifications.

The following table presents the aging of the recorded investment in past-due loans as of December 31, 2022 and 2021 by class of loans (in thousands):

December 31, 2022	30 - 59 Days Past Due	60 - 90 Days Past Due	Greater Than 90 Days Past Due	Total Past Due	Loans Not Past Due	Total
Commercial real estate	$ —	$ —	$ 4,982	$ 4,982	$ 1,041,458	$ 1,046,440
Consumer real estate	455	231	190	876	394,247	395,123
Construction and land development	—	—	8	8	229,896	229,904
Commercial and industrial	99	53	4,749	4,901	489,879	494,780
Consumer	181	39	67	287	52,729	53,016
Other	—	—	37	37	80,535	80,572
Purchased credit impaired	194	165	189	548	12,415	12,963
Total	$ 929	$ 488	$ 10,222	$ 11,639	$ 2,301,159	$ 2,312,798
December 31, 2021						
Commercial real estate	$ —	$ —	$ 1,115	$ 1,115	$ 820,240	$ 821,355
Consumer real estate	1,806	—	241	2,047	312,711	314,758
Construction and land development	—	—	11	11	214,208	214,219
Commercial and industrial	57	48	268	373	494,991	495,364
Consumer	164	170	26	360	45,417	45,777
Other	—	—	—	—	55,035	55,035
Purchased credit impaired	302	153	459	914	18,347	19,261
Total	$ 2,329	$ 371	$ 2,120	$ 4,820	$ 1,960,949	$ 1,965,769

The following table presents the recorded investment in non-accrual loans, past due loans over 89 days and accruing and troubled debt restructurings by class of loans as of December 31, 2022 and 2021 (in thousands):

	Non-Accrual	Past Due Over 90 Days and Accruing	Troubled Debt Restructurings
December 31, 2022			
Commercial real estate	$ 4,982	$ —	$ —
Consumer real estate	456	87	—
Construction and land development	8	—	—
Commercial and industrial	4,065	744	344
Consumer	54	14	—
Other	—	37	—
Purchased credit impaired	1,149	143	—
Total	$ 10,714	$ 1,025	$ 344
December 31, 2021			
Commercial real estate	$ —	$ 1,115	$ 1,115
Consumer real estate	1,086	54	654
Construction and land development	11	—	—
Commercial and industrial	324	112	63
Consumer	31	10	—
Other	—	—	—
Purchased credit impaired	1,806	89	—
Total	$ 3,258	$ 1,380	$ 1,832

As of December 31, 2022 and 2021 the Company had recorded investments in TDRs of $0.3 million and $1.8 million, respectively. The Company did not allocate a specific allowance for those loans at December 31, 2022 or 2021 and there were no commitments to lend additional amounts. Loans accounted for as TDR include modifications from original terms such as those due to bankruptcy proceedings, certain modifications of amortization periods or extended suspension of principal payments due to customer financial difficulties. In order to determine whether a borrower is experiencing financial difficulty, an evaluation is performed of the probability that the borrower will be in payment default on any of its debt in the foreseeable future without the modification. This evaluation is performed under the Company's loan policy. Loans accounted for as TDR are individually evaluated for impairment.

The following table presents loans by class modified as TDR that occurred during the year ended December 31, 2022 (in thousands). There were no new TDR loans identified during the year ended December 31, 2021.

	Number of contracts	Pre modification outstanding recorded investment	Post modification outstanding recorded investment, net of related allowance
2022			
Commercial real estate	—	$ —	$ —
Consumer real estate	—	—	—
Construction and land development	—	—	—
Commercial and industrial	1	86	86
Consumer	—	—	—
Other	—	—	—
Total	1	86	86

The TDR which was modified in 2022 is currently over 90 days past due. There were no TDR for which there was a payment default within the twelve months following the modification during the years ended December 31, 2021 or 2020.

A loan is considered to be in payment default once it is 30 days contractually past due under the modified terms.

Acquired Loans

On July 1, 2020, the Company acquired FCB and BOW (see Note 2 for more information). As a result of the acquisitions, the Company recorded loans with a fair value of $294.7 million. Of those loans, $33.6 million were considered to be purchased credit impaired ("PCI") loans, which are loans for which it is probable at the acquisition date that all contractually required payments will not be collected. The remaining loans are considered to be purchased non-impaired loans and their related fair value discount or premium is recognized as an adjustment to yield over the remaining life of each loan.

The following table relates to acquired FCB and BOW PCI loans and summarizes the contractually required payments, which includes principal and interest, expected cash flows to be collected, and the fair value of acquired PCI loans at the acquisition date (in thousands):

	FCB and BOW acquired on July 1, 2020
Contractually required payments	$ 42,443
Nonaccretable difference	4,501
Cash flows expected to be collected at acquisition	37,942
Accretable yield	4,349
Fair value of PCI loans at acquisition date	$ 33,593

The following table relates to acquired FCB and BOW purchased non-impaired loans and provides the contractually required payments, fair value, and estimate of contractual cash flows not expected to be collected at the acquisition date (in thousands):

	FCB and BOW acquired on July 1, 2020
Contractually required payments	$ 296,527
Fair value of acquired loans at acquisition date	260,701
Contractual cash flows not expected to be collected	3,718

The following table presents changes in the carrying value of PCI loans (in thousands):

	For the year ended December 31, 2022	For the year ended December 31, 2021	For the year ended December 31, 2020
Balance at beginning of period	$ 19,261	$ 28,392	$ 1,605
Additions due to the acquisitions	—	—	33,593
Change due to payments received and accretion	(6,217)	(8,940)	(6,806)
Reclassification of discount to allowance for loan losses	(81)	(191)	—
Balance at end of period	$ 12,963	$ 19,261	$ 28,392

The following table presents changes in the accretable yield for PCI loans (in thousands):

	For the year ended December 31, 2022	For the year ended December 31, 2021	For the year ended December 31, 2020
Balance at beginning of period	$ 5,763	$ 4,068	$ 915
Additions due to the acquisitions	—	—	4,349
Accretion	(1,565)	(1,987)	(1,196)
Reclassification from nonaccretable difference	304	1,519	—
Other changes, net	(206)	2,163	—
Balance at end of period	$ 4,296	$ 5,763	$ 4,068

PCI loans had a $0.1 million and $0.2 million impact on the ALL for the years ended December 31, 2022 and 2021, respectively and no impact on the ALL for the year ended December 31, 2020.

NOTE 5 – LOAN SERVICING

Mortgage loans serviced for the Federal Home Loan Mortgage Corporation (“FHLMC”) are not reported as assets. The principal balance of these loans at December 31, 2022 and 2021 was $137.2 million and $154.0 million, respectively. Custodial escrow balances maintained in connection with serviced loans was $0.5 million at December 31, 2022 and 2021.

Activity for loan servicing rights and the related valuation allowance are summarized as follows (in thousands):

	For the year ended December 31, 2022	For the year ended December 31, 2021
Loan servicing rights:		
Balance at beginning of period	$ 1,425	$ 1,634
Additions	29	229
Amortized to offset other noninterest income	(450)	(438)
Balance at end of period	$ 1,004	$ 1,425
Valuation allowance:		
Balance at beginning of period	$ (372)	$ (449)
Additions expensed	—	—
Reductions credited to other noninterest income	47	77
Direct write-downs	—	—
Balance at end of period	$ (325)	$ (372)

NOTE 6 – PREMISES AND EQUIPMENT

Premises and equipment at December 31, 2022 and 2021 are summarized as follows (in thousands):

	Range of useful lives	December 31, 2022	December 31, 2021
Land	Not applicable	$ 6,402	$ 6,630
Buildings	39 years	18,686	18,900
Leasehold improvements	1 to 17 years	1,007	990
Furniture and equipment	1 to 7 years	6,312	5,561
Fixed assets in process	Not applicable	234	20
		32,641	32,101
Less accumulated depreciation and amortization		(7,786)	(6,374)
		$ 24,855	$ 25,727

Premises and equipment depreciation and amortization expense for the years ended December 31, 2022, 2021 and 2020 totaled $1.4 million, $1.5 million and $1.4 million, respectively.

NOTE 7 – LEASES

The Company leases certain premises and equipment under operating leases that expire at various dates, through 2032, and in most instances, include options to renew or extend at market rates and terms. At December 31, 2022, the Company had lease liabilities totaling $11.0 million and right-of-use assets totaling $10.1 million related to these leases. Lease liabilities and right-of-use assets are reflected in other liabilities and other assets, respectively. At December 31, 2022, the weighted average remaining lease term for operating leases was 8.2 years and the weighted average discount rate used in the measurement of operating lease liabilities was 3.39%.

Lease costs were as follows (in thousands):

	December 31, 2022	December 31, 2021	December 31, 2020
Operating lease cost	$ 2,164	$ 2,102	$ 1,946
Short-term lease cost	16	—	—
Variable least cost	—	—	—
Total lease cost	$ 2,180	$ 2,102	$ 1,946

There were no sale and leaseback transactions, leveraged leases, or lease transactions with related parties during the year ended December 31, 2022 or 2021.

A maturity analysis of operating lease liabilities and reconciliation of the undiscounted cash flows to the total operating lease liability is as follows (in thousands):

	December 31, 2022
Lease payments due:	
2023	$ 1,834
2024	1,543
2025	1,549
2026	1,537
2027	1,285
2028 and thereafter	4,967
Total undiscounted cash flows	12,715
Discount on cash flows	(1,738)
Total lease liability	$ 10,977

NOTE 8 – GOODWILL AND INTANGIBLE ASSETS

Goodwill

The change in goodwill during the years ended December 31, 2022 and 2021 was as follows (in thousands):

	2022	2021
Beginning of year	$ 41,068	$ 41,068
Acquired goodwill	—	—
Impairment	—	—
End of year	$ 41,068	$ 41,068

Goodwill represents the excess of the purchase price over the sum of the estimated fair values of the tangible and identifiable intangible assets acquired less the estimated fair value of the liabilities assumed. Goodwill has an indefinite useful life and is evaluated for impairment annually or more frequently if events and circumstances indicate that the asset might be impaired. An impairment loss is recognized to the extent that the carrying amount exceeds the asset's fair value. Qualitative factors are assessed to first determine if it is more likely than not (more than 50%) that the carrying value of goodwill is less than fair value. During the year ended December 31, 2022, qualitative factors indicated it was more likely than not that the carrying value of goodwill was less than fair value, thus there were no indicators of impairment and no quantitative testing was performed.

Intangible assets with definite useful lives are amortized over their estimated useful lives to their estimated residual values. Goodwill is the only intangible asset with an indefinite life on the balance sheet.

Other intangible assets consist of core deposit intangible assets arising from whole bank acquisitions and are amortized on an accelerated method over their estimated useful lives, which range from six to ten years.

Acquired Intangible Assets

Acquired intangible assets at December 31, 2022 and 2021 were as follows (in thousands):

	December 31, 2022		December 31, 2021	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Amortized intangible assets:				
Core deposit intangibles	$ 12,837	$ (7,836)	$ 12,837	$ (6,146)

For the years ended December 31, 2022, 2021 and 2020, amortization expense was $1.7 million, $1.9 million and $1.8 million, respectively.

Estimated amortization expense for each of the next five years is as follows (in thousands):

Year ending December 31:		
2023		1,441
2024		1,192
2025		943
2026		694
2027		445
Thereafter		286
Total	$	5,001

NOTE 9 – OTHER REAL ESTATE OWNED

Other real estate owned activity was as follows (in thousands):

	2022	2021	2020
Beginning balance	$ 266	$ 523	$ 1,044
Additions due to acquisitions	—	—	571
Loans transferred to other real estate owned	—	2,022	452
Direct write-downs	—	—	—
Sales of other real estate owned	(266)	(2,279)	(1,544)
End of year	$ —	$ 266	$ 523

There was no valuation allowance allocated to properties held for the years ended December 31, 2021 and 2020.

(Income) expenses related to other real estate owned during the years ended December 31, 2022, 2021 and 2020, respectively include (in thousands):

	2022	2021	2020
Net gain on sales	$ (102)	$ (49)	$ (273)
Provision for unrealized losses	—	—	—
Operating expenses, net of rental income	—	—	—
Total	$ (102)	$ (49)	$ (273)

NOTE 10 – DEPOSITS

Time deposits that exceed the FDIC deposit insurance limit of $250,000 at December 31, 2022 and 2021 were $379.9 million and $55.4 million, respectively.

Scheduled maturities of time deposits for the next five years and thereafter are as follows (in thousands):

Maturity:		
2023	$	599,018
2024		84,075
2025		15,589
2026		3,478
2027		5,892
Thereafter		644
	$	708,696

At December 31, 2022 and 2021, the Company had $1.0 million and $0.3 million, respectively of deposit accounts in overdraft status that were reclassified to loans in the accompanying balance sheets.

NOTE 11 – SHORT-TERM BORROWINGS AND LONG-TERM DEBT

Short-Term Borrowings

The Company had short-term borrowings from the FHLB totaling $15.0 million as of December 31, 2022. The Company did not have any short-term borrowings as of December 31, 2021. These advances are non-callable; interest payments are due monthly, with principal due at maturity.

The following is a summary of the contractual maturities and average effective rates of outstanding advances (dollars in thousands):

	December 31, 2022		December 31, 2021	
Year	Amount	Interest Rates	Amount	Interest Rates
2023	15,000	4.33%	—	—

Advances from the FHLB are collateralized by investment securities with a market value of $20.3 million, FHLB stock and certain commercial and residential real estate mortgage loans totaling $721.0 million under a blanket mortgage collateral agreement. At December 31, 2022, the amount of available credit from the FHLB totaled $509.4 million.

Subordinated Notes

The Company issued $30.0 million of fixed-to-floating rate subordinated notes during the third quarter of 2020, which were recorded net of issuance costs of $0.6 million, that mature June 30, 2030. Beginning on or after June 30, 2025, the Company may redeem the notes, in whole or in part, at their principal amount plus any accrued and unpaid interest. The notes have a fixed interest rate of 5.25% per annum for the first five years. Thereafter, the interest rate will reset quarterly to an interest rate per annum equal to a benchmark rate (which is expected to be Three-Month Term SOFR) plus 513 basis points. The carrying value of subordinated notes was $29.7 million and $29.5 million at December 31, 2022 and 2021, respectively.

NOTE 12 – ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)

The following were changes in accumulated other comprehensive income (loss) by component, net of tax, for the years ended December 31, 2022 and 2021 (in thousands):

	Unrealized Gains and Losses on Available for Sale Securities
Year Ended December 31, 2022	
Beginning balance	$ (1,270)
Other comprehensive loss before reclassification, net of tax	(48,776)
Amounts reclassified from accumulated other comprehensive loss, net of tax	(6)
Net current period other comprehensive loss	(48,782)
Ending balance	$ (50,052)
Year Ended December 31, 2021	
Beginning balance	$ 7,728
Other comprehensive income before reclassification, net of tax	(8,977)
Amounts reclassified from accumulated other comprehensive loss, net of tax	(21)
Net current period other comprehensive loss	(8,998)
Ending balance	$ (1,270)

The following were significant amounts reclassified out of each component of accumulated other comprehensive income (loss) for the years ended December 31, 2022, 2021 and 2020 (in thousands):

Details about Accumulated Other Comprehensive Income Components	Year Ended December 31, 2022	Year Ended December 31, 2021	Year Ended December 31, 2020	Affected Line Item in the Statement Where Net Income is Presented
Realized losses on cash flow hedges	$ —	$ —	$ (2,466)	Interest expense - savings and money market accounts
	—	—	(213)	Interest expense - Federal Home Loan Bank advances
	$ —	$ —	$ (2,679)	Total
Realized gains on available-for-sale securities	$ 8	$ 28	$ 125	Net gain on sale of securities
	(2)	(7)	(33)	Income tax expense
	$ 6	$ 21	$ 92	Net of tax

NOTE 13 – INCOME TAXES

The components of income tax expense are summarized as follows (in thousands):

	2022	2021	2020
Current:			
Federal	$ 8,956	$ 12,174	$ 8,822
State	327	732	1,552
	9,283	12,906	10,374
Deferred:			
Federal	451	(158)	(3,523)
State	19	(49)	(816)
	470	(207)	(4,339)
Total	$ 9,753	$ 12,699	$ 6,035

A reconciliation of actual income tax expense in the financial statements to the “expected” tax expense (computed by applying the statutory federal income tax rate of 21% to income before income taxes) for the years ended December 31, 2022, 2021 and 2020 is as follows (in thousands):

	2022	2021	2020
Computed tax expense at statutory rate	$ 10,242	$ 12,889	$ 6,454
State income taxes, net of effect of federal income taxes	273	540	582
Tax-exempt interest income	(265)	(294)	(278)
Earnings on bank owned life insurance contracts	(629)	(384)	(186)
Disallowed expenses	61	66	69
Excess tax (benefit) expense related to stock compensation	(45)	(163)	91
Nondeductible acquisition related expenses	—	—	132
CARES act net operating loss carryback	—	—	(772)
Federal tax credits	(421)	(57)	—
Amortization of investment in low-income housing credits	412	56	—
Other	125	46	(57)
Total	$ 9,753	$ 12,699	$ 6,035

The effective tax rate compared favorably to the statutory federal rate of 21% and Tennessee excise tax rate of 6.5% primarily due to investments in qualified municipal securities and company owned life insurance, federal and state tax credits and the recognition of excess tax benefits related to stock compensation, net of the effect of certain non-deductible expenses. During the year ended December 31, 2020, the Company recorded an income tax benefit of $0.8 million related to the permanent tax rate benefit of Net Operating Loss carrybacks as a result of the Coronavirus Aid, Relief, and Economic Security Act ("CARES Act").

Significant items that gave rise to deferred taxes at December 31, 2022 and 2021 were as follows (in thousands):

	December 31, 2022	December 31, 2021
Deferred tax assets:		
Allowance for loan losses	$ 5,525	$ 4,863
Net operating loss carryforward	317	422
Organization and preopening costs	56	158
Stock-based compensation	307	152
Acquired loans	673	769
Accrued contributions	336	297
Acquired deposits	95	214
Accrued compensation	1,001	2,670
Deferred loan fees	2,301	1,004
Unrealized loss on securities available for sale	18,285	1,161
Other	200	215
Deferred tax assets	29,096	11,925
Deferred tax liabilities:		
Depreciation	1,609	1,563
Goodwill	624	465
Partnership investments	826	96
Amortization of core deposit intangible	770	1,136
Other acquired assets	229	337
Other	409	353
Deferred tax liabilities	4,467	3,950
Net deferred tax asset	$ 24,629	$ 7,975

At December 31, 2022, the Company had federal net operating loss carryforwards of approximately $1.5 million, which expire at various dates from 2030 to 2032. Deferred tax assets are fully recognized because the benefits are more likely than not to be realized based on management's estimation of future taxable earnings.

There were no significant unrecognized income tax benefits as of December 31, 2022 or December 31, 2021. As of December 31, 2022 and 2021 the Company had no accrued interest or penalties related to uncertain tax penalties.

NOTE 14 – COMMITMENTS AND CONTINGENCIES

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

The following table sets forth outstanding financial instruments whose contract amounts represent credit risk as of December 31, 2022 and 2021 (in thousands):

	Contract or notional amount	
	December 31, 2022	December 31, 2021
Financial instruments whose contract amounts represent credit risk:		
Unused commitments to extend credit	$ 1,112,950	$ 831,075
Standby letters of credit	7,288	10,623
Total	$ 1,120,238	$ 841,698

The Company is party to litigation and claims arising in the normal course of business. Management believes that the liabilities, if any, arising from such litigation and claims as of December 31, 2022, will not have a material impact on the financial statements of the Company. The Company was notified of a potential operational loss in the amount of $0.7 million during the third quarter of 2022 which was recorded in the quarter. However, as of December 31, 2022 the Company and its legal counsel believe it is more likely than not that the liability will not be payable. Therefore, based on new information since recording the loss, the Company deems this loss recovered and reversed any losses in

the fourth quarter of 2022 previously booked and a loss contingency is not recorded in the Company's liabilities as of December 31, 2022.

NOTE 15 – CONCENTRATION OF CREDIT RISK

Substantially all of the Company’s loans, commitments, and standby letters of credit have been granted to customers in the Company’s market areas. The concentrations of credit by type of loan are set forth in Note 4 to the financial statements.

At December 31, 2022 and 2021, the Company’s cash and due from banks, federal funds sold and interest-bearing deposits in financial institutions aggregated $108.0 million and $358.8 million, respectively, in excess of insured limits of which $99.3 million and $305.7 million, respectively, were due from the Federal Reserve.

NOTE 16 – REGULATORY MATTERS AND RESTRICTIONS ON DIVIDENDS

The Company and the Bank are subject to regulatory capital requirements administered by the Federal Reserve and the Bank is also subject to the regulatory capital requirements of the Tennessee Department of Financial Institutions. Failure to meet capital requirements can initiate certain mandatory – and possibly additional discretionary – actions by regulators that could, in that event, have a material adverse effect on the institutions’ financial statements. The relevant regulations require the Company and the Bank to meet specific capital adequacy guidelines that involve quantitative measures of their assets, liabilities and certain off-balance-sheet items as calculated under regulatory accounting principles. The capital classifications of the Company and the Bank are also subject to qualitative judgments by their regulators about components, risk weightings, and other factors. Those qualitative judgments could also affect the capital status of the Company and the Bank and the amount of dividends the Company and the Bank may distribute. The final rules implementing the Basel Committee on Banking Supervision’s capital guidelines for U.S. Banks (Basel III rules) became effective for the Company on January 1, 2015 with full compliance with all of the requirements being phased in over a multi-year schedule, and fully phased in by January 1, 2019. The net unrealized gain or loss on available for sale securities is not included in computing regulatory capital. Management believes as of December 31, 2022, the Company and the Bank met all regulatory capital adequacy requirements to which they are subject.

The Federal Deposit Insurance Corporation Improvement Act of 1991 establishes a system of “prompt corrective action” to resolve the problems of undercapitalized insured depository institutions. Under this system, federal banking regulators have established five capital categories: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized, although these terms are not used to represent overall financial condition. Federal banking regulators are required to take various mandatory supervisory actions and are authorized to take other discretionary actions with respect to institutions in the three undercapitalized categories. The severity of the action depends upon the capital category in which the institution is placed. For example, institutions in all three undercapitalized categories are automatically restricted from paying distributions and management fees, whereas only an institution that is significantly undercapitalized or critically undercapitalized is restricted in its compensation paid to senior executive officers. Generally, subject to a narrow exception, the banking regulator must appoint a receiver or conservator for an institution that is critically undercapitalized.

At December 31, 2022 and 2021, the Company and the Bank were well capitalized under the regulatory framework for prompt corrective action. There have been no conditions or events subsequent to December 31, 2022 that management believes have changed the Company’s or the Bank’s category.

The Company's and the Bank's capital amounts and ratios are presented in the following table (dollars in thousands):

	Actual		Minimum capital requirement (1)		Minimum to be well-capitalized (2)	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
At December 31, 2022:						
Total capital to risk-weighted assets:						
CapStar Financial Holdings, Inc.	$410,704	14.51%	$226,491	8.0%	N/A	N/A
CapStar Bank	402,453	14.22	226,407	8.0	283,009	10.0
Tier I capital to risk-weighted assets:						
CapStar Financial Holdings, Inc.	356,913	12.61	169,868	6.0	N/A	N/A
CapStar Bank	378,328	13.37	169,805	6.0	226,407	8.0
Common equity Tier 1 capital to risk weighted assets:						
CapStar Financial Holdings, Inc.	356,913	12.61	127,401	4.5	N/A	N/A
CapStar Bank	361,828	12.79	127,354	4.5	183,956	6.5
Tier I capital to average assets:						
CapStar Financial Holdings, Inc.	356,913	11.40	125,202	4.0	N/A	N/A
CapStar Bank	378,328	12.10	125,089	4.0	156,361	5.0
At December 31, 2021:						
Total capital to risk-weighted assets:						
CapStar Financial Holdings, Inc.	$384,116	16.29%	$188,610	8.0%	N/A	N/A
CapStar Bank	370,919	15.74	188,471	8.0	235,589	10.0
Tier I capital to risk-weighted assets:						
CapStar Financial Holdings, Inc.	332,567	14.11	141,458	6.0	N/A	N/A
CapStar Bank	348,902	14.81	141,354	6.0	188,471	8.0
Common equity Tier 1 capital to risk weighted assets:						
CapStar Financial Holdings, Inc.	332,567	14.11	106,093	4.5	N/A	N/A
CapStar Bank	332,402	14.11	106,015	4.5	153,133	6.5
Tier I capital to average assets:						
CapStar Financial Holdings, Inc.	332,567	10.69	124,437	4.0	N/A	N/A
CapStar Bank	348,902	11.23	124,246	4.0	155,308	5.0

(1) For the calendar year 2022, the Company was required to maintain a capital conservation buffer of Tier 1 common equity capital in excess of minimum risk-based capital ratios by at least 2.5% to avoid limits on capital distributions and certain discretionary bonus payments to executive officers and similar employees.

(2) For the Company to be well-capitalized, the Bank must be well-capitalized and the Company must not be subject to any written agreement, order, capital directive, or prompt corrective action directive issued by the Federal Reserve to meet and maintain a specific capital level for any capital measure.

Under Tennessee banking law, the Bank is subject to restrictions on the payment of dividends. Banking regulations limit the amount of dividends that may be paid without prior approval of the Tennessee Department of Financial Institutions. Under these regulations, the amount of dividends that may be paid in any calendar year without prior approval of the Tennessee Department of Financial Institutions is limited to the current year's net income, combined with the retained net income of the preceding two years, subject to the capital requirements described above. The Bank's payment of dividends may also be affected or limited by other factors, such as the requirement to maintain adequate capital above regulatory guidelines. The federal banking agencies have indicated that paying dividends that deplete a depository institution's capital base to an inadequate level would be an unsafe and unsound banking practice. Under the Federal Deposit Insurance Corporation Improvement Act of 1991, a depository institution may not pay any dividends if payment would cause it to become undercapitalized or if it already is undercapitalized. Moreover, the federal agencies have issued policy statements that provide that Company holding companies and insured banks should generally only pay dividends out of current operating earnings.

Based on these regulations, the Bank was eligible to pay $89.9 million and $82.5 million of dividends as of December 31, 2022 and 2021, respectively. The Bank paid the Company $14.1 million of dividends during 2022.

NOTE 17 – STOCK OPTIONS AND RESTRICTED SHARES

On April 23, 2021, the shareholders of CapStar Financial Holdings, Inc. approved the 2021 Stock Incentive Plan (the "Plan"), which replaced the 2016 Stock Incentive Plan. The Plan provides for the grant of stock-based incentives, including stock options, restricted stock units, performance awards and restricted stock, to employees, directors and service providers that are subject to forfeiture until vesting conditions have been satisfied by the award recipient under the terms of the award. The Plan is intended to help align the interests of employees and our shareholders and reward our employees for improved Company performance. The Plan reserved 1,168,543 shares of stock for issuance of stock incentives. Stock incentives include both restricted stock and stock option grants. Total shares issuable under the plan were 1,118,225 at December 31, 2022.

The Company has recognized stock-based compensation expense, within salaries and employee benefits for employees, and within other noninterest expense for directors, in the consolidated statements of income as follows (in thousands):

	For the year ended December 31,		
	2022	2021	2020
Stock-based compensation expense before income taxes	$ 1,355	$ 1,600	$ 1,223
Less: deferred tax benefit	(354)	(418)	(320)
Reduction of net income	$ 1,001	$ 1,182	$ 903

Restricted Shares, Restricted Stock Units, and Performance Stock Units

We grant time-vested restricted stock units and performance stock units to certain key employees and directors under our stock award plan. Compensation expense is recognized over the vesting period of the awards based on the fair value of the stock at the issue date. Awards vest ratably over a two or three-year vesting period depending on the specific award.

Performance stock units vest based upon the attainment of certain performance metrics over a three-year cumulative performance period. Certain of these awards are eligible to receive dividend equivalent shares. The grant date fair value of these awards approximates the market value of the shares. For awards based upon the achievement of the performance goals, the awards are earned ratably from 0% to 188%. If the performance goals are met at the end of the performance period, the award is adjusted to reflect the Company's three-year total shareholder return (TSR) performance relative to a capital market peer group. This TSR modifier cannot cause the award to exceed the maximum of 188%.

The recipients have the right to vote and receive dividends but cannot sell, transfer, assign, pledge, hypothecate, or otherwise encumber the restricted stock until the shares have vested. A summary of the changes in the Company's nonvested stock awards for the years ended December 31, 2022, 2021, and 2020 follows:

	Restricted Shares	Weighted Average Grant Date Fair Value
Year Ended December 31, 2022		
Nonvested at beginning of period	177,020	$ 14.00
Granted	92,212	21.22
Vested	(58,637)	16.34
Forfeited	(40,169)	15.35
Nonvested at end of period	170,426	$ 16.76
Year Ended December 31, 2021		
Nonvested at beginning of period	148,414	$ 14.39
Granted	143,591	14.84
Vested	(91,763)	14.99
Forfeited	(23,222)	14.52
Nonvested at end of period	177,020	$ 14.00
Year Ended December 31, 2020		
Nonvested at beginning of period	84,697	$ 17.44
Granted	144,557	13.73
Vested	(76,715)	16.50
Forfeited	(4,125)	14.45
Nonvested at end of period	148,414	$ 14.39

As of December 31, 2022, there was $1.6 million of total unrecognized compensation cost related to nonvested shares granted under the Plan. The cost is expected to be recognized over a weighted-average period of 1.7 years. The total fair value of shares vested during the years ended December 31, 2022, 2021 and 2020 was $1.0 million, $1.7 million and $1.0 million, respectively.

Stock Options

Option awards are generally granted with an exercise price equal to the fair value of the Company's common stock at the date of grant. Option awards generally have a three year vesting period and a ten year contractual term.

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model that uses the assumptions noted in the table below. Expected volatility is based on calculations performed by management using industry data. The expected term of options granted was calculated using the "simplified" method for plain vanilla options as permitted under authoritative literature. The risk-free 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.

The fair value of options when granted is determined using the following weighted average assumptions as of the grant date. There were no options granted during 2022, 2021, or 2020.

A summary of the activity in stock options for years ended December 31, 2022, 2021, and 2020 follows:

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (years)
Year Ended December 31, 2022			
Outstanding at beginning of period	130,245	$ 11.96	
Granted	—	—	
Exercised	(5,800)	8.79	
Forfeited or expired	—	—	
Outstanding at end of period	124,445	$ 12.11	4.0
Fully vested and expected to vest	124,445	$ 12.11	4.0
Exercisable at end of period	124,445	$ 12.11	4.0
Year Ended December 31, 2021			
Outstanding at beginning of period	226,589	$ 11.73	
Granted	—	—	
Exercised	(96,344)	11.41	
Forfeited or expired	—	—	
Outstanding at end of period	130,245	$ 11.96	4.9
Fully vested and expected to vest	130,245	$ 11.96	4.9
Exercisable at end of period	113,578	$ 11.54	4.5
Year Ended December 31, 2020			
Outstanding at beginning of period	271,202	$ 11.22	
Granted	—	—	
Exercised	(24,613)	6.75	
Forfeited or expired	(20,000)	10.92	
Outstanding at end of period	226,589	$ 11.73	3.9
Fully vested and expected to vest	226,589	$ 11.73	3.9
Exercisable at end of period	193,255	$ 11.19	3.1

Information related to stock options during 2022, 2021 and 2020 follows:

	2022	2021	2020
Intrinsic value of options exercised	$ 71,340	$ 821,174	$ 188,662
Cash received from option exercises	50,982	1,077,489	105,847
Tax benefit realized from option exercises	18,648	148,312	16,524
Weighted average fair value of options granted	—	—	—

As of December 31, 2022, all compensation cost related to stock options granted under the Plan has been recognized.

NOTE 18– EMPLOYMENT CONTRACTS

The Company has entered into employment contracts with certain senior executives with various expiration dates. Most of the contracts have an option for annual renewal by mutual agreement. The agreements specify that in certain terminating events the Company will be obligated to provide certain benefits and pay each of the senior executives severance based on their annual salaries. These terminating events include termination of employment without “Cause” (as defined in the agreements) or in certain other circumstances specified in the agreements.

NOTE 19 – EMPLOYEE BENEFIT PLANS

The Company has a Retirement Savings 401(k) Plan in which employees may participate. The Company has elected a safe harbor 401(k) plan and as such is required to make an annual contribution of 3% of the employees' salaries annually. An employee does not have to contribute to receive the employer contribution. In addition, the Company may make an additional discretionary contribution up to 6% of the employees' salaries annually. For the years ended December 31, 2022, 2021 and 2020, the Company contributed $1.0 million, $1.0 million and $0.8 million respectively, to the 401(k) Plan.

The Company also has a Health Reimbursement Plan in place to offset the cost of healthcare deductibles for employees. At the end of the year, up to one-half of the unused balance in the employee's account will be available for the following year up to a maximum of the deductible for that employee.

NOTE 20 – DERIVATIVE INSTRUMENTS

The Company utilizes interest rate swap agreements as part of its asset liability management strategy to help manage its interest rate risk position. The notional amount of the interest rate swaps does not represent amounts exchanged by the parties. The amount exchanged is determined by reference to the notional amount and the other terms of the individual interest rate swap agreements.

Interest Rate Swaps Designated as Cash Flow Hedges

There were no interest rate swaps designated as cash flow hedges as of December 31, 2022, 2021, or 2020. The company previously terminated an interest rate swap during 2019, which resulted in a termination fee of $1.5 million which continued to be amortized as the corresponding hedged items, consisting of LIBOR-based brokered deposits and FHLB borrowings, were expected to remain outstanding until the initial maturities of the terminated swaps. However, during the year ended December 31, 2020, it was determined that in light of the Company's surplus liquidity position this funding was expected to be terminated at the next renewal date and thus the previously terminated interest rate swaps which had been designated as cash flow hedges were no longer deemed effective, therefore, remaining unrealized losses of $1.9 million included in accumulated other comprehensive income were recognized in net income. There are no unrealized gains or losses on cash flow hedges in accumulated other comprehensive income as of December 31, 2022 or 2021.

Other Interest Rate Swaps

The Company also enters into swaps to facilitate customer transactions and meet their financing needs. Upon entering into these transactions the Company enters into offsetting positions with large U.S. financial institutions in order to minimize market risk to the Company. A summary of the Company's customer related interest rate swaps is as follows (in thousands):

	December 31, 2022		December 31, 2021	
	Notional amount	Estimated fair value	Notional amount	Estimated fair value
Interest rate swap agreements:				
Pay fixed/receive variable swaps	$ 35,641	$ (2,343)	$ 54,055	$ (1,594)
Pay variable/receive fixed swaps	35,641	2,343	54,055	1,594
Total	$ 71,282	$ —	$ 108,110	$ —

Mortgage Banking Derivatives

The Company enters into various derivative agreements with customers in the form of interest-rate lock commitments which are commitments to originate mortgage loans whereby the interest rate on the loan is determined prior to funding and the customers have locked into that interest rate. The derivatives are valued using a model that utilizes market interest rates and other unobservable inputs. Changes in the fair value of these commitments due to fluctuations in interest rates that are to be originated to our loans held for sale portfolio are economically hedged through the use of forward sale commitments of mortgage-backed securities. The gains and losses arising from this derivative activity are reflected in current period earnings under mortgage banking income. Interest rate lock commitments are valued using a model with significant unobservable market parameters. Forward sale commitments are valued based on quoted prices for similar assets in an active market with inputs that are observable.

The net gains (losses) relating to mortgage banking derivative instruments included in mortgage banking income were as follows (dollars in thousands):

	For the year ended December 31, 2022	For the year ended December 31, 2021	For the year ended December 31, 2020
Mortgage loan interest rate lock commitments	$ 690	$ (1,911)	$ 1,959
Mortgage-backed securities forward sales commitments	(187)	466	(478)
Total	$ 503	$ (1,445)	$ 1,481

The amount and fair value of mortgage banking derivatives included in the consolidated balance sheets was as follows (dollars in thousands):

	December 31, 2022		December 31, 2021	
	Notional amount	Estimated fair value	Notional amount	Estimated fair value
Included in other assets:				
Mortgage loan interest rate lock commitments	$ 19,413	$ 6	$ 50,281	$ 696
Mortgage-backed securities forward sales commitments	12,500	27	—	—
Included in other liabilities:				
Mortgage-backed securities forward sales commitments	$ —	$ —	$ 43,000	$ (160)

NOTE 21 – RELATED PARTY

The Company may enter into loan transactions with certain directors, executive officers, significant shareholders, and their affiliates. Such transactions were made in the ordinary course of business on substantially the same terms, including interest rates and collateral, as those prevailing at the same time for comparable transactions with persons not affiliated with the Company, and did not, in the opinion of management, involve more than normal credit risk or present other unfavorable features. None of these loans were impaired at December 31, 2022 or 2021. Activity within these loans during the years ended December 31, 2022 and 2021 was as follows (in thousands):

	Total commitment	Total funded commitment
Year ended December 31, 2022		
Beginning of period	$ 10,577	$ 8,538
New commitments/draw downs	42,625	24,871
Repayments	(439)	(104)
End of period	$ 52,763	$ 33,305
Year ended December 31, 2021		
Beginning of period	$ 18,024	$ 9,782
New commitments/draw downs	1,314	2,896
Repayments	(8,761)	(4,140)
End of period	$ 10,577	$ 8,538

Deposits from directors, executive officers, significant shareholders and their affiliates at December 31, 2022 and 2021 were $30.9 million and $40.8 million, respectively.

NOTE 22 – FAIR VALUE

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

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

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

Level 3: Significant unobservable inputs that reflect a reporting entity's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

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

Investment Securities : The fair values for investment securities are determined by quoted market prices, if available (Level 1). For securities where quoted prices are not available, fair values are calculated based on market prices of similar securities (Level 2), using matrix pricing. Matrix pricing is a mathematical technique commonly used to price debt securities that are not actively traded and values debt securities by relying on quoted prices for the specific securities and the securities' relationship to other benchmark quoted securities (Level 2 inputs). For securities where quoted prices or market prices of similar securities are not available, fair values are calculated using discounted cash flows or other market indicators (Level 3). See below for additional discussion of Level 3 valuation methodologies and significant inputs. The fair values of all securities are determined from third party pricing services without adjustment.

Derivatives-Interest Rate Swaps : The fair values of derivatives are based on valuation models using observable market data as of the measurement date (Level 2). The Company's derivatives are traded in an over-the-counter market where quoted market prices are not always available. Therefore, the fair values of derivatives are determined using quantitative models that utilize multiple market inputs. The inputs will vary based on the type of derivative, but could include interest rates, prices and indices to generate continuous yield or pricing curves, prepayment rates, and volatility factors to value the position. The majority of market inputs are actively quoted and can be validated through external sources, including brokers, market transactions and third-party pricing services. The fair values of all interest rate swaps are determined from third party pricing services without adjustment.

Impaired Loans : The fair value of impaired loans with specific allocations of the allowance for loan losses is generally based on recent appraisals. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the independent appraisers to adjust for differences between the comparable sales and income data available for similar loans and collateral underlying such loans. Such adjustments result in a Level 3 classification of the inputs for determining fair value. Collateral may be valued using an appraisal, net book value per the borrower's financial statements, or aging reports, adjusted or discounted based on management's historical knowledge, changes in market conditions from the time of the valuation, and management's expertise and knowledge of the client and client's business, resulting in a Level 3 fair value classification. Impaired loans are evaluated on at least a quarterly basis for additional impairment and adjusted in accordance with the loan policy.

Other Real Estate Owned : Assets acquired through or instead of loan foreclosure are initially recorded at fair value less costs to sell when acquired, establishing a new cost basis. These assets are subsequently accounted for at lower of cost or fair value less estimated costs to sell. Fair value is commonly based on recent real estate appraisals which are updated no less frequently than annually. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach with data from comparable properties. Adjustments are routinely made in the appraisal process by the independent appraisers to adjust for differences between the comparable sales and income data available. Appraisals may be adjusted or discounted based on management's historical knowledge, changes in market conditions from the time of the valuation, and/or management's expertise and knowledge of the collateral. Such adjustments result in a Level 3 classification of the inputs for determining fair value. Real estate owned properties are evaluated on a quarterly basis for additional impairment and adjusted accordingly. The Company had no other real estate owned carried at fair value at December 31, 2022 or 2021.

Loans Held For Sale: Loans held for sale are carried at either fair value, if elected, or the lower of cost or fair value on a pool-level basis. Origination fees and costs for loans held for sale recorded at lower of cost or market are capitalized in the basis of the loan and are included in the calculation of realized gains and losses upon sale. Origination fees and costs are recognized in earnings at the time of origination for loans held for sale that are recorded at fair value. Fair value is determined using quoted prices for similar assets, adjusted for specific attributes of that loan or other observable market data, such as outstanding commitments from third party investors (Level 2).

Derivatives-Mortgage Loan Interest Rate Lock Commitments: Interest rate lock commitments that relate to the origination of mortgage loans that will be held for sale are recorded at fair value, determined as the amount that would be required to settle each derivative instrument at the balance sheet date. The fair value of the interest rate lock commitment is derived from the fair value of related mortgage loans, which is based on observable market data and includes the expected net future cash flows related to servicing of the loans. In estimating the fair value of an interest rate lock commitment, the Company assigns a probability to the interest rate lock commitment based on an expectation that it will be exercised and the loan will be funded (a "pull through" rate). The expected pull through rates are applied to the fair value of the unclosed mortgage pipeline, resulting in a Level 3 fair value classification. The pull through rate is a statistical analysis of our actual rate lock fallout history to determine the sensitivity of the residential mortgage loan pipeline compared to interest rate changes and other deterministic values. New market prices are applied based on updated loan characteristics and new fallout ratios (i.e., the inverse of the pull through rate) are applied accordingly. Significant increases (decreases) in the pull through rate in isolation result in a significantly higher (lower) fair value measurement. Changes to the fair value of interest rate lock commitments are recognized based on interest rate changes, changes in the probability that the commitment will be exercised, and the passage of time.

Derivatives-Mortgage-Backed Securities Forward Sales Commitments: The Company utilizes mortgage-backed securities forward sales commitments to hedge mortgage loan interest rate lock commitments. Mortgage-backed securities forward sales commitments are recorded at fair value based on quoted prices for similar assets in an active market with inputs that are observable, resulting in a Level 2 fair value classification.

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

	Fair value measurements at December 31, 2022			
	Carrying Value	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Assets:				
Securities available-for-sale:				
U.S. government agency securities	$ 12,902	$ —	$ 12,902	$ —
State and municipal securities	68,312	—	68,312	—
Mortgage-backed securities	244,828	—	244,828	—
Asset-backed securities	3,270	—	3,270	—
Other debt securities	67,104	—	67,104	—
Loans held for sale	12,636	—	12,636	—
Derivative assets:				
Interest rate swaps - customer related	2,343	—	2,343	—
Mortgage loan interest rate lock commitments	6	—	—	6
Mortgage-backed securities forward sales commitments	27	—	27	—
Liabilities:				
Derivative liabilities:				
Derivative Liabilities - customer related	(2,343)	—	(2,343)	—

	Fair value measurements at December 31, 2021			
	Carrying Value	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Assets:				
Securities available-for-sale:				
U.S. government agency securities	$ 11,503	$ —	$ 11,503	$ —
State and municipal securities	82,560	—	82,560	—
Mortgage-backed securities	293,607	—	293,607	—
Asset-backed securities	3,339	—	3,339	—
Other debt securities	68,387	—	68,387	—
Loans held for sale	37,306		37,306	
Derivatives:				
Derivative Liabilities - customer related	1,594	—	1,594	—
Mortgage loan interest rate lock commitments	696	—	—	696
Liabilities:				
Derivatives:				
Derivative Liabilities - customer related	(1,594)	—	(1,594)	—
Mortgage-backed securities forward sales commitments	(160)	—	(160)	—

The table below presents a reconciliation of all assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the years ended December 31, 2022 and 2021 (dollars in thousands):

	Mortgage Loan Interest Rate Lock Commitments	
	2022	2021
Balance of recurring Level 3 assets at January 1st	$ 696	$ 2,607
Total gains or losses for the period:		
Included in mortgage banking income	(690)	(1,911)
Balance of recurring Level 3 assets at December 31st	$ 6	$ 696

The following table presents quantitative information about recurring Level 3 fair value measurements at December 31, 2022 (dollars in thousands).

December 31, 2022	Fair Value	Valuation Technique(s)	Unobservable Input(s)	Range (Weighted-Average)
Assets:				
Non-hedging derivatives:				
Mortgage loan interest rate lock commitments	$ 6	Consensus pricing	Origination pull-through rate	80% - 100% (94%)

December 31, 2021	Fair Value	Valuation Technique(s)	Unobservable Input(s)	Range (Weighted-Average)
Assets:				
Non-hedging derivatives:				
Mortgage loan interest rate lock commitments	$ 696	Consensus pricing	Origination pull-through rate	60% - 98% (80%)

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

	Fair value measurements at December 31, 2022			
	Carrying Value	Quoted prices in active markets for identical assets (level 1)	Significant other observable inputs (level 2)	Significant unobservable inputs (level 3)
Assets:				
Impaired loans:				
Commercial and industrial	$ 3,169	$ —	$ —	$ 3,169

	Fair value measurements at December 31, 2021			
	Carrying Value	Quoted prices in active markets for identical assets (level 1)	Significant other observable inputs (level 2)	Significant unobservable inputs (level 3)
Assets:				
Impaired loans:				
Consumer real estate	$ 454	$ —	$ —	$ 454

The following table presents quantitative information about Level 3 fair value measurements for assets measured at fair value on a nonrecurring basis (dollars in thousands):

December 31, 2022	Fair Value	Valuation Technique(s)	Unobservable Input(s)	Range (Weighted-Average)
Impaired loans:				
Commercial and industrial	$ 3,069	Sales comparison approach	Appraisal discounts	10%
Commercial and industrial	$ 100	Income approach	Fair value discount	9%

December 31, 2021	Fair Value	Valuation Technique(s)	Unobservable Input(s)	Range (Weighted-Average)
Impaired loans:				
Consumer real estate	$ 454	Sales comparison approach	Appraisal discounts	10%

Fair Value of Financial Instruments

The carrying value and estimated fair values of the Company's financial instruments at December 31, 2022 and 2021 were as follows (in thousands):

	December 31, 2022		December 31, 2021		
	Carrying amount	Fair value	Carrying amount	Fair value	Fair value level of input
Financial assets:					
Cash and due from banks, interest-bearing deposits in financial institutions	$ 130,838	$ 130,838	$ 395,225	$ 395,225	Level 1
Federal funds sold	4,467	4,467	19,900	19,900	Level 1
Securities available-for-sale	396,416	396,416	459,396	459,396	Level 2
Securities held-to-maturity	1,240	1,240	1,782	1,830	Level 2
Loans held for sale	44,708	46,585	83,715	84,934	Level 2
Restricted equity securities	16,632	N/A	14,453	N/A	N/A
Loans	2,312,798	2,265,617	1,965,769	1,963,803	Level 3
Accrued interest receivable	10,511	10,511	7,376	7,376	Level 2
Other assets	93,230	93,230	91,064	91,064	Level 2 / Level 3
Financial liabilities:					
Deposits	2,679,819	2,432,740	2,684,281	2,517,856	Level 3
Subordinated notes and Federal Home Loan bank advances and other borrowings	44,666	43,831	29,532	30,477	Level 2
Other liabilities	4,605	4,605	1,842	1,842	Level 3

The methods and assumptions, not previously presented, used to estimate fair values are described as follows:

(a) *Cash and Due from Banks, Interest-Bearing Deposits in Financial Institutions*

For these short-term instruments, the carrying amount is a reasonable estimate of fair value.

(b) *Federal Funds Sold*

Federal funds sold clear on a daily basis. For this reason, the carrying amount is a reasonable estimate of fair value.

(c) *Loans Held for Sal*e

Loans held for sale include residential mortgage loans, the guaranteed portion of SBA loans, and Tri-Net loans. The fair value of residential mortgage and SBA loans held for sale is measured using an exit price notion. The fair value of Tri-Net loans held for sale is measured using an exit price notion in as much as observable market data is available. Where there is no observable market data, the fair value of Tri-Net loans held for sale is estimated using discounted cash flow models. There were no Tri-Net loans held for sale as of December 31, 2022.

(d) *Restricted Equity Securities*

It is not practical to determine the fair value of restricted securities due to restrictions placed on their transferability.

(e) *Loans Held for Investment*

In accordance with the adoption of ASU 2016-01, the fair value of loans is measured using an exit price notion. Fair values for impaired loans are estimated using discounted cash flow models or based on the fair value of the underlying collateral.

(f) *Accrued interest receivable*

The carrying amount of accrued interest approximates fair value.

(g) Other Assets

Included in other assets are bank owned life insurance and certain interest rate swap agreements. The fair values of interest rate swap agreements are based on independent pricing services that utilize pricing models with observable market inputs. For bank owned life insurance, the carrying amount is based on the cash surrender value and is a reasonable estimate of fair value.

(h) Deposits

The fair value of demand deposits, savings accounts and certain money market deposits is the amount payable on demand at the reporting date. The fair value of certificates of deposit is estimated by discounted cash flow models, using current market interest rates offered on certificates with similar remaining maturities.

(i) Federal Home Loan Bank Advances and Other Borrowings

The fair value of fixed rate Federal Home Loan Bank Advances and other borrowings is estimated using discounted cash flow models, using current market interest rates offered on certificates, advances and other borrowings with similar remaining maturities.

(j) Other Liabilities

Included in other liabilities are accrued interest payable and certain interest rate swap agreements. The fair values of interest rate swap agreements are based on independent pricing services that utilize pricing models with observable market inputs. The carrying amounts of accrued interest approximate fair value.

(k) Off-Balance Sheet Instruments

Fair values for off-balance sheet, credit-related financial instruments are based on fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the counterparties' credit standing. The fair value of commitments is not material.

(l) Limitations

Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial instruments. These estimates do not reflect any premium or discount that could result from offering for sale at one time the Company's entire holdings of a particular instrument. Because no market exists for a significant portion of the Company's 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 could significantly affect the estimates.

Fair value estimates are based on estimating 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, fixed assets are not considered financial instruments and their value has not been incorporated into the fair value estimates. In addition, the 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 the estimates.

NOTE 23 – PARENT COMPANY ONLY FINANCIAL INFORMATION

The following information presents the condensed balance sheets of CapStar Financial Holdings, Inc. as of the years ended December 31, 2022 and 2021 (in thousands).

Condensed Balance Sheets

	December 31, 2022	December 31, 2021
Assets		
Cash and cash equivalents	$ 7,346	$ 12,050
Investment in consolidated subsidiary	375,596	396,429
Other assets	932	1,208
Total assets	$ 383,874	$ 409,687
Liabilities and Shareholders' Equity		
Subordinated debt	$ 29,666	$ 29,532
Other liabilities	26	61
Total shareholders' equity	354,182	380,094
Total liabilities and shareholders' equity	$ 383,874	$ 409,687

The following information presents the statements of income, and statements of cash flows of CapStar Financial Holdings, Inc. for the years ended December 31, 2022, 2021 and 2020 (in thousands).

Condensed Income Statements

	Year Ended December 31, 2022	Year Ended December 31, 2021	Year Ended December 31, 2020
Income - dividends from subsidiary	$ 14,100	$ 5,150	$ 4,075
Interest expense subordinated debt	1,575	1,575	792
Other expenses	884	954	1,373
Income (loss) before income taxes and equity in undistributed net income of subsidiary	11,641	2,621	1,910
Income tax benefit	(651)	(645)	(552)
Income before equity in undistributed net income of subsidiary	12,292	3,266	2,462
Equity in undistributed net income of subsidiary	26,725	45,411	22,234
Net income	$ 39,017	$ 48,677	$ 24,696

Condensed Statements of Cash Flow

	Year Ended December 31, 2022	Year Ended December 31, 2021	Year Ended December 31, 2020
Cash flows from operating activities:			
Net income	$ 39,017	$ 48,677	$ 24,696
Adjustments to reconcile net income to net cash used in operating activities:			
Changes in other assets and liabilities	(13,594)	(4,871)	(2,935)
Equity in undistributed net income of subsidiary	(26,725)	(45,411)	(22,234)
Net cash used in operating activities	(1,302)	(1,605)	(473)
Cash flows from investing activities:			
Cash paid for acquisitions	—	—	(27,278)
Dividends received from CapStar Bank	14,100	5,150	4,075
Net cash provided by (used in) investing activities	14,100	5,150	(23,203)
Cash flows from financing activities:			
Issuance of subordinated debt	—	—	29,387
Repurchase of common stock	(9,574)	(462)	(1,437)
Exercise of common stock options and warrants	(79)	858	63
Common stock dividends paid	(7,849)	(5,067)	(4,035)
Net cash (used in) provided by financing activities	(17,502)	(4,671)	23,978
Net (decrease) increase in cash and cash equivalents	(4,704)	(1,126)	302
Cash and cash equivalents at beginning of period	12,050	13,176	12,874
Cash and cash equivalents at end of period	$ 7,346	$ 12,050	$ 13,176

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURES

None.

ITEM 9A. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we conducted an evaluation of the effectiveness of the design and operation of its disclosure controls and procedures (as such term is defined in Exchange Act Rule 13a-15(e)) as of December 31, 2022. Based on that evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures, were effective as of the end of the period covered by this Report.

Changes in Internal Control over Financial Reporting

Material Weakness in Internal Control Over Financial Reporting

A material weakness (as defined in Rule 12b-2 under the Exchange Act) is a deficiency, or combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the Company's annual or interim financial statements will not be prevented or detected on a timely basis.

During the quarter ended September 30, 2022 management reported a material weakness over the design of internal control over financial reporting for our general ledger account balancing made up of the following deficiencies:

1. Insufficient management review over general ledger accounts assigned to the Company's Operations Division led to certain accounts not being appropriately balanced.
2. Inadequate oversight and governance of the Company's general ledger accounts by the Company's Accounting Division led to the insufficient management review being unidentified.

Remediation of Material Weakness

As of the quarter ended December 31, 2022, the material weakness described above has been remediated through the implementation of measures to help ensure that control deficiencies contributing to the material weakness have been remediated. Such measures include assigning each general ledger account an owner and second reviewer, implementing procedures for the Accounting Division to review and attest to each general ledger account, and ensuring our internal audit plans test the effectiveness of our general ledger account oversight. We consider the material weakness remediated as the applicable controls have operated for a sufficient period of time and management has concluded, through testing, that the controls are operating effectively.

There were no changes other than those described above in the Company's internal control over financial reporting (as such term is defined in Exchange Act Rule 13a-15(f)) that occurred during the quarter ended December 31, 2022, that materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Management's Annual Report on Internal Control over Financial Reporting

The management of the Company is responsible for establishing and maintaining adequate internal control over financial reporting. The Company's internal control over financial reporting was designed by, or under the supervision of, the company's principal executive and principal financial officers and effected by the company's board of directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of the Company's financial statements in accordance with U.S. GAAP. Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

As of December 31, 2022, management assessed the effectiveness of the Company's internal control over financial reporting based on the criteria for effective internal control over financial reporting established in "Internal Control-Integrated Framework," issued by the Committee of Sponsoring Organizations ("COSO") of the Treadway

Commission in 2013. Management also conducted an assessment of requirements pertaining to Section 112 of the Federal Deposit Insurance Corporation Improvement Act. This section relates to management's evaluation of internal control over financial reporting, including controls over the preparation of financial statements in accordance with the instructions to the Consolidated Financial Statements for Bank Holding Companies (Form FR Y-9C) and in compliance with laws and regulations. Our evaluation included a review of the documentation of controls, evaluations of the design of the internal control system and tests of the effectiveness of internal controls. Based on such assessment, management determined that, as of December 31, 2022, the Company's internal control over financial reporting was effective.

The effectiveness of the Company's internal control over financial reporting as of December 31, 2022, has been audited by Elliott Davis LLC, an independent registered public accounting firm, as stated in their report included on page **Error! Bookmark not defined.** of this Annual Report on Form 10-K.

ITEM 9B. OTHER INFORMATION

None.

ITEM 9C. DISCLOSURE REGARDING FOREIGN JURISDICTIONS THAT PREVENT INSPECTIONS

Not applicable.

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

(a) Information Regarding Directors and Executive Officers. Information required by this Item 10 regarding our directors, director nominees and executive officers is in the following sections of the 2023 Proxy Statement, each of which is incorporated herein by reference:

- “Director Nominees” under the heading “Proposal 1 – Election of Directors"
- “Corporate Governance” under the heading “Environmental, Social and Governance Framework”; and
- “Executive Officers”

(b) Compliance with Section 16(a) of the Exchange Act. If applicable, information required by this Item 10 regarding compliance with Section 16(a) of the Exchange Act contained under the caption “Delinquent Section 16(a) Reports” in the 2023 Proxy Statement is incorporated herein by reference.

(c) Code of Business Conduct and Ethics. We have adopted a Corporate Code of Ethics (“Code”). This Code is posted on the “Corporate Governance” section of our Internet website at https://ir.capstarbank.com/corporate-governance/highlights.

(d) Procedures for Shareholders to Recommend Director Nominees. There have been no material changes to the procedures by which security holders may recommend nominees to our Board.

(e) Audit Committee Information. Information required by this Item 10 regarding our Audit Committee and our audit committee financial experts is contained under the captions “Committees of our Board” and “Audit Committee,” under the heading "Environmental, Social, and Governance Framework - Corporate Governance" in the 2023 Proxy Statement is incorporated herein by reference.

ITEM 11. EXECUTIVE COMPENSATION

Information required by this Item 11 regarding director and executive officer compensation, the Compensation Committee Report, the risks arising from our compensation policies and practices for employees, pay ratio disclosure, and compensation committee interlocks and insider participation is contained in the following sections of the 2023 Proxy Statement, each of which is incorporated herein by reference:

- “Executive Compensation”;
- “Director Compensation”; and
- “Compensation Committee Interlocks and Insider Participation” under the heading ”Environmental, Social and Governance Framework – Corporate Governance.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

The following table summarizes information concerning the Company's equity compensation plans at December 31, 2022:

Plan Category	Number of shares to be issued upon exercise of outstanding options, warrants and rights (a)	Weighted average exercise price of outstanding options, warrants and rights (b)	Number of shares remaining available for future issuances under equity compensation plans (excluding shares reflected in column (a)) (c)
Equity compensation plans approved by shareholders:			
	124,445	$ 12.11	1,118,225
Equity compensation plans not approved by shareholders	—	—	—
Total	124,445	$ 12.11	1,118,225

Information required by this Item 12 regarding security ownership of certain persons is contained under the heading "Security Ownership of Certain Beneficial Owners and Management" in the 2023 Proxy Statement and is incorporated herein by reference.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

Information required by this Item 13 regarding certain relationships and related transactions is contained under the heading "Certain Relationships and Related Transactions" in the 2023 Proxy Statement and is incorporated herein by reference. Information required by this Item 13 regarding director independence contained under the heading "Environmental, Social and Governance Framework – Corporate Governance" in the 2023 Proxy Statement is incorporated herein by reference.

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

Information required by Item 14 regarding fees we paid to our principal accountant and the pre-approval policies and procedures established by the Audit Committee of our Board contained under the captions "Audit and Non-Audit Fees" and "Pre-Approval Policies and Procedures" under the heading "Proposal 3 – Ratification of the Appointment of the Registered Public Accounting Firm" in the 2023 Proxy Statement is incorporated herein by reference.

PART IV

ITEM 15. EXHIBIT AND FINANCIAL STATEMENT SCHEDULES

(a) The following is a list of documents filed as a part of this Report:

(1) Financial Statements

The following consolidated financial statements of CapStar and its subsidiary and related reports of our independent registered public accounting firm are incorporated into this Item 15 by reference from Part II - Item 8, pages 61 through 112.

Consolidated Balance Sheets as of December 31, 2022 and 2021
Consolidated Statements of Income for the years ended December 2022, 2021, and 2020
Consolidated Statements of Changes in Shareholders' Equity for the years ended December 31, 2022, 2021, 2020
Consolidated Statements of Comprehensive Income for the years ended December 31, 2022, 2021 and 2020
Consolidated Statements of Cash Flows for the years ended December 31, 2022, 2021, 2020
Notes to Consolidated Financial Statements

(2) Financial Statement Schedules. Schedules to the consolidated financial statements are omitted, as the required information is not applicable

(3) Exhibits - The exhibits required to be filed by Item 601 of Regulation S-K are listed in the Exhibit Index immediately preceding the signature pages to this Annual Report on 10-K, which is incorporated herein by this reference.

ITEM 16. FORM 10-K SUMMARY

None.

EXHIBIT INDEX

Exhibit Number	Description
3.1	Charter of CapStar Financial Holdings, Inc. (incorporated by reference herein to Exhibit 3.1 to the Company's Registration Statement on Form S-1 (File Number 333-213367) filed on August 29, 2016)
3.2	Amended and Restated Bylaws of CapStar Financial Holdings, Inc. (incorporated by reference herein to Exhibit 3.1 to the Company's Current Report on Form 8-K on October 28, 2019)
4.1	Form of Common Stock Certificate (incorporated by reference herein to Exhibit 4.1 to Amendment No. 2 to the Company's Registration Statement on Form S-1 (File Number 333-213367) filed on September 20, 2016)
4.2	Description of Registrant's Securities, registered pursuant to Section 12 of the Securities Exchange Act of 1934 (incorporated by reference herein to Exhibit 4.3 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2020 and filed on March 5, 2021.
10.1†	Executive Employment Agreement, dated April 21, 2022, between CapStar Financial Holdings, Inc., CapStar Bank, and Timothy K. Schools (incorporated by reference herein to Exhibit 10.1 to the Company's Current Report on Form 8-K filed on April 26, 2022)
10.2†	Change in Control Agreement, dated April 21, 2022, between CapStar Financial Holdings, Inc., CapStar Bank, and Timothy K. Schools (incorporated by reference herein to Exhibit 10.2 to the Company's Current Report on Form 8-K filed on April 26, 2022)
10.3†	Non-Qualified Stock Option Agreement, dated May 22, 2019, between CapStar Financial Holdings, Inc., CapStar Bank, and Timothy K. Schools (incorporated by reference herein to Exhibit 10.3 to the Company's Quarterly Report on Form 10-Q filed on August 7, 2019)
10.4†	Executive Employment Agreement, dated April 21, 2022, between CapStar Financial Holdings, Inc., CapStar Bank, and Christopher Tietz (incorporated by reference herein to Exhibit 10.2 to the Company's Current Report on Form 8-K filed on April 26, 2022
10.5†	Change in Control Agreement, dated April 21, 2022, between CapStar Financial Holdings, Inc., CapStar Bank, and Christopher Tietz (incorporated by reference herein to Exhibit 10.4 to the Company's Current Report on Form 8-K filed on April 26, 2022
10.6†	CapStar Financial Holdings, Inc. Stock Incentive Plan (incorporated by reference herein to Exhibit 10.5 to the Company's Registration Statement on Form S-1 (File Number 333-213367) filed on August 29, 2016)
10.7†	First Amendment to the CapStar Financial Holdings, Inc. Stock Incentive Plan (incorporated by reference herein to Exhibit 10.1 to the Company's Current Report on Form 8-K filed on May 30, 2017)
10.8†	Second Amendment to the CapStar Financial Holdings, Inc. Stock Incentive Plan (incorporated by reference herein to Appendix A to the Company's Definitive Proxy Statement filed on March 19, 2018)
10.9†	CapStar Financial Holdings, Inc. form of Restricted Stock Agreement (incorporated by reference herein to Exhibit 10.6 to the Company's Registration Statement on Form S-1 (File Number 333-213367) filed on August 29, 2016)

10.10†	CapStar Financial Holdings, Inc. form of Restricted Stock Agreement to replace awards of CapStar Bank Restricted Stock (incorporated by reference herein to Exhibit 10.8 to the Company’s Registration Statement on Form S-1 (File Number 333-213367) filed on August 29, 2016)
10.11†	CapStar Financial Holdings, Inc. form of Non-Qualified Stock Option Agreement (incorporated by reference herein to Exhibit 10.7 to the Company’s Registration Statement on Form S-1 (File Number 333-213367) filed on August 29, 2016)
10.12†	CapStar Financial Holdings, Inc. form of Non-Qualified Stock Option Agreement to replace awards of CapStar Bank Options (incorporated by reference herein to Exhibit 10.9 to the Company’s Registration Statement on Form S-1 (File Number 333-213367) filed on August 29, 2016)
10.13†	Athens Bancshares Corporation 2010 Equity Incentive Plan and related form agreement (incorporated by reference herein to Exhibit 4.5 to the Company’s Registration Statement on Form S-8 (File Number 333-227625) filed on October 1, 2018)
10.14†	CapStar Financial Holdings, Inc. 2021 Stock Incentive Plan (incorporated by reference herein to Appendix A to the Company’s Definitive Proxy Statement filed on March 26, 2021)
10.15†	Employment Agreement Dated June 1, 2022 By and Among CapStar Financial Holdings, CapStar Bank and Michael J. Fowler (incorporated by reference herein to Exhibit 10.1 to the Company’s Current Report on Form 8-K filed on June 6, 2022)
10.16†	Employment Agreement Dated June 1, 2022 By and Among CapStar Financial Holdings, CapStar Bank and John A. Davis (incorporated by reference herein to Exhibit 10.2 to the Company’s Current Report on Form 8-K filed on June 6, 2022)
10.17†	Employment Agreement Dated June 1, 2022 By and Among CapStar Financial Holdings, CapStar Bank and Kevin Lambert (incorporated by reference herein to Exhibit 10.3 to the Company’s Current Report on Form 8-K filed on June 6, 2022)
10.18†	Employment Agreement Dated June 1, 2022 By and Among CapStar Financial Holdings, CapStar Bank and Jennie O'Bryan (incorporated by reference herein to Exhibit 10.4 to the Company’s Current Report on Form 8-K filed on June 6, 2022)
10.19†	Employment Agreement Dated June 1, 2022 By and Among CapStar Financial Holdings, CapStar Bank and Amy Goodin (incorporated by reference herein to Exhibit 10.5 to the Company’s Current Report on Form 8-K filed on June 6, 2022)
10.20†	Change in Control Continuity Agreement Dated June 1, 2022 By and Among CapStar Financial Holdings, CapStar Bank and Michael J. Fowler (incorporated by reference herein to Exhibit 10.6 to the Company’s Current Report on Form 8-K filed on June 6, 2022)
10.21†	Change in Control Continuity Agreement Dated June 1, 2022 By and Among CapStar Financial Holdings, CapStar Bank and John A. Davis (incorporated by reference herein to Exhibit 10.7 to the Company’s Current Report on Form 8-K filed on June 6, 2022)
10.22†	Change in Control Continuity Agreement Dated June 1, 2022 By and Among CapStar Financial Holdings, CapStar Bank and Kevin Lambert (incorporated by reference herein to Exhibit 10.8 to the Company’s Current Report on Form 8-K filed on June 6, 2022)

10.23†	Change in Control Continuity Agreement Dated June 1, 2022 By and Among CapStar Financial Holdings, CapStar Bank and Jennie O'Bryan (incorporated by reference herein to Exhibit 10.9 to the Company's Current Report on Form 8-K filed on June 6, 2022)
10.24†	Change in Control Continuity Agreement Dated June 1, 2022 By and Among CapStar Financial Holdings, CapStar Bank and Amy Goodin (incorporated by reference herein to Exhibit 10.10 to the Company's Current Report on Form 8-K filed on June 6, 2022)
10.25†	Executive Employment Agreement, dated October 28, 2022, between CapStar Financial Holdings, Inc., CapStar Bank, and Kenneth E. Webb (incorporated by reference herein to Exhibit 10.1 to the Company's Current Report on Form 8-K filed on November 3, 2022)
10.26†	Change in Control Continuity Agreement Dated June 1, 2022 By and Among CapStar Financial Holdings, CapStar Bank and Kenneth E. Webb (incorporated by reference herein to Exhibit 10.2 to the Company's Current Report on Form 8-K filed on November 3, 2022)
21.1	Subsidiaries of CapStar Financial Holdings, Inc. (incorporated by reference herein to Exhibit 21.1 to the Company's Annual Report on Form 10-K filed on March 7, 2022)
23.1	Consent of Elliot Davis, LLC*
31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended, adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, as amended.*
31.2	Certification of Chief Financial Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended, adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, as amended.*
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, as amended.**
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, as amended.**
101 INS	Inline XBRL Instance Document - the instance document does not appear in the Interactive Data File because in XBRL tags are embedded within the Inline XBRL document.
101 SCH	Inline XBRL Taxonomy Extension Schema Document
101 CAL	Inline XBRL Taxonomy Calculation Linkbase Document.*
101 LAB	Inline XBRL Taxonomy Labels Linkbase Document.*
101 PRE	Inline XBRL Taxonomy Presentation Linkbase Document.*
101 DEF	Inline XBRL Taxonomy Extension Definition Linkbase Document.*
104	The cover page of CapStar Financial Holdings, Inc.'s Annual Report on Form 10-K for the year ended December 31, 2022, formatted in Inline XBRL

* Filed with this Annual Report on Form 10-K.
** Furnished with this Annual Report on Form 10-K.
† Represents a management contract or a compensatory plan or arrangement.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, as amended, the Registrant has duly caused this Report to be signed on its behalf by the undersigned, thereunto duly authorized.

CAPSTAR FINANCIAL HOLDINGS, INC.

Date: March 3, 2023

By: /s/ Timothy K. Schools
Timothy K. Schools
President and Chief Executive Officer

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

Signature	Title	Date
/s/ Timothy K. Schools Timothy K. Schools	Director, President and Chief Executive Officer (Principal Executive Officer)	March 3, 2023
/s/ Michael J. Fowler Michael J. Fowler	Chief Financial Officer (Principal Financial Officer)	March 3, 2023
/s/ Jeffrey L. Moody Jeffrey L. Moody	Controller (Principal Accounting Officer)	March 3, 2023
/s/ L. Earl Bentz L. Earl Bentz	Director	March 3, 2023
/s/ Sam B. DeVane Sam B. DeVane	Director	March 3, 2023
/s/ Thomas R. Flynn Thomas R. Flynn	Director	March 3, 2023
/s/ Louis A. Green III Louis A. Green III	Director	March 3, 2023
/s/ Valora S. Gurganious Valora S. Gurganious	Director	March 3, 2023
/s/ Myra NanDora Jenne Myra NanDora Jenne	Director	March 3, 2023
/s/ Joelle J. Phillips Joelle J. Phillips	Director	March 3, 2023
/s/ Stephen B. Smith Stephen B. Smith	Director	March 3, 2023
/s/ James S. Turner, Jr. James S. Turner, Jr.	Director	March 3, 2023
/s/ Toby S. Wilt Toby S. Wilt	Director	March 3, 2023

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We Are CapStar

Our Mission

To win long-term relationships and positively impact our customers' lives by setting the standard in ***Guidance***, ***Responsiveness***, ***Flexibility***, and ***Service***.

Our Vision

To be the employer of choice and the go-to financial services provider in the markets we serve.

Our Values

We operate with an owner mindset.
At the root of everything we do, the underlying goal is to produce compound annual returns to shareholders greater than industry and market averages.

We are one team.
We seek what is most beneficial for CapStar, rather than what is best for ourselves or a single group. Individuals alone cannot achieve our ultimate goals.

We follow the Golden Rule.
Treating others as we expect to be treated is the blueprint for every interaction with each other, our customers, and as ambassadors of CapStar in our communities.

Our team plays to win.
We aspire to be the best. Clear goals and objectives guide our purpose. We are driven, focused on continuous improvement, and never satisfied.

Everyone makes an impact.
Diversity and inclusion of people, thoughts, and voices are priorities in every aspect of our company. We strive to recruit and retain highly effective teammates who positively impact our culture and meet company objectives.

We are obsessed with *Wowing!* customers.
We work tirelessly to win each customer. Every day we have a chance to gain a new customer and retain an existing one. The day we forget that we will become just another bank.

Fast is better than slow.
To win, we act fast. We operate with a sense of urgency established by our customer's timeline and need for responsiveness. Our decisions are thorough, but response is rapid.

We celebrate everything!
Large or small, we communicate and celebrate everything. We are passionate about the success of our teammates and customers.

CAPSTAR™
FINANCIAL HOLDINGS, INC.