UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

☒ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the Quarterly Period ended September 30, 2023 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 001-38671

CAPITAL BANCORP INC.
(Exact name of registrant as specified in its charter)

Maryland	**52-2083046**
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)
2275 Research Boulevard Suite 600	
Rockville Maryland	**20850**
(Address of principal executive offices)	(Zip Code)

(301) 468-8848
Registrant's telephone number, including area code

Not Applicable
(Former Name or Former Address, if Changed Since Last Report)

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, par value $0.01 per share	CBNK	NASDAQ Stock Market

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the 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 x 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 x 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 definitions 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	☐	Smaller 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 is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No x

As of November 7, 2023, the Company had 13,894,419 shares of common stock, par value $0.01 per share, outstanding.

Capital Bancorp, Inc. and Subsidiaries
Form 10-Q
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PART I. CONSOLIDATED FINANCIAL INFORMATION
Item 1. CONSOLIDATED FINANCIAL STATEMENTS

Capital Bancorp, Inc. and Subsidiaries

Consolidated Balance Sheets *(unaudited)*

(in thousands except share data)	September 30, 2023	December 31, 2022
Assets		
Cash and due from banks	**$ 13,767**	$ 19,963
Interest-bearing deposits at other financial institutions	**130,428**	39,764
Federal funds sold	**1,957**	20,688
Total cash and cash equivalents	**146,152**	80,415
Investment securities available for sale	**206,055**	252,481
Restricted investments	**4,340**	7,362
Loans held for sale	**4,843**	7,416
U.S. Small Business Administration (“SBA”) Payroll Protection Program (“PPP”) loans receivable, net of fees and costs	**750**	2,163
Portfolio loans receivable, net of deferred fees and costs	**1,861,929**	1,728,592
Less allowance for credit losses	**(28,279)**	(26,385)
Total portfolio loans held for investment, net	**1,833,650**	1,702,207
Premises and equipment, net	**5,297**	3,386
Accrued interest receivable	**11,231**	9,489
Deferred tax asset	**13,644**	13,777
Bank owned life insurance	**37,315**	36,524
Other assets	**9,207**	8,435
Total assets	**$ 2,272,484**	$ 2,123,655
Liabilities		
Deposits		
Noninterest-bearing	**$ 680,803**	$ 674,313
Interest-bearing	**1,287,185**	1,083,759
Total deposits	**1,967,988**	1,758,072
Federal Home Loan Bank advances	**22,000**	107,000
Other borrowed funds	**12,062**	12,062
Accrued interest payable	**5,204**	1,031
Other liabilities	**22,352**	21,475
Total liabilities	**2,029,606**	1,899,640
Stockholders' equity		
Common stock, $.01 par value; 49,000,000 shares authorized; 13,896,062 issued and outstanding at September 30, 2023; 14,138,829 issued and outstanding at December 31, 2022	**139**	141
Additional paid-in capital	**54,549**	58,190
Retained earnings	**206,033**	182,435
Accumulated other comprehensive loss	**(17,843)**	(16,751)
Total stockholders' equity	**242,878**	224,015
Total liabilities and stockholders' equity	**$ 2,272,484**	$ 2,123,655

See accompanying Notes to Unaudited Consolidated Financial Statements

Capital Bancorp, Inc. and Subsidiaries

Consolidated Statements of Income *(unaudited)*

(dollars in thousands except per share data)	Three Months Ended September 30, 2023	Three Months Ended September 30, 2022	Nine Months Ended September 30, 2023	Nine Months Ended September 30, 2022
Interest income				
Loans, including fees	**$ 45,385**	$ 36,451	**$ 129,651**	$ 105,645
Investment securities available for sale	**1,089**	1,362	**3,732**	2,510
Federal funds sold and other	**1,267**	527	**2,854**	1,143
Total interest income	**47,741**	38,340	**136,237**	109,298
Interest expense				
Deposits	**10,703**	1,386	**27,866**	3,234
Borrowed funds	**228**	277	**1,734**	656
Total interest expense	**10,931**	1,663	**29,600**	3,890
Net interest income	**36,810**	36,677	**106,637**	105,408
Provision for credit losses	**2,280**	1,260	**6,802**	4,247
Provision for credit losses on unfunded commitments	**24**	—	**5**	—
Net interest income after provision for credit losses	**34,506**	35,417	**99,830**	101,161
Noninterest income				
Service charges on deposits	**250**	199	**724**	545
Credit card fees	**4,387**	5,524	**13,303**	17,658
Mortgage banking revenue	**1,243**	969	**3,730**	4,312
Other income	**446**	416	**1,282**	1,296
Total noninterest income	**6,326**	7,108	**19,039**	23,811
Noninterest expenses				
Salaries and employee benefits	**12,419**	10,747	**37,116**	31,129
Occupancy and equipment	**1,351**	1,138	**4,100**	3,476
Professional fees	**2,358**	3,848	**7,340**	8,586
Data processing	**6,469**	7,178	**19,558**	22,721
Advertising	**1,565**	1,632	**4,728**	5,494
Loan processing	**426**	625	**1,435**	1,352
Foreclosed real estate expenses (income), net	**1**	—	**7**	(183)
Other operating	**3,457**	2,926	**9,576**	9,804
Total noninterest expenses	**28,046**	28,094	**83,860**	82,379
Income before income taxes	**12,786**	14,431	**35,009**	42,593
Income tax expense	**2,998**	3,336	**8,168**	9,779
Net income	**$ 9,788**	$ 11,095	**$ 26,841**	$ 32,814
Basic earnings per share	**$ 0.70**	$ 0.79	**$ 1.91**	$ 2.34
Diluted earnings per share	**$ 0.70**	$ 0.77	**$ 1.90**	$ 2.29
Weighted average common shares outstanding:				
Basic	**13,932,848**	14,030,408	**14,038,230**	14,008,885
Diluted	**14,023,906**	14,374,980	**14,111,887**	14,328,602

See accompanying Notes to Unaudited Consolidated Financial Statements

Capital Bancorp, Inc. and Subsidiaries

Consolidated Statements of Comprehensive Income *(unaudited)*

(in thousands)	Three Months Ended September 30, 2023	Three Months Ended September 30, 2022	Nine Months Ended September 30, 2023	Nine Months Ended September 30, 2022
Net income	**$ 9,788**	$ 11,095	**$ 26,841**	$ 32,814
Other comprehensive income (loss):				
Unrealized loss on investment securities available for sale	**(1,820)**	(5,684)	**(883)**	(22,026)
Income tax benefit (expense) relating to the items above	**28**	1,437	**(209)**	5,519
Other comprehensive loss	**(1,792)**	(4,247)	**(1,092)**	(16,507)
Comprehensive income	**$ 7,996**	$ 6,848	**$ 25,749**	$ 16,307

See accompanying Notes to Unaudited Consolidated Financial Statements

Capital Bancorp, Inc. and Subsidiaries
Consolidated Statements of Changes in Stockholders' Equity *(unaudited)*

(dollars in thousands)	Common Stock Shares	Common Stock Amount	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Total Stockholders' Equity
Balance, December 31, 2021	**13,962,334**	**$ 140**	**$ 54,306**	**$ 144,533**	**$ (1,076)**	**$ 197,903**
Net income	—	—	—	10,211	—	**10,211**
Unrealized loss on investment securities available for sale, net of income taxes	—	—	—	—	(6,747)	**(6,747)**
Stock options exercised, net of shares withheld for purchase price	27,028	—	339	(95)	—	**244**
Shares issued as compensation	11,158	—	164	—	—	**164**
Stock-based compensation	—	—	417	—	—	**417**
Cash dividends to stockholders ($0.05 per share)	—	—	—	(700)	—	**(700)**
Balance, March 31, 2022	**14,000,520**	**$ 140**	**$ 55,226**	**$ 153,949**	**$ (7,823)**	**$ 201,492**
Net income	—	—	—	11,508	—	**11,508**
Unrealized loss on investment securities available for sale, net of income taxes	—	—	—	—	(5,513)	**(5,513)**
Stock options exercised, net of shares withheld for purchase price	6,638	—	84	(7)	—	**77**
Shares issued as compensation	3,000	—	37	—	—	**37**
Stock-based compensation	—	—	415	—	—	**415**
Cash dividends to stockholders ($0.05 per share)	—	—	—	(700)	—	**(700)**
Balance, June 30, 2022	**14,010,158**	**$ 140**	**$ 55,762**	**$ 164,750**	**$ (13,336)**	**$ 207,316**
Net income	—	—	—	11,095	—	**11,095**
Unrealized loss on investment securities available for sale, net of income taxes	—	—	—	—	(4,247)	**(4,247)**
Stock options exercised, net of shares withheld for purchase price	28,441	—	355	(87)	—	**268**
Shares issued as compensation	—	—	—	—	—	**—**
Stock-based compensation	—	—	415	—	—	**415**
Cash dividends to stockholders ($0.06 per share)	—	—	—	(842)	—	**(842)**
Balance, September 30, 2022	**14,038,599**	**$ 140**	**$ 56,532**	**$ 174,916**	**$ (17,583)**	**$ 214,005**

See accompanying Notes to Unaudited Consolidated Financial Statements

Capital Bancorp, Inc. and Subsidiaries
Consolidated Statements of Changes in Stockholders' Equity *(unaudited)*

(dollars in thousands)	Common Stock Shares	Common Stock Amount	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Total Stockholders' Equity
Balance, December 31, 2022	**14,138,829**	**$ 141**	**$ 58,190**	**$ 182,435**	**$ (16,751)**	**$ 224,015**
Cumulative effect adjustment due to adoption of the CECL standard	—	—	—	(29)	—	**(29)**
Net income	—	—	—	9,735	—	**9,735**
Unrealized gain on investment securities available for sale, net of income taxes	—	—	—	—	2,792	**2,792**
Stock options exercised, net of shares withheld for purchase price	63,064	1	782	(194)	—	**589**
Shares issued as compensation	28,081	—	585	(39)	—	**546**
Stock-based compensation	—	—	438	—	—	**438**
Cash dividends to stockholders ($0.06 per share)	—	—	—	(850)	—	**(850)**
Shares repurchased and retired	(146,937)	(1)	(2,718)			**(2,719)**
Balance, March 31, 2023	**14,083,037**	**$ 141**	**$ 57,277**	**$ 191,058**	**$ (13,959)**	**$ 234,517**
Net income	—	—	—	7,318	—	**7,318**
Unrealized loss on investment securities available for sale, net of income taxes	—	—	—	—	(2,092)	**(2,092)**
Stock options exercised, net of shares withheld for purchase price	34,687	—	429	(6)	—	**423**
Shares issued as compensation	2,097	—	26	(37)	—	**(11)**
Stock-based compensation	—	—	438	—	—	**438**
Cash dividends to stockholders ($0.06 per share)	—	—	—	(843)	—	**(843)**
Shares repurchased and retired	(138,407)	(1)	(2,314)	—	—	**(2,315)**
Balance, June 30, 2023	**13,981,414**	**$ 140**	**$ 55,856**	**$ 197,490**	**$ (16,051)**	**$ 237,435**
Net income	—	—	—	9,788	—	**9,788**
Unrealized loss on investment securities available for sale, net of income taxes	—	—	—	—	(1,792)	**(1,792)**
Stock options exercised, net of shares withheld for purchase price	12,244	—	153	(130)	—	**23**
Stock-based compensation	—	—	441	—	—	**441**
Cash dividends to stockholders ($0.08 per share)	—	—	—	(1,115)	—	**(1,115)**
Shares repurchased and retired	(100,575)	(1)	(1,901)	—	—	**(1,902)**
Balance, September 30, 2023	**13,893,083**	**$ 139**	**$ 54,549**	**$ 206,033**	**$ (17,843)**	**$ 242,878**

See accompanying Notes to Unaudited Consolidated Financial Statements

(in thousands)	Nine Months Ended September 30, 2023	2022
Cash flows from operating activities		
Net income	**$ 26,841**	$ 32,814
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for credit losses	**6,802**	4,247
Provision for credit losses on unfunded commitments	**5**	—
Provision for mortgage put-back reserve, net	**12**	6
Net amortization on investments	**82**	520
Premises and equipment depreciation	**235**	283
Lease asset amortization	**396**	807
Increase in cash surrender value of BOLI	**(791)**	(761)
Executive long-term incentive plan expense	**297**	436
Stock-based compensation expense	**1,317**	1,247
Director and employee compensation paid in Company stock	**535**	201
Deferred income tax (benefit) expense	**(76)**	1,264
Loss on marketable equity securities	**—**	13
Valuation decrease on derivatives	**8**	5
Gain on sale of foreclosed real estate	**—**	(20)
Increase (decrease) in valuation of loans held for sale carried at fair value	**6**	(4,312)
Proceeds from sales of loans held for sale	**144,871**	269,446
Originations of loans held for sale	**(142,304)**	(256,020)
Changes in assets and liabilities:		
(Increase) decrease in accrued interest receivable	**(1,742)**	11
Increase (decrease) in taxes payable	**450**	(282)
Increase in other assets	**(781)**	(1,880)
Increase in accrued interest payable	**4,173**	8
Increase (decrease) in other liabilities	**889**	(2,680)
Net cash provided by operating activities	**41,225**	45,353
Cash flows from investing activities		
Purchases of securities available for sale	**—**	(113,078)
Proceeds from maturities, calls and paydowns of securities available for sale	**45,461**	5,368
Net sales (purchases) of restricted investments	**3,022**	(129)
Net decrease in SBA-PPP loans receivable	**1,413**	105,623
Net increase in portfolio loans receivable	**(139,049)**	(127,356)
Net purchases of premises and equipment	**(2,542)**	(1,020)
Proceeds from sales of foreclosed real estate	**—**	106
Net cash used in investing activities	**(91,695)**	(130,486)

See accompanying Notes to Unaudited Consolidated Financial Statements

(in thousands)	Nine Months Ended September 30, 2023	2022
Cash flows from financing activities		
Net increase (decrease) in:		
Noninterest-bearing deposits	**6,490**	18,383
Interest-bearing deposits	**203,426**	(77,929)
Federal Home Loan Bank repayments	**(85,000)**	—
Dividends paid	**(2,808)**	(2,242)
Repurchase of common stock	**(6,936)**	—
Net proceeds from exercise of stock options	**1,035**	589
Net cash provided by (used for) financing activities	**116,207**	(61,199)
Net increase (decrease) in cash and cash equivalents	**65,737**	(146,332)
Cash and cash equivalents, beginning of year	**$ 80,415**	183,395
Cash and cash equivalents, end of period	**$ 146,152**	$ 37,063
Noncash activities:		
Change in unrealized losses on investments	**$ (883)**	$ (22,026)
Cash paid during the period for:		
Taxes	**$ 7,704**	$ 8,797
Interest	**$ 25,427**	$ 3,882

See accompanying Notes to Unaudited Consolidated Financial Statements

Note 1 - Nature of Business and Basis of Presentation

Nature of operations:

Capital Bancorp, Inc. is a Maryland corporation and the bank holding company (the “Company”) for Capital Bank, N.A. (the “Bank”). The Company's primary operations are conducted by the Bank, which operates branches in Rockville and Columbia, Maryland; Reston, Virginia; and the District of Columbia. The Bank is principally engaged in the business of investing in commercial, real estate, and credit card loans and attracting deposits. The Company originates residential mortgages for sale in the secondary market through Capital Bank Home Loans (“CBHL”), the Bank’s residential mortgage banking arm, and issues credit cards through OpenSky®, a digitally-driven nationwide credit card platform providing secured, partially secured, and unsecured credit solutions.

The Company formed Church Street Capital, LLC (“Church Street Capital”) in 2014 to provide short-term secured real estate financing to Washington, D.C. area investors and developers that may not meet all Bank credit criteria. At September 30, 2023, Church Street Capital had loans totaling $8.0 million with a collectively assessed allowance for credit losses (“ACL”) of $280 thousand. Refer to Note 5 - Portfolio Loans Receivable to the Unaudited Consolidated Financial Statements for further discussion of the consolidated ACL.

In addition, the Company owns all of the stock of Capital Bancorp (MD) Statutory Trust I (the “Trust”). The Trust is a special purpose non-consolidated entity organized for the sole purpose of issuing trust preferred securities.

Basis of presentation:

The accompanying unaudited interim consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) for interim financial information and with rules and regulations of the Securities and Exchange Commission (“SEC”) and include the activity of the Company and its wholly-owned subsidiaries, the Bank and Church Street Capital. The statements do not include all of the information and footnotes required by GAAP for complete financial statements. All adjustments have been made which, in the opinion of management, are necessary for a fair presentation of the results for the interim periods presented. Such adjustments are all of a normal and recurring nature. All significant inter-company accounts and transactions have been eliminated in consolidation. The results of operations for the three and nine months ended September 30, 2023 are not necessarily indicative of the results that may be expected for the full year. These unaudited interim consolidated financial statements should be read in conjunction with the Company’s audited financial statements and the notes thereto as of December 31, 2022, included in the Company’s Annual Report on Form 10-K for the fiscal year ended December 31, 2022.

The Company reports its activities as four business segments: commercial banking; mortgage lending; credit cards; and corporate activities. In determining the appropriateness of segment definition, the Company considers components of the business about which financial information is available and regularly evaluated relative to resource allocation and performance assessment.

Significant accounting policies:

The preparation of consolidated financial statements in accordance with GAAP requires estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses and related disclosures of contingent assets and liabilities. The primary reference point for the estimates is historical experience and assumptions believed to be reasonable regarding the value of certain assets and

Note 1 - Nature of Business and Basis of Presentation (continued)

liabilities that are not readily available from other sources. Estimates are evaluated on an ongoing basis. Actual results may materially differ from these estimates under different assumptions or conditions.

Cash and cash equivalents

For purposes of reporting cash flows, cash and cash equivalents include cash on hand, amounts due from financial institutions, interest-bearing deposits with financial institutions and federal funds sold. Generally, federal funds are sold for one-day periods.

Investment securities

Investment securities are classified as available for sale and carried at fair value with unrealized gains and losses included in stockholders' equity on an after-tax basis. Premiums and discounts on investment securities are amortized or accreted using the interest method. Changes in the fair value of debt securities available for sale are included in stockholders' equity as unrealized gains and losses, net of the related tax effect.

Management evaluates all investments in an unrealized loss position on a quarterly basis, and more frequently when economic or market conditions warrant such evaluation. If the Company has the intent to sell the security or it is more likely than not that the Company will be required to sell the security, the security is written down to fair value and the entire loss is recorded in earnings.

If either of the above criteria is not met, the Company evaluates whether the decline in fair value is the result of credit losses or other factors. In making the assessment, the Company may consider various factors including the extent to which fair value is less than amortized cost, performance on any underlying collateral, downgrades in the ratings of the security by a rating agency, the failure of the issuer to make scheduled interest or principal payments and adverse conditions specifically related to the security. If the assessment indicates that a credit loss exists, the present value of cash flows expected to be collected are compared to the amortized cost basis of the security and any excess is recorded as an ACL, limited by the amount that the fair value is less than the amortized cost basis. Any amount of unrealized loss that has not been recorded through an ACL is recognized in other comprehensive income.

Changes in the ACL are recorded as provision for (or reversal of) credit loss expense. Losses are charged against the ACL when management believes an AFS security is confirmed to be uncollectible or when either of the criteria regarding intent or requirement to sell is met. At September 30, 2023, there was no ACL related to the AFS portfolio.

Loans held for sale

Mortgage loans originated and intended for sale are recorded at fair value, determined individually, as of the balance sheet date. Fair value is determined based on outstanding investor commitments, or in the absence of such commitments, based on current investor yield requirements. Gains and losses on loan sales are determined by the specific-identification method. The Company's current practice is to sell residential mortgage loans on a servicing released basis. Interest on loans held for sale is credited to income based on the principal amounts outstanding.

Upon sale and delivery, loans are legally isolated from the Company and the Company has no ability to restrict or constrain the ability of third-party investors to pledge or exchange the mortgage loans. The Company does not have the entitlement or ability to repurchase the mortgage loans or unilaterally cause third-party investors to put the mortgage loans back to the Company. Unrealized and realized gains on

Note 1 - Nature of Business and Basis of Presentation (continued)

loan sales are determined using the specific-identification method and are recognized through mortgage banking activity in the Consolidated Statements of Income.

The Company elects to measure loans held for sale at fair value to better align reported results with the underlying economic changes in value of the loans on the Company's balance sheet.

U.S. Small Business Administration Paycheck Protection Program

During the global COVID-19 pandemic, pursuant to the CARES Act and the Consolidated Appropriations Act, 2021, the United States Small Business Administration Payroll Protection Program ("SBA-PPP") provided forgivable loans to small businesses to enable them to maintain payroll, hire back employees who had been laid off, and cover overhead. SBA-PPP loans have an interest rate of 1%, have two or five year terms, and carry a 100% guarantee of the SBA. The program ended on May 31, 2021. SBA-PPP loans are eligible to be forgiven by the SBA.

Due to the unique nature of these provisions, SBA-PPP loans have been disclosed as a separate balance sheet item. Origination fees received by the SBA are capitalized into the carrying amount of the loans. The deferred fee income, net of origination costs, is recognized over the life of the loan as an adjustment to yield using the effective interest method. The remaining net deferred income is recognized upon forgiveness of the loan.

Portfolio loans and the allowance for credit losses

Loans are stated at the principal amount outstanding, adjusted for deferred origination fees and costs, discounts on loans acquired, and the ACL. Interest is accrued based on the loan principal balances and stated interest rates. Origination fees and costs are recognized as an adjustment to the related loan yield using approximate interest methods. For credit card loans, loan origination fees and direct loan origination costs are amortized on a straight-line basis over a 12-month period.

Loans are considered past due if the required principal and interest payments have not been received as of the date such payments were due. For reporting purposes, the Company discontinues the accrual of interest at the earlier of the date any portion of the principal and/or interest is 90 days past due, or at such time as we determine that it is probable that not all principal and interest payments will be collected, and that collateral is insufficient to discharge the debt in full. When the interest accrual is discontinued, all unpaid accrued interest is reversed from income. Generally, interest payments on nonaccrual loans are recorded as a reduction of the principal balance. Interest income is subsequently recognized only to the extent cash payments are received in excess of principal due.

Loans are generally charged-off in part or in full when management determines the loan to be uncollectible. Factors for charge-off that may be considered include: repayments deemed to be extended out beyond reasonable time frames, customer bankruptcy and lack of assets, and/or collateral deficiencies.

On January 1, 2023, we adopted Accounting Standards Update ("ASU") 2016-13 "Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments" ("ASU 2016-13"), which replaces the incurred loss methodology for determining our provision for credit losses and ACL with an expected loss methodology that is referred to as the Current Expected Credit Loss model ("CECL"). The measurement of expected credit losses under the CECL methodology is applicable to financial assets measured at amortized cost, including loans receivable and held-to-maturity ("HTM") debt securities. It also applies to off-balance sheet credit exposures not accounted for as insurance (loan

Note 1 - Nature of Business and Basis of Presentation (continued)

commitments, standby letters of credit, financial guarantees, and other similar instruments) and net investments in leases recognized by a lessor in accordance with ASU 2016-02 “Leases (Topic 842)”.

In addition, ASU 2016-13 made changes to the accounting for AFS debt securities. One such change is to require credit-related impairments to be recognized as an ACL rather than as a write-down of the security’s amortized cost basis when the Company does not intend to sell or believes that the Company will be required to sell the securities prior to recovery of the security’s amortized cost basis. The Company adopted ASU 2016-13 using the modified retrospective method. Results for reporting periods beginning after January 1, 2023 are presented under ASU 2016-13 while prior period amounts continue to be reported in accordance with previously applicable GAAP. The Company does not own HTM debt securities. There was no ACL on available for sale securities at September 30, 2023.

The following table illustrates the impact of the adoption of ASC 326, or the CECL standard. The adoption of the standard required an $804 thousand increase in the ACL and a $775 thousand reduction to the reserve for unfunded commitments (“RUC”). The improved precision of the calculation of the historical utilization of unfunded commitments gave rise to the reduction. The net impact of the adoption of the CECL standard to retained earnings was $29 thousand.

	January 1, 2023		
(in thousands)	**Pre-adoption of the CECL standard**	**As Reported Under ASC 326**	**Impact of adoption of the CECL standard**
Assets:			
Real estate:			
Residential	$ 484,735	$ 484,735	$ —
Commercial	664,551	664,551	—
Construction	238,099	238,099	—
Commercial and Industrial	220,221	220,221	—
Credit card, net of reserve	128,434	128,434	—
Other consumer	1,179	1,179	—
Portfolio loans receivable, gross	$ 1,737,219	$ 1,737,219	$ —
Deferred origination fees, net	(8,627)	(8,627)	—
Allowance for credit losses	(26,385)	(27,189)	(804)
Portfolio loans receivable, net	$ 1,702,207	$ 1,701,403	$ (804)
Liabilities: Reserve for unfunded commitments	$ 1,682	$ 907	$ (775)

We maintain an ACL that represents management’s estimate of the expected credit losses and risks inherent in our loan portfolio. The amount of the ACL should not be interpreted as an indication that charge-offs in future periods will necessarily occur in those amounts, or at all. The allowance immediately recognizes lifetime expected credit losses when a financial asset is originated or purchased. The ACL is a valuation account that is deducted from the amortized cost basis of loans to present the net amount expected to be collected on the loans. Loans, or portions thereof, are charged-off against the allowance when they are deemed uncollectible. Factors for charge-off that may be considered include: repayments deemed to be extended out beyond reasonable time frames, customer bankruptcy and lack of assets, and/or collateral deficiencies. Expected recoveries do not exceed the aggregate of amounts previously charged-off and expected to be charged-off.

In determining the ACL, we estimate losses collectively based on quantitative analysis of historical

Note 1 - Nature of Business and Basis of Presentation (continued)

credit losses adjusted for current conditions and reasonable and supportable forecasts of collectability of future cash flows over the remaining term of each financial instrument. The Company has elected to utilize a discounted cash flow methodology for all segments, except for the other consumer portfolio segment, which applies a simplified, remaining life approach. See further detail regarding our forecasting methodology in the “Discounted Cash Flow Method” section below.

Quarterly, the Company utilizes a Qualitative Scorecard to consider the need to qualitatively adjust expected credit loss estimates for information not already captured in the quantitative loss estimation process, which may impact expected credit losses. The Qualitative Scorecard evaluates certain risk environments such as economic conditions, changes in the nature and volume of portfolios, changes in experience, depth, and ability of lending management, changes in volume and severity of past due loans and similar conditions, and changes in the value of underlying collateral. The scorecard results help the Company analyze directional consistency to risk conditions and circumstances that should be considered for each loan segment and to refine its estimates of expected credit losses. As of September 30, 2023, there have been no significant changes applied through the Qualitative Scorecard subsequent to implementation on January 1, 2023.

Purchased Credit Deterioration

Upon adoption of ASU 2016-13, loans which were identified as Purchase Credit Impaired under the incurred loss model are identified as Purchased Credit Deteriorated (“PCD”) loans at January 1, 2023 without reassessment. In future acquisitions, the Company may purchase loans, some of which have experienced more than insignificant credit deterioration since origination. In those cases, the Company will consider certain criteria including days past due, accrual status, risk rating, credit mark, and other relevant factors in assessing whether purchased loans are PCD. PCD loans are recorded at the amount paid and the Company will determine the initial ACL required for PCD assets with no impact to earnings. The loan’s purchase price and ACL is then the initial amortized cost basis for PCD loans. The difference between the initial amortized cost basis and the par value of the loan is a noncredit discount or premium, which is amortized into interest income over the life of the loan. Subsequent to initial recognition, PCD loans are subject to the same interest income recognition and impairment model as non-PCD loans, with changes to the ACL recorded through provision expense.

Discounted Cash Flow Method

The Company uses the discounted cash flow (“DCF”) method to estimate expected credit losses for each portfolio loan segment, with the exception of other consumer loans. For each of these loan segments, the Company generates cash flow projections at the instrument level. Payment expectations are adjusted for estimated prepayment speed and for probability and severity of a loss. The expected credit losses derived from the DCF are estimated over the contractual term of the loans, adjusted for expected prepayments when appropriate. The modeling of expected prepayment speeds is based on historical internal data. The contractual term excludes expected extensions, renewals and modifications.

The Company uses regression analysis of historical internal and peer data to determine suitable portfolio segment level loss drivers to utilize when modeling lifetime probability of default and loss given default. This analysis also determines how expected probability of default and loss given default will react to forecasted levels of the loss drivers.

For the credit card portfolio, a major consideration in the determination of the ACL is our historical loss experience. The Company calculates the credit card ACL collectively, applying segmentation based on collateral positions: secured, partially secured, and unsecured.

Note 1 - Nature of Business and Basis of Presentation (continued)

For all DCF models, the Company has elected to use a four quarter forecast period across all portfolio segments. After the forecasted period, the models will revert to a long run average of each economic factor over four quarters. The Company uses economic projections from reputable and independent third parties to inform its loss driver forecast over the forecast period.

The combination of adjustments for credit expectations (default and loss) and timing expectations (prepayment, curtailment, and time to recovery) produces an expected cash flow stream at the instrument level. An effective interest rate is calculated by the Company, adjusted for any net deferred fees or costs, premium, or discount existing at the origination or acquisition, to produce an instrument-level net present value of expected cash flows. The ACL reflects the difference between the amortized cost basis and the present value of the expected cash flows.

Individual Evaluation

The Company will evaluate individual instruments for expected credit losses when those instruments do not share similar risk characteristics with instruments evaluated on a collective basis. Instruments may be evaluated whether or not there is an expectation of collectability in place. Instruments evaluated individually are not included in the Company’s collective analysis. Collateral dependent or secured loans with respect to which the Company expects repayment to be provided substantially through the operation or sale of the collateral utilize a collateral-based methodology in which ACL is measured based on the difference between the net realizable value of the collateral and the amortized cost basis of the asset as of the measurement date. If the collateral valuation is equal to or greater than amortized cost, no reserve is applied. If a loan is not collateral dependent, the loan will be analyzed based on a forecast of future cash flows.

Credit Losses on Off-Balance Sheet Credit Exposures

The Company’s financial instruments include off-balance sheet credit instruments such as unfunded commitments to make loans, commercial letters of credit issued, and commitments to fund other investments. The Company’s maximum exposure to credit loss in the event of nonperformance by the other party to the financial instrument for off-balance sheet loan commitments is represented by the contractual amount of the credit commitment. Loan commitments and lines of credit are generally made on the same terms, including with regard to collateral, as outstanding loans.

The Company maintains RUC on off-balance sheet credit exposures through a provision reflected in other liabilities. Increases or decreases in the reserve are charged to or released from the provision for credit losses for unfunded commitments in the consolidated statements of income. The provision (credit) for credit losses on off-balance sheet exposures prior to January 1, 2023 was included in other noninterest expense in the consolidated statements of income. The RUC on off-balance credit exposures is estimated by loan segment at each balance sheet date under the current expected credit loss model based on the segment loss factor and the estimated utilization rate of the unfunded commitments. The Company has analyzed its historic funding behavior at the segment level to determine an expected utilization rate.

The above methodology for determining an appropriate ACL is based on a comprehensive analysis of the loan portfolio in accordance with ASC 326. The analysis considers all significant factors that affect the expected collectability of the portfolio and supports the expected credit losses estimated by this process. It is important to recognize that the related process, methodology, and underlying assumptions require a substantial degree of judgment. Additional disclosure on the ACL, and qualitative factors can be found in Part II, Item 1A - Risk Factors and Note 5 - Portfolio Loans Receivable.

Note 1 - Nature of Business and Basis of Presentation (continued)

Credit Losses on SBA-PPP loans and interest receivable

The ACL for SBA-PPP loans was separately evaluated given the explicit government guarantee. The Company has incorporated historical experience with similar SBA guarantees and underwriting adjusted for reasonable and supportable forecasts and concluded the expected credit loss is zero and, therefore, no allowance has been assigned to these loans.

The Company does not measure an ACL on accrued interest receivable balances because these balances are written off as a reduction to interest income when loans are placed on nonaccrual status.

Loan modifications

Effective January 1, 2023, the Company adopted ASU 2022-02 - Financial Instruments - Credit Losses (Topic 326): Troubled Debt Restructurings and Vintage Disclosures. From time to time, the Company may elect to modify the contractual terms of loans to a borrower experiencing financial difficulties as a way to mitigate loss, to proactively work with borrowers in financial difficulty, or to comply with regulations regarding the treatment of certain bankruptcy filing and discharge situations. These modifications may include reductions in the interest rate, payment extensions, forgiveness of principal, forbearance or other actions. Under ASU 2022-02, modifications to a loan for a borrower experiencing financial difficulty that have occurred in the current reporting period, are disclosed along with the impact of the modifications. During the three and nine months ended September 30, 2023, the Company did not have any such modifications.

<u>Premises and equipment</u>

Premises and equipment are stated at cost less accumulated depreciation and amortization. Depreciation and amortization are computed using the straight-line method over the estimated useful life of the related property, generally over two to seven years. Leasehold improvements are amortized over the estimated term of the respective leases, which may include renewal options where management has the positive intent to exercise such options, or the estimated useful lives of the improvements, whichever is less. The costs of major renewals and improvements are capitalized with the corresponding costs associated with amortization or depreciation included as a component of occupancy and equipment expense. Expenditures for maintenance, repairs and minor replacements are charged to noninterest expenses as incurred.

<u>Leases</u>

The Company accounts for leases according to ASU 2016-02, *Leases (Topic 842),* and applies a right-of-use (“ROU”) model that requires a lessee to record, for all leases with a lease term of more than 12 months, an asset representing its right to use the underlying asset and a liability to make lease payments. The Company elected to apply the package of practical expedients permitting entities to not reassess: 1) whether any expired or existing contracts are or contain leases; 2) the lease classification for any expired or existing leases; and 3) initial direct costs for any existing leases. Additionally, as provided by ASU 2016-02, the Company elected not to apply the recognition requirements of ASC 842 to short-term leases, defined as leases with a term of 12 months or less, and to recognize the lease payments in net income on short-term leases on a straight-line basis over the lease term.

Note 1 - Nature of Business and Basis of Presentation (continued)

Derivative financial instruments

The Company enters into commitments to fund residential mortgage loans (interest rate locks) with the intention of selling them in the secondary market. The Company also enters into forward sales agreements for certain funded loans and loan commitments. The Company records unfunded commitments intended for loans held for sale and forward sales agreements at fair value with changes in fair value recorded as a component of mortgage banking revenue. Loans originated and intended for sale in the secondary market are carried at fair value. For pipeline loans which are not pre-sold to an investor, the Company endeavors to manage the interest rate risk on rate lock commitments by entering into forward sale contracts, whereby the Company obtains the right to deliver securities to investors in the future at a specified price. Such contracts are accounted for as derivatives and are recorded at fair value as derivative assets or liabilities, with changes in fair value recorded in mortgage banking revenue.

The Company accounts for derivative instruments and hedging activities according to guidelines established in ASC 815-10, *Accounting for Derivative Instruments and Hedging Activities*, as amended. The Company recognizes all derivatives as either assets or liabilities on the balance sheet and measures those instruments at fair value. Changes in fair value of derivatives designated and accounted for as cash flow hedges, to the extent they are effective as hedges, are recorded in other comprehensive income, net of deferred taxes. Any hedge ineffectiveness would be recognized in the income statement line item pertaining to the hedged item. As of September 30, 2023, there were no derivative instruments held which would require recognition by the Company.

Fair value measurements

Fair value is the price that would be received to sell an asset or paid to transfer a liability in the principal or most advantageous market for an asset or liability in an orderly transaction between market participants at the measurement date. The degree of management judgment involved in determining the fair value of a financial instrument is dependent upon the availability of quoted market prices or observable market inputs. For financial instruments that are traded actively and have quoted market prices or observable market inputs, there is minimal subjectivity involved in measuring fair value. However, when quoted market prices or observable market inputs are not fully available, significant management judgment may be necessary to estimate fair value. In developing our fair value estimates, we endeavor to maximize the use of observable inputs and minimize the use of unobservable inputs.

The fair value hierarchy defines Level 1 valuations as those based on quoted prices (unadjusted) for identical assets or liabilities in active markets. Level 2 valuations include inputs based on quoted prices for similar assets or liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument. Level 3 valuations are based on at least one significant assumption not observable in the market, or significant management judgment or estimation, some of which may be internally developed.

Financial assets that are recorded at fair value on a recurring basis include investment securities available for sale, loans held for sale, and derivative financial instruments. Financial liabilities that are recorded at fair value on a recurring basis are comprised of derivative financial instruments. Additional information is included in Note 8 - Fair Value.

Note 1 - Nature of Business and Basis of Presentation (continued)

Bank-owned life insurance

The Company had $37.3 million of bank-owned life insurance at September 30, 2023 and $36.5 million at December 31, 2022.

The Company recognized income on bank-owned life insurance, which is included in other noninterest income, of $274 thousand for the three months ended September 30, 2023 and $255 thousand for the three months ended September 30, 2022, and recognized $791 thousand for the nine months ended September 30, 2023 and $761 thousand for the nine months ended September 30, 2022.

Income taxes

Deferred tax assets and liabilities are determined based on the difference between the financial statement and tax basis of assets and liabilities, using enacted tax rates in effect for the year in which the differences are expected to reverse. Deferred tax assets are recognized when it is deemed more likely than not that the benefits of such deferred income taxes will be realized.

Earnings per share

Earnings per share is computed by dividing net income available to common stockholders by the weighted average number of shares outstanding. Diluted earnings per share is computed by dividing net income by the weighted average number of common shares outstanding, adjusted for the dilutive effect of stock options and restricted stock using the treasury stock method. At September 30, 2023, there were 282 thousand stock options excluded from the calculation as their effect would have been anti-dilutive, whereas at September 30, 2022 there were 141 thousand such options.

Comprehensive loss

The Company reports as comprehensive loss all changes in stockholders' equity during the year from non-stockholder sources. Other comprehensive loss refers to all components (income, expenses, gains, and losses) of comprehensive loss that are excluded from net income.

The Company's only component of other comprehensive loss is unrealized losses on investment securities available for sale, net of income taxes. Information concerning the Company's accumulated other comprehensive loss as of September 30, 2023 and December 31, 2022 is as follows:

(in thousands)	September 30, 2023	December 31, 2022
Unrealized losses on securities available for sale	$ (23,299)	$ (22,416)
Deferred tax benefit	5,456	5,665
Total accumulated comprehensive loss	$ (17,843)	$ (16,751)

Recently issued accounting pronouncements:

In March 2020, the Financial Accounting Standards Board ("FASB") released ASU 2020-04 - Reference Rate Reform, Topic 848, which provides temporary guidance to ease the potential accounting burden in accounting for, or recognizing the effects of, reference rate reform on financial reporting. The new standard is a result of London Interbank Offered Rate ("LIBOR") likely being discontinued as an available benchmark rate. The standard is elective and provides optional expedients and exceptions for applying GAAP to contracts, hedging relationships, or other transactions that reference LIBOR, or another

Note 1 - Nature of Business and Basis of Presentation (continued)

reference rate expected to be discontinued. The amendments in the update are effective for all entities between March 12, 2020 and an extended sunset date of December 31, 2024 which was extended by ASU 2022-06 issued by FASB in December 2022. The adoption of this guidance is not expected to have a material impact on the Company’s financial statements.

Other accounting standards that have been issued or proposed by the FASB or other standards-setting bodies are not expected to have a material impact on the Company's financial position, results of operations or cash flows.

Reclassifications:

Certain reclassifications have been made to amounts reported in prior periods to conform to the current period presentation. The reclassifications had no material effect on net income or total stockholders' equity.

Subsequent events:

Subsequent events are events or transactions that occur after the balance sheet date but before financial statements are issued. Recognized subsequent events are events or transactions that provide additional evidence about conditions that existed at the date of the balance sheet, including the estimates inherent in the process of preparing financial statements. Non-recognized subsequent events are events that provide evidence about conditions that did not exist at the date of the balance sheet but arose after that date. Management has reviewed events through the date the financial statements were available to be issued and no subsequent events occurred requiring accrual or disclosure.

Note 2 - Cash and Cash Equivalents

Cash and cash equivalents include cash and amounts due from banks, interest-bearing deposits and federal funds sold. The Bank is required by regulations to maintain an average cash reserve balance based on a percentage of deposits; however, on March 15, 2020, the Federal Reserve announced that reserve requirement ratios would be reduced to zero percent effective March 26, 2020, due to economic conditions, which eliminated the reserve requirement for all depository institutions. The reserve requirement is still at zero percent as of September 30, 2023.

Note 3 - Investment Securities

The amortized cost and estimated fair value of investment securities at September 30, 2023 and December 31, 2022 are summarized as follows:

Note 3 - Investment Securities (continued)

(in thousands)	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
September 30, 2023				
U.S. Treasuries	**$ 171,496**	**$ —**	**$ (16,683)**	**$ 154,8**
Municipal	**10,807**	**—**	**(2,890)**	**7,9**
Corporate	**5,000**	**—**	**(660)**	**4,3**
Asset-backed securities	**7,318**	**14**	**(66)**	**7,2**
Mortgage-backed securities	**34,733**	**—**	**(3,014)**	**31,7**
Total	**$ 229,354**	**$ 14**	**$ (23,313)**	**$ 206,0**
December 31, 2022				
U.S. Treasuries	$ 215,486	$ —	$ (16,037)	$ 199,4
Municipal	10,815	—	(2,803)	8,0
Corporate	5,000	—	(400)	4,6
Asset-backed securities	7,970	—	(259)	7,7
Mortgage-backed securities	35,626	—	(2,917)	32,7
Total	$ 274,897	$ —	$ (22,416)	$ 252,4

There were no securities sold during the nine months ended September 30, 2023 or the nine months ended September 30, 2022. There was no ACL on available for sale securities at September 30, 2023.

Information related to unrealized losses in the investment portfolio as of September 30, 2023 and December 31, 2022 is summarized as follows:

	Less than 12 months		12 months or longer		Total	
(in thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
September 30, 2023						
U.S. Treasuries	**$ —**	**$ —**	**$ 154,813**	**$ (16,683)**	**$ 154,813**	**$ (16,68**
Municipal	**—**	**—**	**7,917**	**(2,890)**	**7,917**	**(2,89**
Corporate	**—**	**—**	**4,340**	**(660)**	**4,340**	**(66**
Asset-backed securities	**—**	**—**	**5,297**	**(66)**	**5,297**	**(6**
Mortgage-backed securities	**—**	**—**	**31,719**	**(3,014)**	**31,719**	**(3,01**
Total	**$ —**	**$ —**	**$ 204,086**	**$ (23,313)**	**$ 204,086**	**$ (23,31**
December 31, 2022						
U.S. Treasuries	$ 82,102	$ (1,396)	$ 117,347	$ (14,641)	$ 199,449	$ (16,03
Municipal	1,452	(207)	6,560	(2,596)	8,012	(2,80
Corporate	—	—	4,600	(400)	4,600	(40
Asset-backed securities	6,156	(237)	1,555	(22)	7,711	(25
Mortgage-backed securities	22,067	(1,884)	10,642	(1,033)	32,709	(2,91
Total	$ 111,777	$ (3,724)	$ 140,704	$ (18,692)	$ 252,481	$ (22,41

At September 30, 2023, there were twenty-four treasury securities, ten municipal securities, five corporate securities, nine mortgage-backed securities, and two asset-backed securities that had been in an unrealized loss position for greater than twelve months. At December 31, 2022, there were sixteen treasury securities, seven municipal securities, five corporate securities, one asset-backed security, and three mortgage-backed securities that had been in an unrealized loss position for greater than twelve months. Management believes that all unrealized losses at September 30, 2023 and December 31, 2022

Note 3 - Investment Securities (continued)

resulted from changes in interest rates and current market conditions and not as a result of credit deterioration. Management has the ability and the intent to hold these investment securities until maturity or until they recover in value. Pledged securities totaled $150.0 million at September 30, 2023 and $0 at December 31, 2022.

Contractual maturities of U.S. government and government-sponsored agencies, asset-backed, municipal, corporate and mortgage-backed securities at September 30, 2023 and December 31, 2022 are shown below. Actual maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call premiums or prepayment penalties.

	September 30, 2023		December 31, 2022	
(in thousands)	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Within one year	**$ 40,024**	**$ 39,165**	$ 53,739	$ 53,204
Over one to five years	**110,756**	**98,920**	88,165	82,538
Over five to ten years	**26,223**	**21,524**	79,090	68,805
Over ten years	**10,300**	**7,461**	10,307	7,514
Asset-backed securities[1]	**7,318**	**7,266**	7,970	7,711
Mortgage-backed securities[1]	**34,733**	**31,719**	35,626	32,709
Total	**$ 229,354**	**$ 206,055**	$ 274,897	$ 252,481

[1] Asset-backed and Mortgage-backed securities are due in monthly installments.

Note 4 - SBA-PPP Loans Receivable

SBA-PPP gross loans receivable totaled $0.8 million at September 30, 2023, and $2.2 million at December 31, 2022, and were all rated as pass credits and were not past due, nonaccrual or otherwise impaired. Unearned net fees associated with the SBA-PPP loans amounted to $17 thousand at September 30, 2023 and $31 thousand at December 31, 2022.

SBA-PPP loans generated income of $11 thousand for the three months ended September 30, 2023 and $0.3 million for the three months ended September 30, 2022, of which, earned fees, primarily on loans forgiven by the SBA, represented $9 thousand and $0.2 million of the income, respectively. SBA-PPP loans generated income of $26 thousand for the nine months ended September 30, 2023 and $3.4 million for the nine months ended September 30, 2022, of which, earned fees, primarily on loans forgiven by the SBA, represented $14 thousand and $3.2 million of the income, respectively.

Note 5 - Portfolio Loans Receivable

Major classifications of portfolio loans receivable are as follows:

Portfolio Loan Categories

	September 30, 2023		December 31, 2022	
(in thousands)	Amount	Percent	Amount	Percent
Real estate:				
Residential	**$ 558,147**	**30 %**	$ 484,735	28 %
Commercial	**670,594**	**35 %**	664,551	38 %
Construction	**280,905**	**15 %**	238,099	14 %
Commercial and Industrial	**236,782**	**13 %**	220,221	13 %
Credit card, net of reserve(1)	**122,533**	**7 %**	128,434	7 %
Other consumer	**948**	**— %**	1,179	— %
Portfolio loans receivable, gross	**1,869,909**	**100 %**	1,737,219	100 %
Deferred origination fees, net	**(7,980)**		(8,627)	
Allowance for credit losses	**(28,279)**		(26,385)	
Portfolio loans receivable, net	**$ 1,833,650**		$ 1,702,207	

(1) Credit card loans are presented net of reserve for interest and fees.

The Company makes loans to customers located primarily in the Washington, D.C. and Baltimore, Maryland metropolitan areas. Although the loan portfolio is diversified, its performance is influenced by the regional economy. The Company's loan categories, excluding SBA-PPP loans, previously discussed in Note 4, are described below.

Residential Real Estate Loans. One-to-four family mortgage loans are primarily secured by owner-occupied primary residences and, to a lesser extent, investor-owned residences. Residential loans are originated through the commercial sales teams and Capital Bank Home Loans division. Residential loans also include home equity lines of credit. Owner-occupied residential real estate loans usually have fixed rates for five or seven years and adjust on an annual basis after the initial term based on a typical maturity of 30 years. Investor residential real estate loans are generally based on 25-year terms with a balloon payment due after five years. Generally, the required minimum debt service coverage ratio is 115%.

Commercial Real Estate Loans. Commercial real estate loans are originated on owner-occupied and non-owner-occupied properties. These loans may be adversely affected by conditions in the real estate markets or in the general economy. Business equity lines of credit totaling $14.2 million as of September

Note 5 - Portfolio Loans Receivable (continued)

30, 2023, and $12.3 million as of December 31, 2022, are included in the commercial real estate loan category. Business equity lines of credit are commercial purpose lines of credit primarily secured by the business owners residential properties. Commercial loans that are secured by owner-occupied commercial real estate and primarily collateralized by operating cash flows are also included in this category of loans. As of September 30, 2023, there were approximately $305.8 million of owner-occupied commercial real estate loans, representing approximately 16.4% of the loan portfolio. In prior reporting periods, the Company classified certain commercial real estate loans as owner-occupied that should have been classified as non owner-occupied. For the reporting periods ended December 31, 2022 and March 31, 2023, the Company disclosed owner-occupied commercial real estate loans of $387.7 million and $377.4 million, respectively. Based on the revised classification metrics, the correct amount of owner-occupied commercial real estate loans at December 31, 2022 and March 31, 2023 was $300.8 million and $300.0 million, respectively. Commercial real estate loan terms are generally extended for 10 years or less and amortize generally over 25 years or less. The interest rates on commercial real estate loans generally have initial fixed rate terms that adjust typically at five years. Origination fees are routinely charged for services. Personal guarantees from the principal owners of the business are generally required, supported by a review of the principal owners' personal financial statements and global debt service obligations. The properties securing the portfolio are diverse in type. This diversity may help reduce the exposure to adverse economic events that affect any single industry.

Construction Loans. Construction loans are offered within the Company's Washington, D.C. and Baltimore, Maryland metropolitan operating areas to builders, primarily for the construction of single-family homes and condominium and townhouse conversions or renovations and, to a lesser extent, to individuals. Construction loans typically have terms of 12 to 18 months. The Company frequently transitions the end purchaser to permanent financing or re-underwriting and sale into the secondary market through Capital Bank Home Loans. According to underwriting standards, the ratio of loan principal to collateral value, as established by an independent appraisal, cannot exceed 75% for investor-owned and 80% for owner-occupied properties, although exceptions are sometimes made. Semi-annual stress testing of the construction loan portfolio is conducted, and underlying real estate conditions are monitored as well as trends in sales outcomes versus underwriting valuations as part of ongoing risk management efforts. The borrowers' progress in construction buildout is monitored against the original underwriting guidelines for construction milestones and completion timelines.

Commercial and Industrial. In addition to other loan products, general commercial loans, including commercial lines of credit, working capital loans, term loans, equipment financing, letters of credit and other loan products, are offered, primarily in target markets, and underwritten based on each borrower's ability to service debt from income. These loans are primarily made based on the identified cash flows of the borrower and secondarily, on the underlying collateral provided by the borrower. Most commercial business loans are secured by a lien on general business assets including, among other things, available real estate, accounts receivable, promissory notes, inventory and equipment. Personal guaranties from the borrower or other principal are generally obtained.

Credit Cards. Through the OpenSky® credit card division, the Company offers secured, partially secured, and unsecured credit cards on a nationwide basis to under-banked populations and those looking to rebuild their credit scores through a fully digital and mobile platform. The secured lines of credit are secured by a noninterest-bearing demand account at the Bank in an amount equal to the full credit limit of the credit card. For the partially secured lines of credit, the Bank offers certain customers an unsecured line in excess of their secured line of credit by using a proprietary scoring model, which considers credit score and repayment history (typically a minimum of six months of on-time payments, but ultimately determined on a case-by-case basis). Partially secured and unsecured credit cards are only extended to existing secured card customers who have demonstrated sound credit behaviors.

Note 5 - Portfolio Loans Receivable (continued)

Approximately $98.1 million and $109.4 million in secured and partially secured credit card balances were protected by savings deposits held by the Company as of September 30, 2023 and December 31, 2022, respectively. Unsecured balances were $27.4 million and $26.8 million, respectively, for the same periods.

Other Consumer Loans. To a limited extent and typically as an accommodation to existing customers, personal consumer loans, such as term loans, car loans and boat loans are offered.

Purchased Credit Deterioration. There were no loans purchased with credit deterioration during the three and nine months ended September 30, 2023.

During the three months ended September 30, 2023 the Company recorded a $284 thousand increase to the ACL, reflected in “Other”, from residual non-accretable discounts on acquired loans post CECL adoption. The following tables set forth the changes in the ACL and an allocation of the ACL by loan segment class for the three and nine months ended September 30, 2023 and September 30, 2022.

(in thousands) **Three Months Ended September 30, 2023**	**Beginning Balance, Prior to Adoption of the CECL Standard**	**Impact of Adopting the CECL Standard**	**Other**	**Provision (Release of Provision) for Credit Losses**	**Charge-Offs**	**Recoveries**	**Ending Balance**
Real estate:							
Residential	$ 5,419	$ —	$ 91	$ 269	$ —	$ —	$ 5,7
Commercial	10,188	—	193	(199)	—	39	10,2
Construction	1,868	—	—	383	—	—	2,2
Commercial and Industrial	4,296	—	—	(35)	(77)	11	4,1
Credit card	5,707	—	—	1,870	(1,753)	—	5,8
Other consumer	17	—	—	(8)	—	—	
Total	$ 27,495	$ —	$ 284	$ 2,280	$ (1,830)	$ 50	$ 28,2
Nine Months Ended September 30, 2023							
Real estate:							
Residential	$ 5,481	$ (1,198)	$ 91	$ 1,405	$ —	$ —	$ 5,7
Commercial	8,098	3,941	193	(2,050)	—	39	10,2
Construction	3,782	(1,973)	—	442	—	—	2,2
Commercial and Industrial	2,935	1,073	—	1,186	(1,020)	21	4,1
Credit card	6,078	(1,045)	—	5,827	(5,036)	—	5,8
Other consumer	11	6	—	(8)	—	—	
Total	$ 26,385	$ 804	$ 284	$ 6,802	$ (6,056)	$ 60	$ 28,2

Note 5 - Portfolio Loans Receivable (continued)

(in thousands) **Three Months Ended September 30, 2022**	Beginning Balance	Provision (Release of Provision) for Loan Losses	Charge-Offs	Recoveries	Ending Balance
Real estate:					
Residential	$ 5,863	$ 106	$ —	$ —	$ 5,96
Commercial	8,857	(489)	—	—	8,36
Construction	4,473	(468)	—	—	4,00
Commercial and Industrial	2,457	(262)	—	—	2,19
Credit card	4,759	2,373	(1,596)	8	5,54
Other consumer	10	—	—	—	1
Total	$ 26,419	$ 1,260	$ (1,596)	$ 8	$ 26,09
Nine Months Ended September 30, 2022					
Real estate:					
Residential	$ 5,612	$ 357	$ —	$ —	$ 5,96
Commercial	8,566	(198)	—	—	8,36
Construction	4,699	(694)	—	—	4,00
Commercial and Industrial	2,637	(442)	—	—	2,19
Credit card	3,655	5,226	(3,375)	38	5,54
Other consumer	12	(2)	—	—	1
Total	$ 25,181	$ 4,247	$ (3,375)	$ 38	$ 26,09

The following tables present a summary of loan balances and the related allowance for loan losses summarized by loan category for each impairment method used as of December 31, 2022.

(in thousands)	Allowance for Loan Losses Ending Balance Evaluated for Impairment:		Outstanding Portfolio Loan Balances Evaluated for Impairment:	
December 31, 2022	Individually	Collectively	Individually	Collectively
Real estate:				
Residential	$ —	$ 5,481	$ 4,288	$ 480,447
Commercial	—	8,098	1,563	662,988
Construction	—	3,782	2,837	235,262
Commercial and Industrial	372	2,563	705	219,516
Credit card	—	6,078	—	128,434
Other consumer	—	11	—	1,179
Total	$ 372	$ 26,013	$ 9,393	$ 1,727,826

Note 5 - Portfolio Loans Receivable (continued)

Past due loans, segregated by age and class of loans, as of September 30, 2023 and December 31, 2022 were as follows:

Portfolio Loans Past Due

(in thousands) September 30, 2023	Loans 30-59 Days Past Due	Loans 60-89 Days Past Due	Loans 90 or More Days Past Due	Total Past Due Loans	Current Loans	Total Portfolio Loans	Accruing Loans 90 or More Days Past Due	Nonaccrual Loans
Real estate:								
Residential	$ 1,761	$ 264	$ 11,889	$ 13,914	$ 544,233	$ 558,147	$ —	$ 12,256
Commercial	826	—	582	1,408	669,186	670,594	—	582
Construction	1,512	2,568	2,033	6,113	274,792	280,905	—	2,033
Commercial and Industrial	574	219	353	1,146	235,636	236,782	—	353
Credit card	7,882	7,314	390	15,586	106,947	122,533	390	—
Other consumer	—	—	—	—	948	948	—	—
Total	$ 12,555	$ 10,365	$ 15,247	$ 38,167	$ 1,831,742	$ 1,869,909	$ 390	$ 15,224

December 31, 2022	Loans 30-59 Days Past Due	Loans 60-89 Days Past Due	Loans 90 or More Days Past Due	Total Past Due Loans	Current Loans	Total Portfolio Loans	Accruing Loans 90 or More Days Past Due	Nonaccrual Loans
Real estate:								
Residential	$ 4	$ 142	$ 4,284	$ 4,430	$ 480,305	$ 484,735	$ —	$ 4,288
Commercial	—	—	1,563	1,563	662,988	664,551	—	1,563
Construction	1,164	640	2,837	4,641	233,458	238,099	—	2,837
Commercial and Industrial	117	386	569	1,072	219,149	220,221	—	705
Credit card	8,473	7,455	363	16,291	112,143	128,434	363	—
Other consumer	—	—	—	—	1,179	1,179	—	—
Total	$ 9,758	$ 8,623	$ 9,616	$ 27,997	$ 1,709,222	$ 1,737,219	$ 363	$ 9,393

There were $8.8 million and $1.3 million of loans secured by one-to-four family residential properties in the process of foreclosure as of September 30, 2023 and December 31, 2022, respectively.

The following presents the nonaccrual loans as of September 30, 2023 and December 31, 2022:

	September 30, 2023				December 31, 2022
(in thousands)	Nonaccrual with No Allowance for Credit Loss	Nonaccrual with an Allowance for Credit Loss	Total Nonaccrual Loans	Interest Recognized on Nonaccrual Loans	Total Nonaccrual Loans
Real estate:					
Residential	$ 11,653	$ 603	$ 12,256	$ 340	$ 4,288
Commercial	582	—	582	71	1,563
Construction	2,033	—	2,033	82	2,837
Commercial and Industrial	278	75	353	53	705
Total	$ 14,546	$ 678	$ 15,224	$ 546	$ 9,393

The Company has certain loans for which repayment is dependent upon the operation or sale of collateral, as the borrower is experiencing financial difficulty. The underlying collateral can vary based upon the type of loan. The following provides more detail about the types of collateral that secure

Note 5 - Portfolio Loans Receivable (continued)

collateral dependent loans:

- Residential real estate loans are primarily secured by owner-occupied primary residences and, to a lesser extent, investor-owned residences.
- Commercial real estate loans can be secured by either owner-occupied commercial real estate or non-owner occupied investment commercial real estate. Typically, owner occupied commercial real estate loans are secured by office buildings, warehouses, manufacturing facilities and other commercial and industrial properties occupied by operating companies. Non-owner occupied commercial real estate loans are generally secured by office buildings and complexes, retail facilities, multifamily complexes, land under development, industrial properties, as well as other commercial or industrial real estate.
- Construction loans are typically secured by owner occupied commercial real estate or non-owner occupied investment real estate. Typically, owner occupied construction loans are secured by office buildings, warehouses, manufacturing facilities, and other commercial and industrial properties that are in process of construction. Non-owner occupied commercial construction loans are generally secured by office buildings and complexes, multi-family complexes, land under development, and other commercial and industrial real estate in process of construction.
- Commercial and industrial loans are generally secured by equipment, inventory, accounts receivable, and other commercial property.

Collateral dependent loans amortized cost

(in thousands)	September 30, 2023
Real estate:	
Residential	$ 12,364
Commercial	2,127
Construction	79
Commercial and Industrial	318
Total	$ 14,888

Of the collateral dependent loans as of September 30, 2023, a specific reserve of $12 thousand was assessed for commercial and industrial loans.

Prior to the adoption of the CECL standard, loans were considered impaired when, based on current information, management believed the Company would not collect all principal and interest payments according to contractual terms. Generally, loans were reviewed for impairment when the risk grade for a loan was downgraded to a classified asset category. For loans that were classified as impaired, an allowance was established when the collateral value, if the loan was collateral dependent, or the discounted cash flows of the impaired loan was lower than the carrying value of the loan. Loans were

Note 5 - Portfolio Loans Receivable (continued)

generally charged-off in part or in full when management determined the loan to be uncollectible.

Impaired portfolio loans for the period ended December 31, 2022 were as follows:

(in thousands) December 31, 2022	Unpaid Contractual Principal Balance	Recorded Investment With No Allowance	Recorded Investment With Allowance	Total Recorded Investment	Related Allowance	Average Recorded Investment Year to Date	Interest Recognized Year to Date
Real estate:							
Residential	$ 4,476	$ 4,288	$ —	$ 4,288	$ —	$ 4,629	$ 149
Commercial	1,647	1,563	—	1,563	—	1,656	52
Construction	2,939	2,837	—	2,837	—	2,938	75
Commercial and Industrial	899	247	458	705	372	1,199	77
Total	$ 9,961	$ 8,935	$ 458	$ 9,393	$ 372	$ 10,422	$ 353

The following tables summarize interest recognized on impaired loans for the period ended September 30, 2022:

Interest Recognized on Impaired Portfolio Loans

	For the For the Three Months Ended September 30, 2022		For the For the Nine Months Ended September 30, 2022	
(in thousands)	Average Recorded Investment	Interest Recognized	Average Recorded Investment	Interest Recognized
Real estate:				
Residential	**$ 3,329**	**$ —**	**$ 3,341**	**$ —**
Commercial	**1,643**	**—**	**1,650**	**—**
Construction	**2,939**	**—**	**2,938**	**—**
Commercial and Industrial	**1,242**	**—**	**1,267**	**—**
Total	**$ 9,153**	**$ —**	**$ 9,196**	**$ —**

Credit quality indicators

As part of the ongoing monitoring of the credit quality of the Company’s loan portfolio, management tracks certain credit quality indicators including trends related to the risk grade of loans, the level of classified loans, net charge-offs, nonperforming loans, and general economic conditions in the Company’s market. From a credit risk standpoint, the Company utilizes a risk grading matrix to assign a risk grade to each of its loans. The classifications of loans reflect a judgment about the risk of expected credit loss associated with each loan. Credit quality indicators are reviewed and adjusted regularly to account for the degree of risk and expected credit loss that the Company believes to be appropriate for each financial asset.

A description of the general characteristics of loans characterized as classified is as follows:

Pass

Loans characterized as pass includes loans graded exceptional, very good, good, satisfactory and pass/watch. The Company believes that there is a low likelihood of credit deterioration related to those loans that are considered pass.

Note 5 - Portfolio Loans Receivable (continued)

Special mention

A special mention loan has potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the asset or in the Company's credit position at some future date. Special mention loans are not adversely classified and do not expose the Company to sufficient risk to warrant adverse classification.

Borrowers may exhibit poor liquidity and leverage positions resulting from generally negative cash flow or negative trends in earnings. Access to alternative financing may be limited to finance companies for business borrowers and may be unavailable for commercial real estate borrowers.

Substandard

A substandard loan is inadequately protected by the current financial condition and paying capacity of the obligor or of the collateral pledged, if any. Substandard loans 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 the deficiencies are not corrected.

Borrowers may exhibit recent or unexpected unprofitable operations, an inadequate debt service coverage ratio, or marginal liquidity and capitalization. These loans require more intense supervision by Company management.

Doubtful

A doubtful loan has all the weaknesses associated with a substandard loan with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable.

The following table presents the balances of classified loans based on the most recent credit quality indicator analysis. Classified loans include Special Mention, Substandard and Doubtful loans. Pass classified loans include loans graded exceptional, very good, good, satisfactory, and pass/watch. Credit card loans are ungraded as they are not individually graded. Charge-offs presented represent gross charge-offs recognized in the current period:

Note 5 - Portfolio Loans Receivable (continued)

September 30, 2023	Term Loans by Origination Year							
(in thousands)	**2023**	**2022**	**2021**	**2020**	**2019**	**Prior**	**Revolving**	**Total**
Residential – Real estate								
Pass	$ 110,131	$ 139,619	$ 80,143	$ 79,163	$ 39,069	$ 92,404	$ —	$ 540,529
Special Mention	—	—	135	3,693	—	519	—	4,347
Substandard	—	—	—	—	26	13,245	—	13,271
Doubtful	—	—	—	—	—	—	—	—
Total	110,131	139,619	80,278	82,856	39,095	106,168	—	558,147
Commercial – Real estate								
Pass	32,279	186,338	157,964	69,462	96,973	118,278	—	661,294
Special Mention	—	6,913	—	—	808	997	—	8,718
Substandard	—	—	—	—	582	—	—	582
Doubtful	—	—	—	—	—	—	—	—
Total	32,279	193,251	157,964	69,462	98,363	119,275	—	670,594
Construction – Real estate								
Pass	118,709	73,164	50,359	25,027	7,239	2,470	—	276,968
Special Mention	—	—	1,282	—	—	614	—	1,896
Substandard	—	—	—	—	597	1,444	—	2,041
Doubtful	—	—	—	—	—	—	—	—
Total	118,709	73,164	51,641	25,027	7,836	4,528	—	280,905
Commercial and Industrial								
Pass	51,963	79,780	28,847	10,522	18,771	25,579	—	215,462
Special Mention	—	161	17,799	2,434	48	284	—	20,726
Substandard	—	98	251	—	42	203	—	594
Doubtful	—	—	—	—	—	—	—	—
Total	51,963	80,039	46,897	12,956	18,861	26,066	—	236,782
Other consumer								
Pass	105	295	160	121	—	267	—	948
Special Mention	—	—	—	—	—	—	—	—
Substandard	—	—	—	—	—	—	—	—
Doubtful	—	—	—	—	—	—	—	—
Total	105	295	160	121	—	267	—	948
Credit card								
Ungraded	—	—	—	—	—	—	122,533	122,533
Portfolio loans receivable, gross	$ 313,187	$ 486,368	$ 336,940	$ 190,422	$ 164,155	$ 256,304	$ 122,533	$ 1,869,909

September 30, 2023								
(in thousands)	**2023**	**2022**	**2021**	**2020**	**2019**	**Prior**	**Revolving**	**Total**
Gross Charge-offs								
Commercial and Industrial	$ —	$ 77	$ —	$ —	$ 943	$ —	$ —	$ 1,020
Credit card	—	—	—	—	—	—	5,036	5,036
Total	$ —	$ 77	$ —	$ —	$ 943	$ —	$ 5,036	$ 6,056

Note 5 - Portfolio Loans Receivable (continued)

The following table presents the balances of classified loans based on credit quality indicator as of December 31, 2022:

(in thousands)	Pass[(1)]	Special Mention	Substandard	Doubtful	Ungraded[(2)]	Total
December 31, 2022						
Real estate:						
Residential	$ 469,304	$ 9,966	$ 5,465	$ —	$ —	$ 484,735
Commercial	657,411	5,577	1,563	—	—	664,551
Construction	235,262	—	2,837	—	—	238,099
Commercial and Industrial	196,381	22,469	1,371	—	—	220,221
Credit card	—	—	—	—	128,434	128,434
Other consumer	1,179	—	—	—	—	1,179
Portfolio loans receivable, gross	$ 1,559,537	$ 38,012	$ 11,236	$ —	$ 128,434	$ 1,737,219

(1) Pass includes loans graded exceptional, very good, good, satisfactory and pass/watch, in addition to credit cards and consumer credits that are not individually graded.
(2) Credit card loans are not individually graded.

Outstanding loan commitments were as follows:

(in thousands)	September 30, 2023	December 31, 2022
Unused lines of credit		
Real Estate:		
Residential	**$ 16,635**	$ 14,336
Residential - Home Equity	**44,069**	43,128
Commercial	**21,483**	36,609
Construction	**115,478**	93,913
Commercial and Industrial	**43,948**	45,747
Credit card[(1)]	**115,637**	111,227
Other consumer	**298**	102
Total	**$ 357,548**	$ 345,062
Letters of credit	**$ 4,641**	$ 5,105

(1) Outstanding loan commitments in the credit card portfolio include $103.8 million and $106.9 million in secured and partially secured balances as of September 30, 2023 and December 31, 2022, respectively.

Lines of credit are agreements to lend to a customer as long as there is no violation of any condition of the contract. Lines of credit generally have variable interest rates. Such lines do not represent future cash requirements because it is unlikely that all customers will, at any given time, draw upon their lines in full. Loan commitments generally have variable interest rates, fixed expiration dates, and may require payment of a fee.

The Company's maximum exposure to credit loss in the event of nonperformance by the customer is the contractual amount of the credit commitment. Loan commitments and lines of credit are generally made on the same terms, including with regard to collateral, as outstanding loans. Management is not aware of any accounting loss to be incurred by funding these loan commitments. The Company maintains an estimated reserve for unfunded commitments and certain off-balance sheet items such as unfunded lines of credit, which is reflected in other liabilities, with increases or decreases in the reserve being charged to or released from operating expense. Activity for this account is as follows for the periods presented:

Note 5 - Portfolio Loans Receivable (continued)

	Three months ended		Nine months ended	
(in thousands)	September 30, 2023	September 30, 2022	September 30, 2023	September 30, 2022
Balance at beginning of period	**$ 888**	$ 1,631	**$ 1,682**	$ 1,736
Impact of adopting the CECL standard on January 1, 2023	**—**	—	**(775)**	—
Provision for (reversal of) reserve for unfunded commitments	**24**	51	**5**	(54)
Balance at end of period	**$ 912**	$ 1,682	**$ 912**	$ 1,682

The Company makes representations and warranties that loans sold to investors meet the investors' program guidelines and that the information provided by the borrowers is accurate and complete. In the event of a default on a loan sold, the investor may have the right to make a claim for losses due to document deficiencies, program non-compliance, early payment default, and fraud or borrower misrepresentations.

The Company maintains a reserve for potential losses on mortgage loans sold, which is reflected in other liabilities, with changes being charged to or released from operating expense. Activity in this reserve is as follows for the periods presented:

	Three months ended		Nine months ended	
(in thousands)	September 30, 2023	September 30, 2022	September 30, 2023	September 30, 2022
Balance at beginning of period	**$ 1,182**	$ 1,166	**$ 1,174**	$ 1,164
Provision for mortgage loan put-back reserve	**4**	4	**12**	6
Balance at end of period	**$ 1,186**	$ 1,170	**$ 1,186**	$ 1,170

Note 6 - Derivative Financial Instruments

As part of its mortgage banking activities, the Company enters into interest rate lock commitments, which are commitments to originate loans whereby the interest rate on the loan is determined prior to funding and customers have locked into that interest rate. The Company then locks the loan and rate in with an investor and commits to deliver the loan if settlement occurs (Best Efforts). Certain loans under rate lock commitments are covered under forward sales contracts. Forward sales contracts are recorded at fair value with changes in fair value recorded in mortgage banking revenue. Interest rate lock commitments and commitments to deliver loans to investors are considered to be derivatives. The market value of interest rate lock commitments and best efforts contracts are not readily ascertainable with precision because they are not actively traded in stand-alone markets. The Company determines the fair value of rate lock commitments by estimating the fair value of the underlying asset, which is impacted by current interest rates and takes into consideration the probability that the rate lock commitments will close or will be funded.

The following table reports the commitment and fair value amounts on the outstanding derivatives:

(in thousands)	September 30, 2023	December 31, 2022
Notional amount of open forward sales agreements	$ —	$ 1,750
Fair value of open forward delivery sales agreements	—	9
Notional amount of interest rate lock commitments	—	626
Fair value of interest rate lock commitments	—	1

Note 7 - Leases

The Company's primary leasing activities relate to certain real estate leases entered into in support of the Company's branch operations and back office operations. The Company leases four of its full service branches and three other locations for corporate/administration activities, operations, and loan production. All property leases under lease agreements have been designated as operating leases. The Company does not have leases designated as finance leases.

The Company determines if an arrangement is a lease at inception. Operating lease ROU assets are included in premises and equipment, and operating lease liabilities are included as other liabilities in the consolidated balance sheets. ROU assets represent the right to use an underlying asset for the lease term and lease liabilities represent the obligation to make lease payments arising from the lease. Operating lease ROU assets and liabilities are recognized at commencement date based on the present value of lease payments over the lease term. As the Company's leases do not provide an implicit rate, the Company uses its incremental borrowing rate based on the information available at commencement date in determining the present value of lease payments. The historical weighted average discount rate was 3.65% at September 30, 2023 and 1.94% at December 31, 2022. The operating lease ROU asset also includes any lease pre-payments. The Company's lease terms may include options to extend or terminate the lease when it is reasonably certain that the Company will exercise that option. Lease expense for lease payments is recognized on a straight-line basis over the lease term. The Company has lease agreements with lease and non-lease components, which the Company has elected to account for separately as the non-lease component amounts are readily determinable under most leases.

As of September 30, 2023, the Company's net lease ROU assets and related lease liabilities were $3.8 million and $4.0 million, respectively, compared to December 31, 2022 balances of $2.1 million of ROU assets and $2.4 million of lease liabilities, and have remaining terms ranging from one to nine years, including extension options that the Company is reasonably certain will be exercised. As of September 30, 2023, the Company had not entered into any material leases that have not yet commenced. The Company's lease information is summarized as follows:

Note 7 - Leases (continued)

(in thousands)	September 30, 2023		December 31, 2022	
Lease Right of Use Asset:				
Lease asset	**$**	**7,229**	$	5,17
Less: Accumulated amortization		**(3,470)**		(3,07
Net lease asset	**$**	**3,759**	$	2,09
Lease Liability:				
Lease liability	**$**	**7,378**		5,32
Less: Accumulated amortization		**(3,397)**		(2,96
Net lease liability	**$**	**3,981**	$	2,35

Future minimum payments for operating leases with initial or remaining terms of one year or more are as follows:

(in thousands)	September 30, 2023	
Amounts due in:		
2023	$	3
2024		1,1
2025		6
2026		6
2027 and thereafter		1,8
Total future lease payments		**4,6**
Discount of cash flows		(6
Present value of net future lease payments	**$**	**3,9**

Note 8 - Fair Value

Generally accepted accounting principles define fair value, establish a framework for measuring fair value, recommend disclosures about fair value, and establish a hierarchy for determining fair value measurement. The hierarchy includes three levels and is based upon the valuation techniques used to measure assets and liabilities. The three levels are as follows:

Level 1 - Inputs to the valuation method are quoted prices (unadjusted) for identical assets or liabilities in active markets. This also includes certain U.S. Treasury and other U.S. Government and government agency securities actively traded in over-the-counter markets;

Level 2 - Inputs to the valuation method include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument; and

Level 3 - Inputs to the valuation method are unobservable and significant to the fair value measurement.

Fair value measurements on a recurring basis

Investment securities available for sale - The fair values of the Company's investment securities available for sale are provided by an independent pricing service. The fair values of the Company's securities are determined based on quoted prices for similar securities under Level 1 or Level 2 inputs.

Note 8 - Fair Value (continued)

Loans held for sale - The fair value of loans held for sale is determined using Level 2 inputs of quoted prices for a similar asset, adjusted for specific attributes of that loan.

Derivative financial instruments - Derivative instruments used to hedge residential mortgage loans held for sale and the related interest rate lock commitments include forward commitments to sell mortgage loans and are reported at fair value utilizing Level 2 inputs. The fair values of derivative financial instruments are based on derivative market data inputs as of the valuation date and the underlying value of mortgage loans for rate lock commitments.

The Company has categorized its financial instruments measured at fair value on a recurring basis as of September 30, 2023 and December 31, 2022 as follows:

(in thousands)

September 30, 2023	Total	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs
Investment securities available for sale				
U.S. Treasuries	$ 154,813	$ 154,813	$ —	$ —
Municipal	7,917	—	7,917	—
Corporate	4,340	—	4,340	—
Asset-backed securities	7,266	—	7,266	—
Mortgage-backed securities	31,719	—	31,719	—
Total	$ 206,055	$ 154,813	$ 51,242	$ —
Loans held for sale	$ 4,843	$ —	$ 4,843	$ —
Derivative assets	$ —	$ —	$ —	$ —
Derivative liabilities	$ —	$ —	$ —	$ —
December 31, 2022				
Investment securities available for sale				
U.S. Treasuries	$ 199,449	$ 199,449	$ —	$ —
Municipal	8,012	—	8,012	—
Corporate	4,600	—	4,600	—
Asset-backed securities	7,711	—	7,711	—
Mortgage-backed securities	32,709	—	32,709	—
Total	$ 252,481	$ 199,449	$ 53,032	$ —
Loans held for sale	$ 7,416	$ —	$ 7,416	$ —
Derivative assets	$ 10	$ —	$ 10	$ —
Derivative liabilities	$ —	$ —	$ —	$ —

Financial instruments recorded using FASB ASC 825-10

Under FASB ASC 825-10, the Company may elect to report most financial instruments and certain other items at fair value on an instrument-by-instrument basis with changes in fair value reported in net income. After the initial adoption, the election is made at the acquisition of an eligible financial asset, financial liability or firm commitment or when certain specified reconsideration events occur. The fair value election, with respect to an item, may not be revoked once an election is made.

The following table reflects the difference between the fair value carrying amount of loans held for sale, measured at fair value under FASB ASC 825-10, and the aggregate unpaid principal amount the

Note 8 - Fair Value (continued)

Company is contractually entitled to receive at maturity:

Fair Value of Loans Held for Sale

(in thousands)	September 30, 2023	December 31, 2022
Aggregate fair value	$ 4,843	$ 7,416
Contractual principal	3,035	6,808
Difference	$ 1,808	$ 608

The Company has elected to account for loans held for sale at fair value to eliminate the mismatch that would occur by recording changes in market value on derivative instruments used to hedge loans held for sale while carrying the loans at the lower of cost or market. As of September 30, 2023 and December 31, 2022, there were no held for sale loans which were classified as nonaccrual.

Fair value measurements on a nonrecurring basis

Individually evaluated loans - The Company has measured expected credit losses based on the fair value of the loan's collateral and discounted cash flow analysis, where appropriate. Fair value of the collateral is generally determined based upon independent third-party appraisals of the properties, or discounted cash flows based upon the expected proceeds. These assets are included as Level 3 fair values. As of September 30, 2023 and December 31, 2022, the fair values consist of loan receivables of $15.3 million and $9.4 million, with specific reserves of $678 thousand and $372 thousand, respectively.

Foreclosed real estate - The Company's foreclosed real estate is measured at fair value less cost to sell. Fair value is determined based on offers and/or appraisals. Cost to sell the real estate is based on standard market factors. The Company categorizes its foreclosed real estate as Level 3. As of September 30, 2023 and December 31, 2022, there was no foreclosed real estate held by the Company.

The Company has categorized its financial instruments measured at fair value on a nonrecurring basis as of September 30, 2023 and December 31, 2022 as follows:

(in thousands)	September 30, 2023	December 31, 2022
Individually evaluated loans for credit loss, net		
Level 3 inputs	14,575	9,021
Total	$ 14,575	9,021

The following table provides information describing the unobservable inputs used in Level 3 fair value measurements at September 30, 2023 and December 31, 2022:

Unobservable Inputs

	Valuation Technique	Unobservable Inputs	Range of Inputs
Individually evaluated loans	Appraised Value/Discounted Cash Flows	Discounts to appraisals or cash flows for estimated holding and/or selling costs	0 to 25%

Fair value of financial instruments

Fair value information about financial instruments, whether or not recognized in the balance sheet, for which it is practical to estimate the value is based upon the characteristics of the instruments and relevant market information. Financial instruments include cash, evidence of ownership in an entity, or contracts

Note 8 - Fair Value (continued)

that convey or impose on an entity the contractual right or obligation to either receive or deliver cash for another financial instrument.

The information used to determine fair value is highly subjective in nature and, therefore, the results are imprecise. Subjective factors include, among other things, estimates of cash flows, risk characteristics, credit quality, and interest rates, all of which are subject to change. Since the fair value is estimated as of the balance sheet date, the amounts that will actually be realized or paid upon settlement or maturity on these various instruments could be significantly different.

The fair value of the Company's loan portfolio includes a credit risk assumption in the determination of the fair value of its loans. This credit risk assumption is intended to approximate the fair value that a market participant would realize in a hypothetical orderly transaction. The Company's loan portfolio is initially fair valued using a segmented approach. The Company divides its loan portfolio into the following categories: variable rate loans, impaired loans, and all other loans. The results are then adjusted to account for credit risk as described above. However, the Company believes a further credit risk discount must be applied through the use of a discounted cash flow model to compensate for illiquidity risk, based on certain assumptions included within the discounted cash flow model, primarily the use of discount rates that better capture inherent credit risk over the lifetime of a loan. This consideration of enhanced credit risk provides an estimated exit price for the Company's loan portfolio.

For variable-rate loans that reprice frequently and have no significant change in credit risk, fair values approximate carrying values. Fair values for impaired loans are estimated using discounted cash flow models or based on the fair value of the underlying collateral.

The fair value of cash and cash equivalents and investments in restricted stocks is the carrying amount. Restricted investments includes equity of the Federal Reserve and other banker's banks.

The fair value of noninterest-bearing deposits and securities sold under agreements to repurchase is the carrying amount.

The fair value of checking, savings, and money market deposits is the amount payable on demand at the reporting date. Fair value of fixed maturity term accounts and individual retirement accounts is estimated using rates currently offered for accounts of similar remaining maturities.

The fair value of certificates of deposit in other financial institutions is estimated based on interest rates currently offered for deposits of similar remaining maturities.

The fair value of borrowings is estimated by discounting the value of contractual cash flows using current market rates for borrowings with similar terms and remaining maturities.

The fair value of outstanding loan commitments, unused lines of credit, and letters of credit are not included in the table since the carrying value generally approximates fair value. These instruments generate fees that approximate those currently charged to originate similar commitments.

The table below presents the carrying amount, fair value, and placement in the fair value hierarchy of the Company's financial instruments.

Note 8 - Fair Value (continued)

	September 30, 2023		December 31, 2022	
(in thousands)	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Financial assets				
Level 1				
Cash and due from banks	**$ 13,767**	**$ 13,767**	$ 19,963	$ 19,963
Interest-bearing deposits at other financial institutions	**130,428**	**130,428**	39,764	39,764
Federal funds sold	**1,957**	**1,957**	20,688	20,688
Level 3				
Portfolio loans receivable, net [1]	**$ 1,834,400**	**$ 1,821,205**	$ 1,704,370	$ 1,659,283
Restricted investments	**4,340**	**4,340**	7,362	7,362
Financial liabilities				
Level 1				
Noninterest-bearing deposits	**$ 680,803**	**$ 680,803**	$ 674,313	$ 674,313
Level 3				
Interest-bearing deposits	**$ 1,287,185**	**$ 1,285,398**	$ 1,083,759	$ 1,090,553
FHLB advances and other borrowed funds	**34,062**	**31,095**	119,062	116,544

(1) Includes SBA-PPP loans and portfolio loans.

Note 9 - Segments

The Company's reportable segments represent business units with discrete financial information whose results are regularly reviewed by management. The four segments include Commercial Banking, Capital Bank Home Loans (the Company's mortgage loan division), OpenSky® (the Company's credit card division) and the Corporate Office. The following schedule presents financial information for each reportable segment at September 30, 2023 and September 30, 2022.

For the Three Months Ended September 30, 2023												
(in thousands)		Commercial Bank		CBHL		OpenSky®		Corporate[2]		Eliminations		Consolidated
Interest income	$	30,409	$	111	$	16,143	$	1,162	$	(84)	$	47,741
Interest expense		10,736		32		—		247		(84)		10,931
Net interest income		19,673		79		16,143		915		—		36,810
Provision for credit losses		275		—		1,875		130		—		2,280
Provision for credit losses on unfunded commitments		24		—		—		—		—		24
Net interest income after provision		19,374		79		14,268		785		—		34,506
Noninterest income		665		1,255		4,405		1		—		6,326
Noninterest expense[1]		15,784		1,502		10,637		123		—		28,046
Net income (loss) before taxes	$	4,255	$	(168)	$	8,036	$	663	$	—	$	12,786
Total assets	$	2,102,749	$	5,280	$	116,318	$	264,950	$	(216,813)	$	2,272,484
For the Three Months Ended September 30, 2022												
Interest income	$	20,382	$	102	$	17,103	$	812	$	(59)	$	38,340
Interest expense		1,449		40		—		233		(59)		1,663
Net interest income		18,933		62		17,103		579		—		36,677
Provision (release of provision) for loan losses		(980)		—		2,240		—		—		1,260
Net interest income after provision		19,913		62		14,863		579		—		35,417
Noninterest income		468		1,115		5,524		1		—		7,108
Noninterest expense[1]		13,798		2,017		12,101		178		—		28,094
Net income (loss) before taxes	$	6,583	$	(840)	$	8,286	$	402	$	—	$	14,431
Total assets	$	1,823,049	$	7,664	$	128,842	$	234,731	$	(184,928)	$	2,009,358

Note 9 - Segments

For the Nine Months Ended September 30, 2023 (in thousands)	Commercial Bank	CBHL	OpenSky®	Corporate[2]	Eliminations	Consolidated
Interest income	$ 85,451	$ 299	$ 47,441	$ 3,274	$ (228)	$ 136,237
Interest expense	29,012	104	—	712	(228)	29,600
Net interest income	56,439	195	47,441	2,562	—	106,637
Provision for credit losses	849	—	5,823	130	—	6,802
Release of credit losses on unfunded commitments	5	—	—	—	—	5
Net interest income after provision	55,585	195	41,618	2,432	—	99,830
Noninterest income	1,964	3,743	13,329	3	—	19,039
Noninterest expense[3]	46,701	4,564	32,146	449	—	83,860
Net income (loss) before taxes	$ 10,848	$ (626)	$ 22,801	$ 1,986	$ —	$ 35,009
Total assets	$ 2,102,749	$ 5,280	$ 116,318	$ 264,950	$ (216,813)	$ 2,272,484
For the Nine Months Ended September 30, 2022						
Interest income	$ 57,794	$ 347	$ 48,823	$ 2,457	$ (123)	$ 109,298
Interest expense	3,255	185	—	573	(123)	3,890
Net interest income	54,539	162	48,823	1,884	—	105,408
Provision (release of provision) for loan losses	(980)	—	5,227	—	—	4,247
Net interest income after provision	55,519	162	43,596	1,884	—	101,161
Noninterest income	1,571	4,580	17,658	2	—	23,811
Noninterest expense[3]	38,741	6,364	36,923	351	—	82,379
Net income (loss) before taxes	$ 18,349	$ (1,622)	$ 24,331	$ 1,535	$ —	$ 42,593
Total assets	$ 1,823,049	$ 7,664	$ 128,842	$ 234,731	$ (184,928)	$ 2,009,358

(1) Noninterest expense includes $6.1 million and $6.6 million in data processing expense in OpenSky's® segment for the three months ended September 30, 2023 and 2022, respectively.
(2) The Corporate segment invests idle cash in revenue producing assets including interest-bearing cash accounts, loan participations and other appropriate investments for the Company.
(3) Noninterest expense includes $17.9 million and $20.9 million in data processing expense in OpenSky's® segment for the nine months ended September 30, 2023 and 2022, respectively.

Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis is intended as a review of significant factors affecting the Company's financial condition and results of operations for the periods indicated. This discussion and analysis should be read in conjunction with the accompanying consolidated financial statements and the related notes and the Company's Annual Report on Form 10-K for the year ended December 31, 2022.

PRIVATE SECURITIES LITIGATION REFORM ACT SAFE HARBOR STATEMENT

This Quarterly Report on Form 10-Q and oral statements made from time-to-time by our representatives contain "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995 that are subject to risks and uncertainties. You should not place undue reliance on such statements because they are subject to numerous risks and uncertainties relating to our operations and the business environment in which we operate, all of which are difficult to predict and many of which are beyond our control. Forward-looking statements include information concerning our possible or assumed future results of operations, including descriptions of our business strategy, expectations, beliefs, projections, anticipated events or trends, growth prospects, financial performance, and similar expressions concerning matters that are not historical facts. These statements often include words such as "may," "believe," "expect," "anticipate," "potential," "opportunity," "intend," "endeavor," "plan," "estimate," "forecast," "could," "project," "seek," "should," "will," or "would," or the negative of these words and phrases or similar words and phrases.

The following factors, among others, could cause our financial performance to differ materially from that expressed in such forward-looking statements:

General Economic Conditions

- economic conditions (including the interest rate environment, government economic and monetary policies, the strength of global financial markets and inflation/deflation) that impact the financial services industry as a whole and/or our business;
- recent adverse developments in the banking industry highlighted by high-profile bank failures and the potential impact of such developments on customer confidence, liquidity, and regulatory responses to these developments;
- the concentration of our business in the Washington, D.C. and Baltimore, Maryland metropolitan areas and the effect of changes in the economic, political and environmental conditions on these markets;
- interest rate risk associated with our business, including sensitivity of our interest earning assets and interest-bearing liabilities to changes in interest rates, and the impact to our earnings from changes in interest rates;
- geopolitical conditions, including acts or threats of terrorism, actions taken by the U.S. or other governments in response to acts or threats of terrorism and/or military conflicts, including the ongoing wars in Ukraine and the Middle East, which could impact business and economic conditions in the U.S. and abroad;

General Business Operations

- our ability to prudently manage our growth and execute our strategy;
- our plans to grow our commercial real estate and commercial business loan portfolios which may carry material risks of non-payment or other unfavorable consequences;

- adequacy of reserves, including our allowance for credit losses;
- deterioration of our asset quality;
- risks associated with our residential mortgage banking business;
- risks associated with our OpenSky® credit card division, including compliance with applicable consumer finance and fraud prevention regulations;
- results of examinations of us by our regulators, including the possibility that our regulators may, among other things, require us to increase our allowance for credit losses or to write-down assets;
- the effectiveness of our internal controls over financial reporting and our ability to remediate any future material weakness in our internal controls over financial reporting;
- changes in the value of collateral securing our loans;
- our dependence on our management team and board of directors and changes in management and board composition;
- liquidity and operations risks associated with our business;
- our ability to maintain important customer deposit relationships and our reputation;
- operational risks associated with our business;
- strategic acquisitions we may undertake to achieve our goals;
- the sufficiency of our capital, including sources of capital and the extent to which we may be required to raise additional capital to meet our goals;
- fluctuations in the fair value of our investment securities that are beyond our control;
- potential exposure to fraud, negligence, computer theft and cyber-crime;
- cybersecurity threats and incidents and related potential costs and risks, including reputation, financial and litigation risks;
- the adequacy of our risk management framework;
- our dependence on our information technology and telecommunications systems and the potential for any systems failures or interruptions;
- our dependence upon outside third parties for the processing and handling of our records and data;
- our ability to adapt to technological change;
- our engagement in derivative transactions;
- volatility and direction of market interest rates;
- increased competition in the financial services industry, particularly from regional and national institutions;
- our ability to adequately manage the transition from USD LIBOR as a reference rate;
- our involvement from time to time in legal proceedings, examinations and remedial actions by regulators;

- changes in the laws, rules, regulations, interpretations or policies relating to financial institution, accounting, tax, trade, monetary and fiscal matters;
- the financial soundness of other financial institutions;
- further government intervention in the U.S. financial system;
- climate change, including the enhanced regulatory, compliance, credit and reputational risks and costs; and
- natural disasters and adverse weather, acts of terrorism, an outbreak of hostilities or other international or domestic events, and other matters beyond our control.

As you read and consider forward-looking statements, you should understand that these statements are not guarantees of performance or results. They involve risks, uncertainties and assumptions and can change as a result of many possible events or factors, not all of which are known to us or in our control. Although we believe that these forward-looking statements are based on reasonable assumptions, beliefs, and expectations, if a change occurs or our beliefs, assumptions or expectations were incorrect, our business, financial condition, liquidity and/or results of operations may vary materially from those expressed in our forward-looking statements. You should be aware that many factors could affect our actual financial results or results of operations and could cause actual results to differ materially from those in the forward-looking statements. These factors include those described under the heading “Risk Factors” under Item 1A in our Annual Report on Form 10-K for the year ended December 31, 2022 and those referenced herein and in other reports on file with the SEC.

You should keep in mind that any forward-looking statement made by us speaks only as of the date on which we make it. New risks and uncertainties arise from time to time, and it is impossible for us to predict these events or how they may affect us. We have no duty to, and do not intend to, and disclaim any obligation to, update or revise any industry information or forward-looking statements after the date on which they are made.

Critical Accounting Policies

The accounting and reporting policies of the Company are in accordance with GAAP and conform to general practices within the banking industry. The Company’s financial position and results of operations are affected by management’s application of accounting policies, including estimates, assumptions and judgments made to arrive at the carrying value of assets and liabilities and amounts reported for revenues, expenses and related disclosures. Different assumptions in the application of these policies could result in material changes in the Company’s consolidated financial position and/or results of operations. The Company evaluates its critical accounting estimates and assumptions on an ongoing basis and updates them, as deemed necessary. Management has discussed the Company’s critical accounting policies and estimates with the Audit Committee of the Board of Directors of the Company.

The Company’s accounting policies are fundamental to understanding the Company’s consolidated financial position and consolidated results of operations. Accordingly, the Company’s significant accounting policies are discussed in detail in Note 1 “Nature of Business and Basis of Presentation” in the “Notes to the Consolidated Financial Statements” contained in Item 8 "Financial Statements and Supplementary Data" of the Company’s Annual Report on Form 10-K for the year ended December 31, 2022.

The critical accounting and reporting policies include the Company’s accounting for the ACL. The Company provides additional information on its ACL in Note 1 “Significant Accounting Policies” within Part I, Item 1 of this Quarterly Report on Form 10-Q.

Overview

We are Capital Bancorp, Inc., a bank holding company and a Maryland corporation incorporated in 1998, operating primarily through our wholly owned subsidiary, Capital Bank, N.A., a commercial-focused community bank based in Washington D.C. and Baltimore metropolitan areas. The Bank is headquartered in Rockville, Maryland and received its charter in 1999 and began operations in 1999. We serve businesses, not-for-profit associations, entrepreneurs and others throughout the Washington, D.C. and Baltimore, Maryland metropolitan areas through four commercial bank branches, one mortgage office, and two loan production offices.

The Company currently operates three divisions: Commercial Banking, Capital Bank Home Loans, and OpenSky®. The Company reports its activities in four business segments: commercial banking; mortgage lending; credit cards; and corporate activities. In determining the appropriateness of segment definition, the Company considers components of the business about which financial information is available and regularly evaluated relative to resource allocation and performance assessment. The accompanying consolidated financial statements have been prepared in accordance with GAAP, and conform to general practices within the banking industry.

Our Commercial Banking division accounts for the majority of the Bank’s total assets. Our commercial bankers endeavor to provide quality service, customized solutions and tailored advice to commercial clients in our operating markets, primarily in the Washington, D.C. and Baltimore metropolitan areas.

Our Capital Bank Home Loan (“CBHL”) division originates conventional and government-guaranteed residential mortgage loans on a nationwide basis primarily for sale into the secondary market and, in certain circumstances, for the Bank’s loan portfolio.

Our OpenSky® division provides secured, partially secured and unsecured credit cards on a nationwide basis to under-banked populations and those looking to rebuild their credit scores. OpenSky® cards operate on a digital and mobile enabled platform with almost all marketing and application procedures are conducted through website and mobile applications. For the secured credit card, a deposit equal to the full credit limit of the card is made, upon account opening, into a noninterest-bearing demand account with the Bank and the deposit is required to be maintained throughout the life of the card. Using our proprietary scoring model, which considers credit score and repayment history (typically a minimum of six months of on-time repayments, but ultimately determined on a case-by-case basis), OpenSky® also offers certain existing customers an unsecured line supplementary to their secured line of credit.

Capital

As of September 30, 2023, the Bank was in compliance with all applicable regulatory capital requirements to which it was subject, and the Bank was classified as “well capitalized” for purposes of the prompt corrective action regulations. There are no conditions or events since that notification that management believes would change the Bank’s classification. We closely monitor our capital position and intend to take appropriate steps to ensure that our level of capital remains strong.

Results of Operations

Net Income

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

(in thousands)	Three Months Ended September 30, 2023	2022	% Change
Interest income	**$ 47,741**	$ 38,340	24.5
Interest expense	**10,931**	1,663	557.3
Net interest income	**36,810**	36,677	0.4
Provision for credit losses	**2,280**	1,260	81.0
Provision for credit losses on unfunded commitments	**24**	—	
Net interest income after provision	**34,506**	35,417	(2.6)
Noninterest income	**6,326**	7,108	(11.0)
Noninterest expenses	**28,046**	28,094	(0.2)
Net income before income taxes	**12,786**	14,431	(11.4)
Income tax expense	**2,998**	3,336	(10.1)
Net income	**$ 9,788**	$ 11,095	(11.8)

Net income for the three months ended September 30, 2023 was $9.8 million, compared to net income of $11.1 million for the same period in 2022, an 11.8% decrease. Net interest income increased slightly by $0.1 million, or 0.4%, to $36.8 million when comparing the three months ended September 30, 2023 to the three months ended September 30, 2022, primarily due to increased average balances of $245.3 million in portfolio loans combined with a 78 basis point increase in average yield for portfolio loans partially offset by significant increases in the cost of funding.

The provision for credit losses for the three months ended September 30, 2023 was $2.3 million, an increase of $1.0 million, or 81.0%, from the same period in 2022. Net charge-offs for the three months ended September 30, 2023 were $1.8 million, or 0.38% on an annualized basis of average portfolio loans, compared to $1.6 million, or 0.39% on an annualized basis of average loans for the same period in 2022. Of the $1.8 million in net charge-offs during the quarter, $1.4 million related to secured and partially secured cards in the credit card portfolio and $0.3 million related to unsecured cards.

For the quarter ended September 30, 2023, noninterest income was $6.3 million, a decrease of $0.8 million, or 11.0%, from $7.1 million in the prior year quarter. Credit card fees declined by $1.1 million as the number of open customer accounts declined year over year, which resulted in lower interchange and other fee income compared to the prior year quarter.

Noninterest expense was $28.0 million for the three months ended September 30, 2023, as compared to $28.1 million for the three months ended September 30, 2022. The change includes decreases in professional fees of $1.5 million and data processing expense of $0.8 million partially offset by increases in salaries and employee benefits of $1.7 million and other operating expense of $0.5 million.

(in thousands)	Nine Months Ended September 30, 2023	2022	% Change
Interest income	**$ 136,237**	$ 109,298	24.6 %
Interest expense	**29,600**	3,890	660.9 %
Net interest income	**106,637**	105,408	1.2 %
Provision for credit losses	**6,802**	4,247	60.2 %
Provision for credit losses on unfunded commitments	**5**	—	
Net interest income after provision	**99,830**	101,161	(1.3)%
Noninterest income	**19,039**	23,811	(20.0)%
Noninterest expenses	**83,860**	82,379	1.8 %
Net income before income taxes	**35,009**	42,593	(17.8)%
Income tax expense	**8,168**	9,779	(16.5)%
Net income	**$ 26,841**	$ 32,814	(18.2)%

Net income for the nine months ended September 30, 2023 was $26.8 million, compared to net income of $32.8 million for the same period in 2022, an 18.2% decrease. Net interest income increased $1.2 million, or 1.2%, to $106.6 million when comparing the nine months ended September 30, 2023 to the nine months ended September 30, 2022, primarily due to increased average balances of $252.4 million in portfolio loans combined with the 81 basis point increase in average yield for portfolio loans offset by significant increases in the cost of funding.

The provision for credit losses for the nine months ended September 30, 2023 was $6.8 million, an increase of $2.6 million, or 60.2%, from the provision for loan losses for the nine months ended September 30, 2022, attributable primarily to the credit card portfolio.

For the nine months ended September 30, 2023, noninterest income was $19.0 million, a decrease of $4.8 million, or 20.0%, from $23.8 million in the prior year period. The decrease was primarily driven by the decline in credit card fees of $4.4 million as the number of open customer accounts declined to 529,205 at September 30, 2023 from 576,844 at September 30, 2022, which resulted in lower interchange and other fee income recognized compared to the prior year. The elevated interest rate environment continues to put pressure on the mortgage market, leading to declines in home loan sales and home loan refinances, which has resulted in a $0.6 million decrease in mortgage banking revenue compared to the nine months ended September 30, 2022.

Noninterest expense was $83.9 million for the nine months ended September 30, 2023, as compared to $82.4 million for the nine months ended September 30, 2022, an increase of $1.5 million, or 1.8%. The increase was primarily driven by a $6.0 million, or 19.2%, increase in salaries and employee benefits, partially offset by a $3.2 million, or 13.9%, decrease in data processing expenses and a $1.2 million decrease in professional fees due to a reduction in third party consulting fees. The decrease in data processing expenses was the result of a contract renegotiation entered into in the first quarter of 2022 in the OpenSky® Division as well as fewer average open cards during the period.

Net Interest Income and Net Margin Analysis

Net interest income is the difference between interest income on interest earning assets and the cost of funds supporting those assets. Interest earning assets are composed primarily of loans, loans held for sale, investment securities, and interest-bearing deposits with banks. The cost of funds represents interest expense on deposits and borrowings, which consist of federal funds purchased, advances from the Federal Home Loan Bank (“FHLB”), and subordinated notes. Noninterest-bearing deposits and capital also provide sources of funding.

We analyze our ability to maximize income generated from interest earning assets and control the interest expenses associated with our liabilities, measured as net interest income, through our net interest margin and net interest spread. Net interest margin is a ratio calculated as net interest income annualized divided by average interest earning assets for the same period. Net interest spread is the difference between average interest rates earned on interest earning assets and average interest rates paid on interest-bearing liabilities.

Changes in market interest rates and the interest rates we earn on interest earning assets or pay on interest-bearing liabilities, as well as in the volume and mix of interest earning assets, interest-bearing and noninterest-bearing liabilities and stockholders' equity, are usually the largest drivers of periodic changes in net interest income, net interest margin and net interest spread. Fluctuations in market interest rates are driven by many factors, including governmental monetary policies, inflation, deflation, macroeconomic developments, changes in unemployment, the money supply, political and international conditions and conditions in domestic and foreign financial markets. Periodic changes in the volume and types of loans in our loan portfolio are affected by, among other factors, economic and competitive conditions in the Washington, D.C. and Baltimore metropolitan areas, as well as developments affecting the real estate, technology, government services, hospitality and tourism and financial services sectors within our target markets and throughout the Washington, D.C. and Baltimore metropolitan areas. Our ability to respond to changes in these factors by using effective asset-liability management techniques is critical to maintaining the stability of net interest income and net interest margin.

The table below presents the average balances and weighted average rates of the major categories of the Company's assets, liabilities, and stockholders' equity for the three and nine months ended September 30, 2023 and 2022. Weighted average yields are derived by dividing annualized income by the average balance of the related assets, and weighted average rates are derived by dividing annualized expense by the average balance of the related liabilities, for the periods shown. Average outstanding balances are derived by utilizing average daily balances for the time period shown. The weighted average yields and rates include amortization of fees, costs, premiums and discounts, which are considered adjustments to yield/rates. Weighted average yields on tax-exempt securities are not calculated on a fully taxable equivalent basis.

AVERAGE BALANCE SHEET AND NET INTEREST ANALYSIS

($ in thousands)	Three Months Ended September 30, 2023 Average Outstanding Balance	2023 Interest Income/ Expense	2023 Average Yield/ Rate[1]	2022 Average Outstanding Balance	2022 Interest Income/ Expense	2022 Average Yield/ Rate[1]
Assets						
Interest earning assets:						
Interest-bearing deposits	$ 87,112	$ 1,183	5.39 %	$ 101,187	$ 471	1.85 %
Federal funds sold	1,134	15	5.25	1,492	7	1.87
Investment securities	229,731	1,089	1.88	287,944	1,362	1.88
Restricted investments	4,058	69	6.75	4,116	49	4.72
Loans held for sale	6,670	111	6.60	7,879	102	5.15
SBA-PPP loans receivable	906	11	4.82	5,906	263	17.66
Portfolio loans receivable[2]	1,846,866	45,263	9.72	1,601,546	36,086	8.94
Total interest earning assets	2,176,477	47,741	8.70	2,010,070	38,340	7.57
Noninterest earning assets	44,640			39,008		
Total assets	$ 2,221,117			$ 2,049,078		
Liabilities and Stockholders' Equity						
Interest-bearing liabilities:						
Interest-bearing demand accounts	$ 215,527	$ 71	0.13 %	$ 244,929	$ 39	0.06 %
Savings	5,582	3	0.21	9,216	1	0.04
Money market accounts	655,990	6,373	3.85	555,634	815	0.58
Time deposits	374,429	4,256	4.51	155,091	531	1.36
Borrowed funds	34,932	228	2.59	40,700	277	2.70
Total interest-bearing liabilities	1,286,460	10,931	3.37	1,005,570	1,663	0.66
Noninterest-bearing liabilities:						
Noninterest-bearing liabilities	25,047			24,440		
Noninterest-bearing deposits	666,939			802,458		
Stockholders' equity	242,671			216,610		
Total liabilities and stockholders' equity	$ 2,221,117			$ 2,049,078		
Net interest spread			5.33 %			6.91 %
Net interest income		$ 36,810			$ 36,677	
Net interest margin [3]			6.71 %			7.24 %

(1) Annualized.
(2) Includes nonaccrual loans.
(3) For the three months ended September 30, 2023 and 2022, SBA-PPP loans and credit card loans collectively accounted for 266 and 308 basis points of the reported net interest margin, respectively.

($ in thousands)	Three Months Ended September 30, 2023		2022	
Net interest margin, as adjusted (non-GAAP)[(1)]				
Net interest income	**$**	**36,810**	$	36,677
Less: Credit card loan income		**15,792**		16,768
Less: SBA-PPP loan income		**11**		263
Net interest income, as adjusted	**$**	**21,007**	$	19,646
Average interest earning assets		**2,176,477**		2,010,070
Less: Average credit card loans		**116,814**		132,246
Less: Average SBA-PPP loans		**906**		5,906
Total average interest earning assets, as adjusted	**$**	**2,058,757**	$	1,871,918
Net interest margin, as adjusted (non-GAAP)[(2)]		**4.05 %**		4.16 %

(1) The Company uses non-GAAP (United States Generally Accepted Accounting Principles) financial information in its analysis of the Company's performance. The Company's management believes that these non-GAAP financial measures provide a greater understanding of ongoing operations, enhance comparability of results of operations with prior periods and show the effects of significant gains and charges in the periods presented. The Company's management believes that investors may use these non-GAAP financial measures to analyze the Company's financial performance without the impact of unusual items or events that may obscure trends in the Company's underlying performance. This non-GAAP data should be considered in addition to results prepared in accordance with GAAP, and is not a substitute for, or superior to, GAAP results

(2) Annualized.

The net interest margin decreased 53 basis points to 6.71% for the three months ended September 30, 2023 from the same period in 2022 as interest income on credit cards decreased $1.0 million and interest income on SBA-PPP loans totaled $0.3 million for the three months ended September 30, 2022 with no comparable amount in 2023. Net interest margin, excluding credit card and SBA-PPP loans[(1)], decreased to 4.05% for the three months ended September 30, 2023, compared to 4.16% for the same period in 2022.

For the three months ended September 30, 2023, average interest earning assets increased $166.4 million, or 8.3%, to $2.2 billion as compared to the same period in 2022, and the average yield on interest earning assets increased 113 basis points. Compared to the same period in the prior year, average interest-bearing liabilities increased $280.9 million, or 27.9%, and the average cost of interest-bearing liabilities increased to 3.37%, a 271 basis point increase from 0.66%.

(1) A reconciliation of this non-GAAP financial measure is set forth in the table immediately above.

AVERAGE BALANCE SHEET AND NET INTEREST ANALYSIS

($ in thousands)	Nine Months Ended September 30, 2023 Average Outstanding Balance	2023 Interest Income/ Expense	2023 Average Yield/ Rate[1]	2022 Average Outstanding Balance	2022 Interest Income/ Expense	2022 Average Yield/ Rate[1]
Assets						
Interest earning assets:						
Interest-bearing deposits	**$ 72,116**	**$ 2,531**	**4.69 %**	$ 172,033	$ 1,001	0.78 %
Federal funds sold	**1,605**	**53**	**4.42**	2,590	9	0.48
Investment securities	**252,993**	**3,732**	**1.97**	234,294	2,510	1.43
Restricted investments	**5,184**	**270**	**6.96**	3,913	133	4.54
Loans held for sale	**6,145**	**299**	**6.51**	10,921	347	4.25
SBA-PPP loans receivable	**1,600**	**26**	**2.17**	39,063	3,449	11.80
Portfolio loans receivable[2]	**1,799,755**	**129,326**	**9.61**	1,547,386	101,849	8.80
Total interest earning assets	**2,139,398**	**136,237**	**8.51**	2,010,200	109,298	7.27
Noninterest earning assets	**44,123**			47,936		
Total assets	**$ 2,183,521**			$ 2,058,136		
Liabilities and Stockholders' Equity						
Interest-bearing liabilities:						
Interest-bearing demand accounts	**$ 203,099**	**$ 208**	**0.14 %**	$ 265,854	$ 114	0.06 %
Savings	**5,965**	**6**	**0.13**	9,138	4	0.06
Money market accounts	**628,977**	**16,371**	**3.48**	553,794	1,512	0.37
Time deposits	**353,635**	**11,281**	**4.27**	161,982	1,604	1.32
Borrowed funds	**65,192**	**1,734**	**3.56**	36,299	656	2.41
Total interest-bearing liabilities	**1,256,868**	**29,600**	**3.15**	1,027,067	3,890	0.51
Noninterest-bearing liabilities:						
Noninterest-bearing liabilities	**22,846**			23,748		
Noninterest-bearing deposits	**665,821**			797,660		
Stockholders' equity	**237,986**			209,661		
Total liabilities and stockholders' equity	**$ 2,183,521**			$ 2,058,136		
Net interest spread			**5.36 %**			6.76 %
Net interest income		**$ 106,637**			$ 105,408	
Net interest margin [3]			**6.66 %**			7.01 %

(1) Annualized.
(2) Includes nonaccrual loans.
(3) For the nine months ended September 30, 2023 and 2022, SBA-PPP loans and credit card loans collectively accounted for 268 and 307 basis points of the reported net interest margin, respectively.

($ in thousands)	Nine Months Ended September 30, 2023		2022	
Net interest margin, as adjusted (non-GAAP)[(1)]				
Net interest income	**$**	**106,637**	$	105,408
Less: Credit card loan income		**46,419**		47,631
Less: SBA-PPP loan income		**26**		3,449
Net interest income, as adjusted	**$**	**60,192**	$	54,328
Average interest earning assets		**2,139,398**		2,010,200
Less: Average credit card loans		**114,416**		127,266
Less: Average SBA-PPP loans		**1,600**		39,063
Total average interest earning assets, as adjusted	**$**	**2,023,382**	$	1,843,871
Net interest margin, as adjusted (non-GAAP)[(2)]		**3.98 %**		3.94 %

(1) The Company uses non-GAAP (United States Generally Accepted Accounting Principles) financial information in its analysis of the Company's performance. The Company's management believes that these non-GAAP financial measures provide a greater understanding of ongoing operations, enhance comparability of results of operations with prior periods and show the effects of significant gains and charges in the periods presented. The Company's management believes that investors may use these non-GAAP financial measures to analyze the Company's financial performance without the impact of unusual items or events that may obscure trends in the Company's underlying performance. This non-GAAP data should be considered in addition to results prepared in accordance with GAAP, and is not a substitute for, or superior to, GAAP results

(2) Annualized.

The net interest margin decreased 35 basis points to 6.66% for the nine months ended September 30, 2023 from the same period in 2022. Net interest margin, excluding credit card and SBA-PPP loans[(2)], was 3.98% for the nine months ended September 30, 2023, compared to 3.94% for the same period in 2022.

For the nine months ended September 30, 2023, average interest earning assets increased $129.2 million, or 6.4%, to $2.1 billion as compared to the same period in 2022, and the average yield on interest earning assets increased 124 basis points. Compared to the same period in the prior year, average interest-bearing liabilities increased $229.8 million, or 22.4%, while the average cost of interest-bearing liabilities increased 264 basis points to 3.15% from 0.51%.

(2) A reconciliation of this non-GAAP financial measure is set forth in the table immediately above.

The rate/volume table below presents the composition of the change in net interest income for the periods indicated, as allocated between the change in net interest income due to changes in the volume of average earning assets and interest-bearing liabilities, and the changes in net interest income due to changes in interest rates.

RATE/VOLUME ANALYSIS OF NET INTEREST INCOME

	Three Months Ended September 30, 2023 Compared to September 30, 2022			Nine Months Ended September 30, 2023 Compared to September 30, 2022		
	Change Due To			Change Due To		
(in thousands)	Volume	Rate	Interest Variance	Volume	Rate	Interest Variance
Interest Income:						
Interest-bearing deposits	$ (191)	$ 903	$ 712	$ (3,505)	$ 5,035	$ 1,5
Federal funds sold	(5)	13	8	(33)	77	
Investment securities available for sale	(273)	—	(273)	276	946	1,2
Restricted investments	(1)	21	20	66	71	1
Loans held for sale	(20)	29	9	(233)	185	(
SBA-PPP loans receivable	(61)	(191)	(252)	(608)	(2,815)	(3,4
Portfolio loans receivable excluding credit card loans	4,443	5,710	10,153	13,053	15,636	28,6
Credit card loans	(2,086)	1,110	(976)	(5,213)	4,001	(1,2
Total interest income	1,806	7,595	9,401	3,803	23,136	26,9
Interest Expense:						
Interest-bearing demand accounts	(10)	42	32	(66)	160	
Savings	(2)	4	2	(3)	5	
Money market accounts	974	4,584	5,558	1,957	12,902	14,8
Time deposits	2,494	1,231	3,725	6,103	3,574	9,6
Borrowed funds	(38)	(11)	(49)	766	312	1,0
Total interest expense	3,418	5,850	9,268	8,757	16,953	25,7
Net interest income	$ (1,612)	$ 1,745	$ 133	$ (4,954)	$ 6,183	$ 1,2

When comparing the three months ended September 30, 2023 to the same period in 2022, the greatest positive impact to total interest income was the increased market interest rates affecting substantially all interest earning assets. The loan portfolio, excluding credit cards, continued to experience growth through the three months ended September 30, 2023, which contributed an additional $10.2 million in interest income. On a standalone basis, interest income attributable to the credit card portfolio fell by $1.0 million when comparing the three months ended September 30, 2023 to the three months ended September 30, 2022, primarily due to a decrease in open customer accounts and corresponding credit card loan balances, as a result of rising interest rates and late charges, which impacted the rate calculation. Increased market interest rates were the primary driver of increased interest expense, with interest expense on money market accounts and time deposits increasing $4.6 million and $1.2 million, respectively, when comparing the three months ended September 30, 2023 to the three months ended September 30, 2022. An increase in the volume of time deposits contributed an additional $2.5 million to the increase in interest expense.

When comparing the nine months ended September 30, 2023 to the same period in 2022, the largest positive impact to total interest income was the effect of increases in market interest rates on substantially all interest earning assets. Growth in portfolio loan volumes contributed $13.1 million to the increase in interest income, while the heightened interest rates on portfolio loans contributed $15.6 million for the nine months ended September 30, 2023 compared to the same period in the prior year. During the nine months ended September 30, 2022, $105.6 million of SBA-PPP loans were forgiven by the SBA which accelerated the recognition of $3.1 million of deferred fee income. In comparison, during the nine months ended September 30, 2023, $1.4 million of SBA-PPP loan principal was forgiven and $14 thousand of deferred fee income was recognized. Increased interest rates also contributed $17.0 million to increased interest expense comparing the nine months ended September 30, 2023 to the same period in 2022, substantially offsetting the increase in total interest income. The increase in the volume of time deposits contributed an additional $6.1 million to the increase in interest expense.

Rising interest rates have resulted in some customers moving balances from noninterest-bearing deposit accounts to interest-bearing deposit accounts increasing interest expense. The average balance of noninterest-bearing deposits of $666.9 million for the three months ended September 30, 2023 decreased $135.5 million from $802.5 million for the three months ended September 30, 2022. The average balance of interest-bearing deposits of $1.3 billion for the three months ended September 30, 2023 increased $286.7 million from $964.9 million for the three months ended September 30, 2022.

The average balance of noninterest-bearing deposits of $665.8 million for the nine months ended September 30, 2023 decreased $131.8 million from $767.7 million for the nine months ended September 30, 2022. The average balance of interest-bearing deposits of $1.2 billion for the nine months ended September 30, 2023 increased $200.9 million from $990.8 million for the nine months ended September 30, 2022.

Provision for Credit Losses

The provision for credit losses represents the amount of expense charged to current earnings to fund the ACL. The amount for credit losses is based on many factors which reflect management’s assessment of the risk in the loan portfolio. Those factors include historical losses, forecasted cash flows, economic conditions and trends, the value and adequacy of collateral, volume and mix of the portfolio, performance of the portfolio, and internal loan processes of the Company and Bank. For a description of the factors taken into account by our management in determining the ACL, see Note 1 to the Consolidated Financial Statements.

For the three months ended September 30, 2023, the provision for credit losses was $2.3 million, an increase of $1.0 million from the same period in 2022. Net charge-offs for the three months ended September 30, 2023 were $1.8 million, or 0.38% on an annualized basis of average portfolio loans, compared to $1.6 million, or 0.39% on an annualized basis of average portfolio loans for the same period in 2022. Of the $1.8 million in net charge-offs during the quarter, $1.4 million related to secured and partially secured cards in the credit card portfolio and $0.3 million related to unsecured cards.

For the nine months ended September 30, 2023, the provision for credit losses was $6.8 million, an increase of $2.6 million from the same period in 2022, attributable primarily to the credit card portfolio. Net charge-offs for the nine months ended September 30, 2023, were $6.0 million, or 0.45% on an annualized basis of average portfolio loans, compared to $3.3 million, or 0.29% on an annualized basis of average portfolio loans, for the same period in 2022. The $6.0 million in net charge-offs during the nine months ended September 30, 2023 was comprised primarily of credit card portfolio net charge-offs with $4.1 million related to secured and partially secured cards and $1.0 million related to unsecured cards.

Although the majority of OpenSky® credit cards are secured, losses may occur. Some losses result from identity fraud, payment fraud and funding fraud. In addition, losses are sometimes incurred when customers exceed established credit limits as a consequence of certain VISA membership policies that allow cardholders to incur certain charges, such as, for example, rental car charges, gas station charges and hotel deposits, that may exceed card limits. Finally, losses to our credit card portfolio may arise if cardholders cease to maintain the account in good standing with timely payments.

The ACL as a percent of portfolio loans was 1.52% at September 30, 2023. The ACL at December 31, 2022, prior to the adoption of CECL, represented 1.53% of portfolio loans. The maintenance of a high-quality loan portfolio, with an adequate allowance for expected credit losses, will continue to be a primary objective for the Company. See additional discussion regarding the Company's ACL and reserve for unfunded commitments credit exposures at September 30, 2023 in "Financial Condition - Allowance for Credit Losses."

Noninterest Income

Our primary sources of recurring noninterest income are credit card fees, such as interchange fees and statement fees, and mortgage banking revenue. Noninterest income does not include (i) loan origination fees to the extent they exceed the direct loan origination costs, which are generally recognized over the life of the related loan as an adjustment to yield using the interest method or (ii) annual, renewal and late fees related to our credit card portfolio, which are generally recognized over the twelve month life of the related loan as an adjustment to yield using the interest method.

The following table presents, for the periods indicated, the major categories of noninterest income:

	Three Months Ended September 30,			Nine Months Ended September 30,		
(in thousands)	**2023**	**2022**	**% Change**	**2023**	**2022**	**% Change**
Noninterest income:						
Service charges on deposit accounts	**$ 250**	$ 199	25.6 %	**$ 724**	$ 545	32.8
Credit card fees	**4,387**	5,524	(20.6)	**13,303**	17,658	(24.7
Mortgage banking revenue	**1,243**	969	28.3	**3,730**	4,312	(13.5
Other income	**446**	416	7.2	**1,282**	1,296	(1.1
Total noninterest income	**$ 6,326**	$ 7,108	(11.0)%	**$ 19,039**	$ 23,811	(20.0

For the three months ended September 30, 2023, credit card fees of $4.4 million declined by $1.1 million as compared to the three months ended September 30, 2022, as the number of open customer accounts declined year over year, which resulted in lower interchange and other fee income. For the nine months ended September 30, 2023, credit card fees of $13.3 million decreased $4.4 million as compared to the nine months ended September 30, 2022, as the number of open customer accounts declined to 529,205 at September 30, 2023 from 576,844 at September 30, 2022. The elevated interest rate environment continues to put pressure on the mortgage market, leading to declines in home loan sales and home loan refinances, which has resulted in a $0.6 million decrease in mortgage banking revenue compared to the prior year.

The Bank's Capital Bank Home Loan division experienced a decline of 17.3% in mortgage originations during the three months ended September 30, 2023 when compared to the same period in the prior year. A rising interest rate environment continues to dampen home loan sales and home loan refinances which resulted in origination volumes decreasing $10.5 million, to $50.0 million, in the third quarter of 2023, when compared to $60.5 million in the third quarter of 2022. Gain on sale margins increased from 2.05% for the three months ended September 30, 2022, to 2.57% for the three months ended September 30, 2023. Historically-low housing inventory, shortages in new home building materials, and increasing interest rates are likely to continue suppressing origination volumes.

Mortgage loans sold are subject to repurchase in circumstances where documentation is deficient or the underlying loan becomes delinquent or pays off within a specified period following loan funding and sale. The Bank has established a reserve under GAAP for possible repurchases. The reserve was $1.2 million at September 30, 2023 and December 31, 2022. The Bank did not repurchase any loans during the three and nine months ended September 30, 2023 or 2022. The Bank does not originate "sub-prime" mortgage loans and has no exposure to this market segment.

Noninterest Expense

Generally, noninterest expense is comprised of all employee expenses and costs associated with operating our facilities, obtaining and retaining customer relationships and providing bank services, with the largest component being salaries and employee benefits. Noninterest expense also includes operational expenses, such as occupancy and equipment expenses, professional fees, advertising expenses, loan processing expenses and other general and administrative expenses, including FDIC assessments, communications, travel, meals, training, supplies and postage.

The following table presents, for the periods indicated, the major categories of noninterest expense:

(in thousands)	Three Months Ended September 30,			Nine Months Ended September 30,		
	2023	**2022**	**% Change**	**2023**	**2022**	**% Change**
Noninterest expense:						
Salaries and employee benefits	**$ 12,419**	$ 10,747	15.6 %	**$ 37,116**	$ 31,129	19.2 %
Occupancy and equipment	**1,351**	1,138	18.7	**4,100**	3,476	18.0
Professional fees	**2,358**	3,848	(38.7)	**7,340**	8,586	(14.5)
Data processing	**6,469**	7,178	(9.9)	**19,558**	22,721	(13.9)
Advertising	**1,565**	1,632	(4.1)	**4,728**	5,494	(13.9)
Loan processing	**426**	625	(31.8)	**1,435**	1,352	6.1
Foreclosed real estate expenses, net	**1**	—		**7**	(183)	(103.8)
Other operating	**3,457**	2,926	18.1	**9,576**	9,804	(2.3)
Total noninterest expenses	**$ 28,046**	$ 28,094	(0.2)	**$ 83,860**	$ 82,379	1.8

Noninterest expense was $28.0 million for the three months ended September 30, 2023, as compared to $28.1 million for the three months ended September 30, 2022, a decrease of $0.1 million. Professional fees decreased $1.5 million and data processing expenses decreased $0.7 million partially offset by increases in salaries and employee benefits of $1.7 million and other operating expense of $0.5 million.

Noninterest expense was $83.9 million for the nine months ended September 30, 2023, as compared to $82.4 million for the nine months ended September 30, 2022, an increase of $1.5 million, or 1.8%. Salaries and employee benefits increased by $6.0 million, or 19.2%, due in part to growth in headcount in the Commercial Bank segment during the nine months ended September 30, 2023 compared to the same prior year period. Data processing expenses decreased $3.2 million, which was the result of a contract renegotiation entered into during the first quarter of 2022 in the OpenSky® Division as well as fewer average open cards during the period when compared to 2022. Professional fees decreased $1.2 million due to a reduction in third party consulting fees.

Income Tax Expense

The amount of income tax expense we incur is influenced by our pre-tax income and our nondeductible expenses. Deferred tax assets and liabilities are reflected at enacted tax rates in effect for the period in which the deferred tax assets and liabilities are expected to be realized or settled. A valuation allowance is established when necessary to reduce deferred tax assets to the amount expected to be realized.

Income tax expense was $3.0 million and $8.2 million for the three and nine months ended September 30, 2023 compared to $3.3 million and $9.8 million for the same periods, respectively, in 2022. Our effective tax rates increased from 23.1% for the three months ended September 30, 2022 to 23.4% for the three months ended September 30, 2023, and from 23.0% for the nine months ended September 30, 2022 to 23.3% for the nine months ended September 30, 2023, primarily attributable to the application of differing state income tax rates.

Financial Condition

The following table summarizes the Company's financial condition at the dates indicated.

(in thousands)	September 30, 2023	December 31, 2022	$ Change	% Change
Total assets	$ 2,272,484	$ 2,123,655	$ 148,829	7.0
Investment securities available for sale	206,055	252,481	(46,426)	(18.4
Mortgage loans held for sale	4,843	7,416	(2,573)	(34.7
U.S. Small Business Administration ("SBA") Payroll Protection Program ("PPP") loans receivable, net of fees and costs	750	2,163	(1,413)	(65.3
Portfolio loans receivable, net of deferred fees and costs	1,861,929	1,728,592	133,337	7.7
Total deposits	1,967,988	1,758,072	209,916	11.9
FHLB borrowings	22,000	107,000	(85,000)	(79.4
Other borrowed funds	12,062	12,062	—	—
Total stockholders' equity	242,878	224,015	18,863	8.4
Equity to total assets at end of period	10.7 %	10.5 %		1.9
Weighted average number of basic shares outstanding	14,038	14,025		0.1
Weighted average number of diluted shares outstanding	14,112	14,362		(1.7

Total assets at September 30, 2023 increased $148.8 million from the balance at December 31, 2022. Net portfolio loans, which exclude mortgage loans held for sale and SBA-PPP loans, totaled $1.9 billion as of September 30, 2023, an increase of $133.3 million, or 7.7%, from $1.7 billion at December 31, 2022. Increases in portfolio loans receivable were offset by a decrease in mortgage loans held for sale of $2.6 million, or 34.7%, and SBA-PPP loans of $1.4 million when comparing the period end balances at September 30, 2023 to December 31, 2022.

Investment Securities

The Company uses its securities portfolio to provide a source of liquidity, provide an appropriate return on funds invested, manage interest rate risk, meet collateral requirements and meet regulatory capital requirements.

Management classifies investment securities as either held to maturity or available for sale based on our intentions and the Company's ability to hold such securities until maturity. In determining such classifications, securities that management has the positive intent and the Company has the ability to hold until maturity are classified as held to maturity and carried at amortized cost. All other securities are designated as available for sale and carried at estimated fair value with unrealized gains and losses included in stockholders' equity on an after-tax basis. As of September 30, 2023, all securities were classified as available for sale.

To supplement interest income earned on our loan portfolio, the Company invests in U.S. Treasuries, high-quality mortgage-backed securities, government agency bonds, asset-backed securities and high-quality municipal and corporate bonds.

The following tables summarize the contractual maturities, without consideration of call features or pre-refunding dates, and weighted-average yields of investment securities at September 30, 2023 and the amortized cost and carrying value of those securities as of the indicated dates. The weighted average yields were calculated by multiplying the amortized cost of each individual security by its yield, dividing that figure by the portfolio total, and then summing the value of these results to arrive at the weighted average yield. Yields on tax-exempt investments are not calculated on a fully tax equivalent basis.

INVESTMENT MATURITIES

September 30, 2023 (in thousands)	One Year or Less		More Than One Year Through Five Years		More Than Five Years Through Ten Years		More Than Ten Years		Total		
	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Amortized Cost	Fair Value	Weighted Average Yield
Securities Available for Sale:											
U.S. Treasuries	$ 40,024	1.36 %	$ 110,756	1.28 %	$ 20,716	1.47 %	$ —	— %	$ 171,496	$ 154,813	1.32 %
Municipal	—	—	—	—	507	2.54	10,300	1.91	10,807	7,917	1.94
Corporate	—	—	—	—	5,000	4.31	—	—	5,000	4,340	4.31
Asset-backed securities	—	—	—	—	—	—	7,318	3.31	7,318	7,266	3.31
Mortgage-backed securities	—	—	10,031	5.18	13,096	2.92	11,606	1.47	34,733	31,719	3.09
Total	$ 40,024	1.36 %	$ 120,787	1.60 %	$ 39,319	2.33 %	$ 29,224	2.09 %	$ 229,354	$ 206,055	1.75 %

Portfolio Loans Receivable

Our primary source of income is derived from interest earned on loans. Our portfolio loans consist of loans secured by real estate as well as commercial business loans, credit card loans, substantially all of which are secured by corresponding deposits at the Bank and, to a limited extent, other consumer loans. Our loan customers primarily consist of small- to medium-sized businesses, professionals, real estate investors, small residential builders and individuals. Our owner-occupied commercial real estate loans, residential construction loans and commercial business and investment loans provide us with higher risk-adjusted returns, shorter maturities and more sensitivity to interest rate fluctuations, and are complemented by our relatively lower risk residential real estate loans to individuals. Our credit card portfolio supplements our traditional lending products with enhanced yields. Our lending activities, outside of credit cards, are principally directed to our market area consisting of the Washington, D.C. and Baltimore, Maryland metropolitan areas. Refer to Note 5 to Unaudited Consolidated Financial Statements for additional discussion of each major classification of portfolio loans receivable.

The repayment of loans is a source of additional liquidity for the Company. The following table details contractual maturities of our portfolio loans, along with an analysis of loans maturing after one year categorized by rate characteristic. Loans with adjustable interest rates are shown as maturing in the period during which the contract is due. The table does not reflect the effects of possible prepayments.

(in thousands)	One Year or Less Amount	One to Five Years Amount	Over Five Years to Fifteen Years Amount	After Fifteen Years Amount	Total
	As of September 30, 2023				
Real estate:					
Residential	$ 121,641	$ 205,760	$ 89,464	$ 141,282	$ 558,147
Commercial	140,283	258,037	269,095	3,179	670,594
Construction	211,903	60,475	8,527	—	280,905
Commercial and Industrial	69,730	80,799	70,507	15,746	236,782
Credit card	122,533	—	—	—	122,533
Other consumer	335	363	250	—	948
Total portfolio loans, gross	$ 666,425	$ 605,434	$ 437,843	$ 160,207	$ 1,869,909

Loans above maturing after one year categorized by rate characteristic:	Predetermined Interest Rates	Floating or Variable Rates	Total
Real estate:			
Residential	$ 252,151	$ 184,355	$ 436,506
Commercial	358,871	171,440	530,311
Construction	11,922	57,080	69,002
Commercial and Industrial	108,630	58,422	167,052
Other consumer	576	37	613
Total portfolio loans, gross	$ 732,150	$ 471,334	$ 1,203,484

In addition to the portfolio loans shown above, gross SBA-PPP loans receivable, which totaled $0.8 million at September 30, 2023, mature in the one to five year time-frame and carry a fixed rate of interest.

The following table presents non owner-occupied commercial real estate loans and the weighted average loan-to-value ("LTV") by loan type:

(in thousands)	Amount	Weighted Average LTV(1)	% of Non Owner-Occupied Commercial Real Estate Loans	% of Total Portfolio Loans, Gross
	As of September 30, 2023			
Loan type:				
Retail	$ 104,147	53.0 %	29.7 %	5.6 %
Mixed use	75,132	49.1 %	21.4 %	4.0 %
Industrial	63,484	51.3 %	18.1 %	3.4 %
Hotel	60,692	48.1 %	17.3 %	3.2 %
Office	12,476	49.8 %	3.6 %	0.7 %
Other	34,663	51.2 %	9.9 %	1.9 %
Total non owner-occupied commercial real estate loans	$ 350,594	50.7 %	100.0 %	18.7 %
Total portfolio loans, gross	$ 1,869,909			

(1) Weighted average LTV is calculated by reference to the most recent available appraisal of the property securing each loan.

Nonperforming Assets

Loans are placed on nonaccrual status when, in management's opinion, the borrower may be unable to meet payment obligations as they become due, as well as when required by regulatory provisions. Loans may be placed on nonaccrual status regardless of whether or not such loans are considered past due. In general, we place loans on nonaccrual status when they become 90 days past due. We also place loans on nonaccrual status if they are less than 90 days past due if the collection of principal or interest is in doubt. When the interest accrual is discontinued, all unpaid accrued interest is reversed from income.

Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are, in management's opinion, reasonably assured.

Loans are generally charged-off in part or in full when management determines the loan to be uncollectible. Factors for charge-off that may be considered include: repayments deemed to be extended out beyond reasonable time frames, customer bankruptcy and lack of assets, and/or collateral deficiencies. Consumer credit card balances are moved into the charge off queue after they become more than 90 days past due and are charged off not later than 120 days after they become past due. Otherwise, loans that are past due for 180 days or more are charged off unless the loan is well secured and in the process of collection.

The Company believes its approach to lending and the management of nonperforming assets has resulted in sound asset quality and timely resolution of problem assets. The Company has established underwriting guidelines to be followed by our bankers, and routinely monitors our delinquency levels for any negative or adverse trends. There can be no assurance, however, that our loan portfolio will not become subject to increasing pressures from deteriorating borrower credit.

From a credit risk standpoint, we grade watchlist and problem loans into one of five credit quality indicators: pass/watch, special mention, substandard, doubtful or loss. The classifications of loans reflect a judgment about the risks of default and loss associated with each loan. Credit ratings are reviewed regularly and adjusted regularly to reflect the degree of risk and loss that our management believes to be appropriate for each credit. Our lending policy requires the routine monitoring of past due reports, daily overdraft reports, monthly maturing loans, monthly risk rating reports and internal loan review reports. The lending and credit management of the Bank meet periodically to review loans rated pass/watch. The focus of each meeting is to identify and promptly determine any necessary required action within this loan population, which consists of loans that, although considered satisfactory and performing to terms, may exhibit special risk features that warrant management's attention.

Management is intent on maintaining a strong credit review function and risk rating process. The Company has an experienced Credit Administration function, which provides independent analysis of credit requests and the management of problem credits. The Credit Department has developed and implemented analytical procedures for evaluating credit requests, has refined the Company's risk rating system, and continues to adapt and enhance the monitoring of the loan portfolio. The loan portfolio analysis process is intended to contribute to the identification of weaknesses before they become more severe.

A special mention loan has potential weaknesses deserving of management's attention. If uncorrected, such weaknesses may, at a future date, impair the repayment prospects for the asset or our credit position.

Loans that are deemed special mention, substandard, doubtful or loss are listed in the Bank's Problem Loan Status Report. The Problem Loan Status Report provides a detailed summary of the borrower and guarantor status, loan accrual status, collateral evaluation and includes a description of the planned collection and administration program designed to mitigate the Bank's risk of loss and remove the loan from problem status. The Special Asset Committee reviews the Problem Loan Status Report on a quarterly basis for borrowers with an overall loan exposure in excess of $250,000.

At September 30, 2023, the recorded investment in individually assessed loans was $15.3 million, requiring a specific reserve of $0.7 million. At December 31, 2022, prior to the adoption of CECL, the Company carried a recorded investment in impaired loans of $9.4 million, $0.5 million of which required a specific reserve of $0.4 million. The $15.3 million of individually assessed loans at September 30, 2023 included a single $8.2 million, multi-unit residential real estate loan that was downgraded in the first quarter of 2023.

Allowance for Credit Losses

As discussed in Note 1 to the Unaudited Consolidated Financial Statements, we maintain an ACL that represents management's estimate of expected credit losses and risks inherent in our loan portfolio. The balance of the ACL is based on internally assigned risk classifications of loans, historical loss rates, changes in the nature of our loan portfolio, overall portfolio quality, industry concentrations, delinquency trends, current economic factors and the estimated impact of current economic conditions on certain historical loss rates.

A major consideration in the determination of the allowance for credit loss on the credit card portfolio is based on historical loss experience in that portfolio. The Company calculates the credit card ACL collectively, applying segmentation based on collateral positions: secured, partially secured, and unsecured.

The following table presents key ratios for the ACL and nonaccrual loans for the periods indicated:

	Allowance for credit losses to period end portfolio loans [1]		**Nonaccrual loans to total portfolio loans**		**Allowance for credit losses to nonaccrual loans [1]**	
(in thousands)	**September 30, 2023**	**December 31, 2022**	**September 30, 2023**	**December 31, 2022**	**September 30, 2023**	**December 31, 2022**
Real estate:						
Residential	1.04 %	1.13 %	2.20 %	0.88 %	47 %	128 %
Commercial	1.52	1.22	0.09	0.24	1,756	518
Construction	0.80	1.59	0.72	1.19	111	133
Commercial and Industrial	1.77	1.33	0.15	0.32	1,188	417
Credit card	4.75	4.73	—	—	—	—
Other consumer	0.95	0.88	—	—	—	—
Total	1.52 %	1.53 %	0.82 %	0.56 %	186 %	270 %

(1) Allowance calculation excludes SBA-PPP loans.

Total charge-offs for the quarters ended September 30, 2023 and September 30, 2022 were primarily due to credit card charge-offs resulting both from the aging of the portfolio and the shift from an almost exclusively secured card portfolio to a portfolio that also includes partially secured and unsecured exposures. Commercial real estate loans experienced net charge-offs for the nine months ended September 30, 2023 of $1.0 million. Commercial real estate loans experienced net charge-offs for the quarter ended September 30, 2023 of $0.1 million. There were no charge-offs for the commercial loan portfolio for the nine months ended September 30, 2022. The following tables present a summary of the net charge-offs (recovery) of loans as a percentage of average loans for the periods indicated:

	Three Months Ended September 30,					
	2023			**2022**		
(in thousands)	**Net Charge-offs (Recoveries)**	**Average Loans**	**Percent of average portfolio loans[1]**	**Net Charge-offs**	**Average Loans**	**Percent of averag portfolio loans(1**
Real estate:						
Residential	$ —	$ 571,115	— %	$ —	$ 439,603	—
Commercial	(39)	655,743	(0.02)	—	605,433	—
Construction	—	274,792	—	—	240,971	—
Commercial and Industrial	66	227,515	0.12	—	182,113	—
Credit card	1,753	116,814	5.95	1,588	132,246	4.76
Other consumer	—	887	—	—	1,180	—
Total	$ 1,780	$ 1,846,866	0.38 %	$ 1,588	$ 1,601,546	0.39

(in thousands)	Nine Months Ended September 30, 2023					
	2023			2022		
	Net Charge-offs (Recoveries)	Average Loans	Percent of average portfolio loans[1]	Net Charge-offs	Average Loans	Percent of average portfolio loans[1]
Real estate:						
Residential	$ —	$ 551,280	— %	$ —	$ 422,024	— %
Commercial	(39)	653,467	(0.01)	—	577,347	—
Construction	—	259,602	—	—	245,546	—
Commercial and Industrial	999	219,297	0.61	—	174,505	—
Credit card	5,036	114,416	5.88	3,337	127,266	3.51
Other consumer	—	1,693	—	—	698	—
Total	$ 5,996	$ 1,799,755	0.45 %	$ 3,337	$ 1,547,386	0.29 %

(1) Annualized.

As the loan portfolio and ACL review processes continue to evolve, there may be changes to elements of the allowance and this may influence the overall level of the allowance maintained. Historically, the Bank has enjoyed a high-quality loan portfolio with relatively low levels of net charge-offs and low delinquency rates. The maintenance of a high-quality portfolio will continue to be a priority.

Although we believe we have established our ACL in accordance with GAAP and that the ACL is currently adequate to provide for known and inherent losses in the portfolio at all times shown above, future provisions for credit losses will be subject to ongoing evaluations of the risks in our loan portfolio.

The following table shows the allocation of the ACL among loan categories as of the dates indicated. The total allowance is available to absorb losses from any loan category.

(in thousands)	September 30, 2023		December 31, 2022	
	Amount	Percent [1]	Amount	Percent [1]
Real estate:				
Residential	**$ 5,779**	**20 %**	$ 5,481	21 %
Commercial	**10,221**	**36 %**	8,098	31 %
Construction	**2,251**	**8 %**	3,782	14 %
Commercial and Industrial	**4,195**	**15 %**	2,935	11 %
Credit card	**5,824**	**21 %**	6,078	23 %
Other consumer	**9**	**— %**	11	— %
Total allowance for credit losses	**$ 28,279**	**100 %**	$ 26,385	100 %

(1) Loan category as a percentage of total portfolio loans which excludes SBA-PPP loans.

Total Liabilities

Total liabilities at September 30, 2023 increased $130.0 million from December 31, 2022, primarily due to growth in the deposit portfolio of $209.9 million, partially offset by an $85.0 million reduction in FHLB advances.

Deposits

Deposits are a major source of funding for the Company. We offer a variety of deposit products including interest-bearing demand, savings, money market and time accounts, all of which we actively market at competitive pricing. We generate deposits from our customers on a relationship basis and through the efforts of our commercial lending officers and our business banking officers. Our credit card customers are a significant source of low cost deposits. As of September 30, 2023 and December 31, 2022, our credit card customers accounted for $181.2 million and $187.4 million, or 26.6% and 27.8%, respectively, of our total noninterest-bearing deposit balances.

The following table presents the average balances and average rates paid on deposits for the periods indicated:

	For the Nine Months Ended September 30, 2023		For the Year Ended December 31, 2022	
(in thousands)	**Average Balance**	**Average Rate[1]**	Average Balance	Average Rate[1]
Interest-bearing demand accounts	**$ 203,099**	**0.14 %**	$ 253,923	0.07 %
Savings	**5,965**	**0.13**	8,917	0.06
Money market accounts	**628,977**	**3.48**	553,388	0.82
Time deposits	**353,635**	**4.27**	165,854	1.75
Total interest-bearing deposits	**1,191,676**	**3.13**	982,082	0.77
Noninterest-bearing demand accounts	**665,821**		781,971	
Total deposits	**$ 1,857,497**	**2.01 %**	$ 1,764,053	0.43 %

(1) Annualized

Deposit costs increased 158 basis points during the nine months ended September 30, 2023 owing in large part to a series of interest rate increases implemented by the Federal Reserve beginning in early 2022 and the corresponding move from savings accounts to higher rate money market accounts and time deposits. In addition, Average noninterest-bearing deposit balances decreased $116.1 million when compared to December 31, 2022, largely due to the decision by some depositors to move balances from noninterest-bearing deposit accounts to interest-bearing deposit accounts.

The following table presents the maturities of our certificates of deposit as of September 30, 2023.

(in thousands)	**Three Months or Less**	**Over Three Through Six Months**	**Over Six Through Twelve Months**	**Over Twelve Months**	**Total**
$250,000 or more	$ 24,429	$ 24,501	$ 20,080	$ 53,162	$ 122,172
Less than $250,000	65,232	97,279	76,160	22,847	261,518
Total	$ 89,661	$ 121,780	$ 96,240	$ 76,009	$ 383,690

At September 30, 2023, the Company had $383.7 million in total time deposits, an increase of $90.3 million from December 31, 2022. Total brokered time deposits of $128.7 million at September 30, 2023 decreased $3.2 million from $131.8 million at December 31, 2022. Total brokered time deposits as a percentage of total deposits was 6.5% at September 30, 2023.

As of September 30, 2023 and December 31, 2022, based on the methodologies and assumptions used for the Bank's regulatory reporting requirements, approximately $857.7 million or 43.6% and $784.6 million or 44.6%, respectively, of the deposit portfolio was uninsured. Uninsured deposits are comprised of the portion of account balances that are in excess of FDIC insurance limits.

Deposits securing our OpenSky® card lines of credit and deposits from title companies represent the largest concentrations in the deposit portfolio. As of September 30, 2023, these deposits represented 9%

and 15% of deposits, respectively. As of December 31, 2022, these concentrations were 11% and 13% of deposits.

Borrowings

We utilize short-term and long-term borrowings to supplement deposits to fund our lending and investment activities, each of which is discussed below. Despite the uncertain market conditions during the first quarter of 2023 following the closures of Silicon Valley Bank and Signature Bank, our total borrowings decreased during the nine months ended September 30, 2023 to $34.1 million from $119.1 million at December 31, 2022 as our deposits increased during the year.

FHLB Advances. The FHLB allows us to borrow up to 25% of our assets on a blanket floating lien status collateralized by certain securities and loans. As of September 30, 2023, approximately $543.5 million in real estate loans were pledged as collateral to the FHLB and our total borrowing capacity from the FHLB was $369.7 million. As of September 30, 2023, no investment securities were pledged with the FHLB. We utilize these borrowings to meet liquidity needs and to fund certain fixed rate loans in our portfolio. As of September 30, 2023, we had $22.0 million in outstanding advances and $347.7 million in available borrowing capacity from the FHLB.

Other Borrowed Funds. The Company has also issued junior subordinated debentures and other subordinated notes. At September 30, 2023, these other borrowings amounted to $12.1 million, consisting of Floating Rate Junior Subordinated Deferrable Interest Debentures and subordinated notes.

At September 30, 2023, our Floating Rate Junior Subordinated Deferrable Interest Debentures amounted to $2.1 million. The Floating Rate Junior Subordinated Deferrable Interest Debentures (the “Floating Rate Debentures”) were issued in June of 2006, mature on June 15, 2036, and may be redeemed prior to that date under certain circumstances. The principal amount of the Floating Rate Debentures has not changed since issuance, and they accrue interest at a floating rate equal to the three-month CME Term SOFR plus a spread adjustment of 0.26161 percent (or 26.161 bps) plus 187 basis points, payable quarterly. As of September 30, 2023, the rate for the Floating Rate Debentures was 7.54%.

On November 30, 2020, the Company issued $10.0 million in subordinated notes due in 2030 (the “Notes”). The Notes have a ten year term and have a fixed rate of 5.00% for the first five years; thereafter, the rate resets quarterly to a benchmark rate, which is expected to be the three-month SOFR, plus 490 basis points. The Notes may be redeemed in part or in whole, upon the occurrence of certain events.

Federal Reserve Bank of Richmond. The Federal Reserve Bank of Richmond has an available borrower in custody arrangement which allows us to borrow on a collateralized basis. The Company’s borrowing capacity under the Federal Reserve’s discount window program was $16.8 million as of September 30, 2023. Certain commercial loans are pledged under this arrangement. During the first quarter of 2023, we established a line of credit under the Federal Reserve Bank’s Bank Term Funding Program (“BTFP”). We have pledged $150.0 million of U.S. Treasury securities to the Federal Reserve Bank which gives rise to $150.0 million of borrowing capacity. We maintain these borrowing arrangements to meet liquidity needs pursuant to our contingency funding plan. There were no outstanding balances on these lines at September 30, 2023.

The Company also has available lines of credit of $76.0 million with other correspondent banks at September 30, 2023, as well as access to certificate of deposit funding through financial intermediaries. There were no outstanding balances on the lines of credit from correspondent banks at September 30, 2023.

Liquidity

Liquidity is defined as the Bank’s capacity to meet its cash and collateral obligations at a reasonable cost. Maintaining an adequate level of liquidity depends on the Bank’s ability to meet both expected and unexpected cash flows and collateral needs efficiently without adversely affecting either daily operations or the financial condition of the Bank. 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. The Bank’s obligations, and the funding sources used to meet them, depend significantly on our business mix, balance sheet structure and the cash flow profiles of our on- and off-balance sheet obligations. In managing our cash flows, management regularly addresses situations that can give rise to increased liquidity risk. These include funding mismatches, market constraints on the ability to convert assets into cash or in accessing sources of funds (i.e., market liquidity) and contingent liquidity events. Changes in economic conditions or exposure to credit, market, operational, legal and reputational risks also could affect the Bank’s liquidity risk profile and are considered in the assessment of liquidity and asset/liability management.

Management has established a risk 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 integrated into our risk management processes. Critical elements of our liquidity risk management include: corporate governance consisting of oversight by the board of directors and active involvement by management; strategies, policies, procedures, and limits used to manage and mitigate liquidity risk; liquidity risk measurement and monitoring systems (including assessments of the current and prospective cash flows or sources and uses of funds) that are believed to be commensurate with the complexity and business activities of the Bank; active management of intraday liquidity and collateral; a diverse mix of existing and potential future funding sources; holding liquid marketable securities that can be used to meet liquidity needs in situations of stress; contingency funding plans that address potential adverse liquidity events and emergency cash flow requirements; and internal controls and internal audit processes believed to be sufficient to assure the adequacy of the institution’s liquidity risk management process.

We expect funds to be available from a number of basic banking activity sources, including the core deposit base, the repayment and maturity of loans and investment security cash flows. Other potential funding sources include brokered certificates of deposit, deposit listing services, CDARS, borrowings from the FHLB and other lines of credit.

As of September 30, 2023, we had $347.7 million of available borrowing capacity from the FHLB, $16.8 million of available borrowing capacity from the Federal Reserve Bank of Richmond Borrower in Custody program and available lines of credit of $76.0 million with other correspondent banks. At September 30, 2023, the Company also had $150.0 million available through the BTFP, which provides funding collateralized by designated investment securities. The BTFP was established in March 2023 to make additional funding available to banks to ensure they could meet the needs of depositors and to eliminate the need for banks to sell securities in times of stress. There were no borrowings outstanding under this facility at the end of the current period. Further, unpledged investment securities available as collateral for potential additional borrowings totaled $56.1 million at September 30, 2023. Cash and cash equivalents were $146.2 million at September 30, 2023.

Capital Resources

Stockholders’ equity increased $18.9 million for the period ended September 30, 2023 compared to December 31, 2022 largely due to net income of $26.8 million for the nine months ended September 30, 2023. Shares repurchased during the three months ended September 30, 2023 as part of the Company’s stock repurchase program totaled 100,575 shares at an average price of $19.47, for a total cost of $2.0 million including commissions. Shares repurchased during the nine months ended September 30, 2023 as part of the Company's stock repurchase program totaled 385,919 shares at an average price of $18.12, for a total cost of $7.0 million including commissions.

The Company's total stockholders' equity is affected by fluctuations in the fair values of investment securities available for sale. The difference between amortized cost and fair value of investment securities, net of deferred income tax, is included in accumulated other comprehensive loss within stockholders' equity. Accumulated other comprehensive loss is excluded from the Bank's and Company's regulatory capital ratios. The balance in accumulated other comprehensive loss related to unrealized losses on available-for-sale debt securities, net of deferred income tax, amounted to $17.8 million at September 30, 2023 and $16.8 million at December 31, 2022. Changes in accumulated other comprehensive loss are excluded from earnings and directly increase or decrease stockholders' equity. To the extent unrealized losses on investment securities available for sale result from credit losses, unrealized losses are recorded as a charge against earnings. The investment securities section of Management's Discussion and Analysis and Notes 1 and 3 to the unaudited consolidated financial statements provide additional information concerning management's evaluation of investment securities available for sale for credit losses at September 30, 2023.

The Company uses several indicators of capital strength. The most commonly used measure is average common equity to average assets (computed as average equity divided by average total assets), which was 10.93% at September 30, 2023 and 10.22% at December 31, 2022.

The Bank is subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can precipitate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a material effect on the Company's financial condition. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of its assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting practices. The capital amounts and classifications are also subject to qualitative judgments by the regulators.

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum ratios of common equity Tier 1, Tier 1, and total capital as a percentage of assets and off-balance sheet exposures, adjusted for risk weights ranging from 0% to 1,250%. The Bank is also required to maintain capital at a minimum level based on quarterly average assets, which is known as the leverage ratio.

In July 2013, federal bank regulatory agencies issued a final rule that revised their risk-based capital requirements and the method for calculating risk-weighted assets to make them consistent with certain standards that were developed by Basel III and certain provisions of the Dodd-Frank Act. The final rule applies to all depository institutions and bank holding companies and savings and loan holding companies with total consolidated assets of more than $1 billion. The Bank was required to implement the new Basel III capital standards (subject to the phase-in for certain parts of the new rules) as of January 1, 2015. In August of 2018 the Regulatory Relief Act directed the Federal Reserve Board to revise the Small BHC Policy Statement to raise the total consolidated asset limit in the Small BHC Policy Statement from $1 billion to $3 billion. The Company is currently exempt from the consolidated capital requirements.

The ability of the Company to continue to grow is dependent on its earnings and those of the Bank, and the ability to obtain additional funds for contribution to the Bank's capital, through additional borrowings, through the sale of additional common stock or preferred stock, or through the issuance of additional qualifying capital instruments, such as subordinated debt. The capital levels required to be maintained by the Company and Bank may be impacted as a result of the Bank's concentrations in commercial real estate loans. See "Risks Related to the Regulation of Our Industry" in Part I, Item 1A - Risk Factors in the Annual Report on Form 10-K for the year ended December 31, 2022.

As of September 30, 2023, the Bank was in compliance with all applicable regulatory capital requirements to which it was subject, and the Bank was classified as “well capitalized” for purposes of the prompt corrective action regulations. As we deploy our capital and continue to grow our operations, our regulatory capital levels may decrease depending on our level of earnings. However, we intend to monitor and control our growth relative to our earnings in order to remain in compliance with all regulatory capital standards applicable to us.

The following table presents the regulatory capital ratios for the Company and the Bank as of the dates indicated.

(in thousands)	Actual		Minimum Capital Adequacy		To Be Well Capitalized	
September 30, 2023	**Amount**	**Ratio**	**Amount**	**Ratio**	**Amount**	**Ratio**
The Company						
Tier 1 leverage ratio (to average assets)	**$ 260,721**	**11.62 %**	**$ 89,713**	**4.00 %**	**N/A**	**N/A**
Tier 1 capital (to risk-weighted assets)	**260,721**	**15.27**	**102,472**	**6.00**	**N/A**	**N/A**
Common equity tier 1 capital ratio (to risk-weighted assets)	**260,721**	**15.27**	**76,854**	**4.50**	**N/A**	**N/A**
Total capital ratio (to risk-weighted assets)	**292,166**	**17.11**	**136,630**	**8.00**	**N/A**	**N/A**
The Bank						
Tier 1 leverage ratio (to average assets)	**$ 219,909**	**10.04 %**	**$ 87,600**	**4.00 %**	**$ 109,500**	**5.00 %**
Tier 1 capital (to risk-weighted assets)	**219,909**	**13.25**	**99,549**	**6.00**	**132,732**	**8.00**
Common equity tier 1 capital ratio (to risk-weighted assets)	**219,909**	**13.25**	**74,662**	**4.50**	**107,845**	**6.50**
Total capital ratio (to risk-weighted assets)	**240,745**	**14.51**	**132,732**	**8.00**	**165,915**	**10.00**
December 31, 2022						
The Company						
Tier 1 leverage ratio (to average assets)	$ 242,829	11.24 %	$ 86,442	4.00 %	N/A	N/A
Tier 1 capital (to risk-weighted assets)	242,829	15.13	96,315	6.00	N/A	N/A
Common equity tier 1 capital ratio (to risk-weighted assets)	240,767	15.00	72,237	4.50	N/A	N/A
Total capital ratio (to risk-weighted assets)	262,217	16.33	128,421	8.00	N/A	N/A
The Bank						
Tier 1 leverage ratio (to average assets)	$ 199,846	9.47 %	$ 84,416	4.00 %	$ 105,521	5.00 %
Tier 1 capital (to risk-weighted assets)	199,846	12.95	92,574	6.00	123,432	8.00
Common equity tier 1 capital ratio (to risk-weighted assets)	199,846	12.95	69,431	4.50	100,289	6.50
Total capital ratio (to risk-weighted assets)	219,234	14.21	123,432	8.00	154,290	10.00

Contractual Obligations

We have contractual obligations to make future payments on debt agreements. Our liquidity monitoring and management consider both present and future demands for and sources of liquidity.

Off-Balance Sheet Items

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 customers. These transactions include commitments to extend credit and issue 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. Our exposure to credit loss is represented by the contractual amounts of these commitments. The same credit policies and procedures are generally used in making these commitments as for on-balance sheet instruments. We are not aware of any accounting loss to be incurred by funding these commitments; however, we maintain a reserve for unfunded commitments and certain off-balance sheet credit risks, which is recorded in other liabilities on the consolidated balance sheet.

Our commitments associated with outstanding letters of credit and commitments to extend credit expiring by period as of the date indicated are summarized below. Since commitments associated with letters of credit and commitments to extend credit may expire unused, the amounts shown do not necessarily reflect actual future cash funding requirements.

(in thousands)	As of September 30, 2023	As of December 31, 2022
Unfunded lines of credit	**$ 357,548**	$ 345,063
Letters of credit	**4,641**	5,105
Commitment to fund other investments	**3,874**	4,365
Total credit extension commitments	**$ 366,063**	$ 354,533

Unfunded lines of credit represent unused credit facilities to our current borrowers. Lines of credit generally have variable interest rates. Letters of credit are conditional commitments issued by us to guarantee the performance of a customer to a third party. In the event of nonperformance by the customer 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 customer from the underlying collateral, which can include commercial real estate, physical plant and property, inventory, receivables, cash and/or marketable securities. Our policies generally require that letter of credit arrangements contain security and debt covenants similar to those contained in loan agreements. We believe the credit risk associated with issuing letters of credit is substantially the same as the risk involved in extending loan facilities to our customers.

We seek to minimize our exposure to loss under letters of credit and credit commitments by subjecting them to the same credit approval and monitoring procedures as we do for on-balance sheet instruments. The effect on our revenue, expenses, cash flows and liquidity of the unused portions of these letters of credit commitments cannot be precisely predicted because we do not control the extent to which the lines of credit may be used.

Commitments to extend credit are agreements to lend funds to a customer, as long as there is no violation of any condition established in the contract. Commitments generally have variable interest rates, fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being fully drawn, the total commitment amounts disclosed above do not necessarily represent future cash requirements. We evaluate each customer’s creditworthiness on a case-by-case basis. The amount of collateral obtained, if considered necessary by us, upon extension of credit is based on management’s credit evaluation of the customer.

We enter into forward commitments for the delivery of mortgage loans in our current pipeline. Interest rate lock commitments are entered into in order to economically hedge the effect of changes in interest rates resulting from our commitments to fund the loans. These commitments to fund mortgage loans to be sold into the secondary market, along with the interest rate lock commitments and forward commitments for the future delivery of mortgage loans to third party investors, are considered derivatives.

The commitment to fund other investments reflects an obligation to make an investment in a Small Business Investment Company.

Impact of Inflation

The consolidated financial statements and related notes included elsewhere in this report have been prepared in accordance with GAAP. GAAP requires the measurement of financial position and operating results in terms of historical dollars, without considering changes in the relative value of money over time due to inflation or recession.

Unlike many industrial companies, substantially all of the Company’s assets and liabilities are monetary in nature. As a result, interest rates have a more significant impact on our performance than the effects of general levels of inflation. Interest rates may not necessarily move in the same direction or in the same magnitude as the prices of goods and services. However, most other operating expenses are sensitive to changes in levels of inflation.

Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Interest Rate Sensitivity and Market Risk

As a financial institution, our primary component of market risk is interest rate volatility. Our asset liability and funds management policy provides management with the guidelines for funds management, and we have established a measurement system for monitoring our net interest rate sensitivity position**.** We endeavor to manage our sensitivity position within our established guidelines.

Fluctuations in interest rates will ultimately impact both the level of income and the market value of all interest earning assets and interest-bearing liabilities, other than those that have a short term to maturity. Interest rate risk is the potential of economic losses due to future interest rate changes. These economic losses can be reflected as a loss of future net interest income and/or a loss of current fair market values. The objective is to measure the effect on net interest income and to adjust the balance sheet to minimize the inherent risk while at the same time maximizing income.

We endeavor to manage our exposure to interest rates by structuring our balance sheet in the ordinary course of business. We do not enter into instruments such as leveraged derivatives, financial options or financial futures contracts for the purpose of reducing interest rate risk. We endeavor to hedge the interest rate risks of our available for sale mortgage pipeline by using mortgage-backed securities, and short positions. Based on the nature of our operations, we are not subject to foreign exchange or commodity price risk. We do not own any trading assets.

Our exposure to interest rate risk is managed by the Bank’s Asset/Liability Management Committee (“ALCO”) in accordance with policies approved by our board of directors. The ALCO formulates strategies based on perceived levels of interest rate risk. In determining the appropriate level of interest rate risk, the committee considers the impact on earnings and capital of the current outlook for interest rates, potential changes in interest rates, regional economies, liquidity, business strategies and other factors. The ALCO meets regularly to review, among other things, the sensitivity of assets and liabilities to interest rate changes, the book and market values of assets and liabilities, unrealized gains and losses, purchase and sale activities, commitments to originate loans and the maturities of investments and borrowings. Additionally, the ALCO reviews liquidity, cash flow flexibility, maturities of deposits and consumer and commercial deposit activity. Management employs methodologies to manage interest rate risk, which include an analysis of relationships between interest earning assets and interest-bearing liabilities and an interest rate shock simulation model.

The following table indicates that, for periods less than one year, rate-sensitive assets exceeded rate-sensitive liabilities, resulting in an asset-sensitive position. For a bank with an asset-sensitive position, or positive gap, rising interest rates would generally be expected to have a positive effect on net interest income, and falling interest rates would generally be expected to have the opposite effect.

INTEREST SENSITIVITY GAP

September 30, 2023 (in thousands)	Within One Month	After One Month Through Three Months	After Three Through Twelve Months	Within One Year	Greater Than One Year or Non-Sensitive	Total
Assets						
Interest earning assets						
Loans [1]	353,075	$ 455,967	$ 283,232	1,092,274	$ 746,969	$ 1,839,243
Securities	22,012	1,148	40,393	63,553	146,842	210,395
Interest-bearing deposits at other financial institutions	130,428	—	—	130,428	13,767	144,195
Federal funds sold	1,957	—	—	1,957	—	1,957
Total earning assets	$ 507,472	$ 457,115	$ 323,625	$ 1,288,212	$ 907,578	$ 2,195,790
Liabilities						
Interest-bearing liabilities						
Interest-bearing deposits	$ 13,507	$ 27,015	$ 121,566	162,088	$ 741,407	$ 903,495
Time deposits	37,922	51,739	218,020	307,681	76,009	383,690
Total interest-bearing deposits	51,429	78,754	339,586	469,769	817,416	1,287,185
FHLB Advances	—	—	—	—	22,000	22,000
Other borrowed funds	—	—	—	—	12,062	12,062
Total interest-bearing liabilities	$ 51,429	$ 78,754	$ 339,586	$ 469,769	$ 851,478	$ 1,321,247
Period gap	$ 456,043	$ 378,361	$ (15,961)	$ 818,443	$ 56,100	$ 874,543
Cumulative gap	$ 456,043	$ 834,404	$ 818,443	$ 818,443	$ 874,543	
Ratio of cumulative gap to total earning assets	20.77 %	38.00 %	37.27 %	37.27 %	39.83 %	

(1) Includes loans held for sale and loans made under the SBA-PPP loan program.

We use quarterly Earnings at Risk ("EAR") simulations to assess the impact of changing interest rates on our earnings under a variety of scenarios and time horizons. These simulations utilize both instantaneous and parallel changes in the level of interest rates, as well as 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 new growth. Dynamic simulation models are also utilized that rely on assumptions regarding changes in existing lines of business, new business, and changes in management and client behavior.

We also use economic value-based methodologies to measure the degree to which the economic values of the Bank's positions change under different interest rate scenarios. The economic-value approach focuses on a longer-term time horizon and endeavors to capture all future cash flows expected from existing assets and liabilities. The economic value model utilizes a static approach in that the analysis does not incorporate new business; rather, the analysis shows a snapshot in time of the risk inherent in the balance sheet.

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 decay rates, and key rate drivers. Because of the inherent use of these estimates and assumptions in the model, our actual results may, and very 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 decrease liability duration in order to reduce asset sensitivity, or to decrease asset duration and increase liability duration in order to increase asset sensitivity.

The following table summarizes the results of our EAR analysis in simulating the change in net interest income and fair value of equity over a 12-month horizon as of September 30, 2023:

IMPACT ON NET INTEREST INCOME UNDER A STATIC BALANCE SHEET, PARALLEL INTEREST RATE SHOCK

Earnings at Risk	-300 bps	-200 bps	-100 bps	Flat	+100 bps	+200 bps	+300 bps
September 30, 2023	(5.1)%	(4.5)%	(2.5)%	0.0 %	2.4 %	4.7 %	7.1 %

Utilizing an economic value of equity ("EVE") approach, we analyze the risk to capital from the effects of various interest rate scenarios through a long-term discounted cash flow model. This measures the difference between the economic value of our assets and the economic value of our liabilities, which is a proxy for our liquidation value. While this provides some value as a risk measurement tool, management believes EAR is more appropriate in accordance with the going concern principle.

The following table illustrates the results of our EVE analysis as of September 30, 2023.

ECONOMIC VALUE OF EQUITY ANALYSIS UNDER A STATIC BALANCE SHEET, PARALLEL INTEREST RATE SHOCK

Economic Value of Equity	-300 bps	-200 bps	-100 bps	Flat	+100 bps	+200 bps	+300 bps
September 30, 2023	(4.7)%	(1.6)%	(0.2)%	0.0 %	(0.4)%	(1.3)%	(1.5)%

Item 4. CONTROLS AND PROCEDURES.

Evaluation of Disclosure Controls and Procedures

The Company's management, including our Principal Executive Officer and Principal Financial Officer, have evaluated the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e)) under the Securities Exchange Act of 1934, as amended (the "Exchange Act") as of the end of the period covered by this report. Based upon that evaluation, our Principal Executive Officer and Principal Financial Officer concluded that our disclosure controls and procedures were effective to ensure that information required to be disclosed in the reports we file and submit under the Exchange Act is (i) recorded, processed, summarized and reported as and when required and (ii) accumulated and communicated to our management, including our Principal Executive Officer and the Principal Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

Changes in Internal Control over Financial Reporting

There have been no changes, in the Company's internal control over financial reporting (as such term is defined in Rule 13a-15(f) under the Exchange Act) during the fiscal quarter to which this report relates that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. LEGAL PROCEEDINGS.

From time to time, we are a party to various litigation matters incidental to the ordinary conduct of our business. We are not presently a party to any material legal proceedings.

Item 1A. RISK FACTORS.

There are no material changes to the risk factors as previously disclosed under Item 1A in our Annual Report on Form 10-K for the year ended December 31, 2022 and our Form 10-Q for the first quarter of 2023.

Item 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS.

There were no unregistered sales of the Company’s stock during the year to date period ended September 30, 2023.

On July 25, 2022, the Company announced a new stock repurchase program. Under the new program, the Company is authorized to repurchase up to $10.0 million of its outstanding common stock or 500,000 shares of Common Stock, par value $0.01 per share (“Common Stock”). On April 13, 2023, the Company announced approval of up to an additional $5.0 million or 175,000 shares of Common Stock incremental to the July 2022 announcement. The program will expire on December 31, 2024. There were no stock repurchases by the Company under the repurchase program announced on July 25, 2022, prior to the quarter ended March 31, 2023. During the three months ended September 30, 2023, the Company repurchased Common Stock under the stock repurchase program as reflected in the following table.

Period	Total Number of Shares Purchased	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs
July 1, 2023 to July 31, 2023	33,132	$ 19.10	318,476	$ 9,332,007
August 1, 2023 to August 31, 2023	41,779	19.91	360,255	8,500,166
September 1, 2023 to September 30, 2023	25,664	19.22	385,919	8,006,814

Item 3. DEFAULTS UPON SENIOR SECURITIES.

None.

Item 4. MINE SAFETY DISCLOSURES.

Not applicable.

Item 5. OTHER INFORMATION.

Rule 10b5-1 Trading Plans

During the quarter ended September 30, 2023, no officer or director of the Company adopted or terminated any contract, instruction, or written plan for the purchase or sale of securities of the Company's common stock that is intended to satisfy the affirmative defense conditions of Securities Exchange Act Rule 10b5-1(c) or any non-Rule 10b5-1 trading arrangement as defined in 17 CFR § 229.408(c).

Item 6. EXHIBITS.

Exhibit Number	Description
3.1	Amended and Restated Articles of Incorporation, as amended (incorporated by reference to Exhibit 3.1 to the Company's Form 8-K filed on May 23, 2023).
3.2	Amended and Restated Bylaws (incorporated by reference to Exhibit 3.2 to the Company's Form 8-K filed on May 23, 2023).
31.1	Rule 13a-14(a) Certification of the Principal Executive Officer.
31.2	Rule 13a-14(a) Certification of the Principal Financial Officer.
32.1	Section 1350 Certification of Principal Executive Officer and Principal Financial Officer.
101	The following materials from the Quarterly Report on Form 10-Q of Capital Bancorp, Inc. for the quarter ended September 30, 2023, formatted in eXtensible Business Reporting Language (XBRL): (i) Consolidated Balance Sheets, (ii) Consolidated Statements of Income, (iii) Consolidated Statements of Comprehensive Income, (iv) Consolidated Statement of Changes in Shareholders' Equity, (v) Consolidated Statements of Cash Flows and (vi) Notes to Unaudited Consolidated Financial Statements.
104	Cover Page Interactive Data File (formatted as Inline XBRL and contained in Exhibit 101).

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

CAPITAL BANCORP, INC.

Date: November 9, 2023 /s/ Ed Barry
Ed Barry
Chief Executive Officer
(Principal Executive Officer)

Date: November 9, 2023 /s/ Jay Walker
Jay Walker
Chief Financial Officer
(Principal Financial and Accounting Officer)

Section 2: EX-31.1 (RULE 13A-14(A) CERTIFICATION OF THE PRINCIPAL EXECUTIVE OFFICER)

Exhibit 31.1

Rule 13a-14(a) Certification of the Principal Executive Officer.

Exhibit 31.1

Rule 13a-14(a) Certification of the Principal Executive Officer.

I, Ed Barry, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Capital Bancorp, Inc.;

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, 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;

c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 9, 2023 By: /s/ Ed Barry
Ed Barry
Chief Executive Officer

Section 2: EX-31.2 (RULE 13A-14(A) CERTIFICATION OF THE PRINCIPAL FINANCIAL OFFICER)

Exhibit 31.2

Rule 13a-14(a) Certification of the Principal Financial Officer.

Exhibit 31.2

Rule 13a-14(a) Certification of the Principal Financial Officer.

I, Jay Walker, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Capital Bancorp, Inc.;

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, 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;

c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures as of the end of the period covered by this report based on such evaluation; and

d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 9, 2023 By: /s/ Jay Walker
Jay Walker
Principal Financial Officer

Section 2: EX-32.1 (Certification Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002)

Exhibit 32.1

Certification Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

Exhibit 32

Certification Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

In connection with the Quarterly Report of Capital Bancorp, Inc. (the “Company”) on Form 10-Q for the period ended September 30, 2023, as filed with the Securities and Exchange Commission on the date hereof (the “Report”), the undersigned hereby certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that to the undersigned’s best knowledge and belief:

1. The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

Date: November 9, 2023 By: /s/ Ed Barry
Ed Barry
Chief Executive Officer

By: /s/ Jay Walker
Jay Walker
Principal Financial Officer