



FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES

## **2022 FINANCIAL REPORTS**

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**

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## **Independent Auditor's Report**

To the Board of Directors  
First Farmers and Merchants Corporation

### ***Opinion***

We have audited the consolidated financial statements of First Farmers and Merchants Corporation (the "Company"), which comprise the consolidated balance sheet as of December 31, 2022 and the related consolidated statements of income, comprehensive income, stockholders' equity, and cash flows for the year then ended, and the related notes to the consolidated financial statements.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2022 and the results of its operations and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

### ***Basis for Opinion***

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

### ***Report on Prior Year Consolidated Financial Statements***

The consolidated financial statements of First Farmers and Merchants Corporation as of December 31, 2021 were audited by other auditors, who expressed an unmodified opinion on those statements on March 4, 2022.

### ***Responsibilities of Management for the Consolidated Financial Statements***

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

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

### ***Auditor's Responsibilities for the Audit of the Consolidated Financial Statements***

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

To the Board of Directors  
First Farmers and Merchants Corporation

In performing an audit in accordance with GAAS, we:

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

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

#### ***Other Information***

Management is responsible for the other information included in the annual report. The other information comprises the summary consolidated balance sheet and statement of income but does not include the consolidated financial statements and our auditor's report thereon. Our opinion on the consolidated financial statements does not cover the other information, and we do not express an opinion or any form of assurance thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and consider whether a material inconsistency exists between the other information and the consolidated financial statements or whether the other information otherwise appears to be materially misstated. If, based on the work performed, we conclude that an uncorrected material misstatement of the other information exists, we are required to describe it in our report.

*Plante & Moran, PLLC*

March 1, 2023

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**CONSOLIDATED BALANCE SHEETS**  
(Dollars in thousands, except per share data)

|                             |                                                                                                                                                               | December 31,<br>2022 | December 31,<br>2021 |
|-----------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------|----------------------|
| <b>ASSETS</b>               | Cash and due from banks                                                                                                                                       | \$ 27,193            | \$ 19,791            |
|                             | Interest-bearing deposits                                                                                                                                     | 1,754                | 75,065               |
|                             | Federal funds sold                                                                                                                                            | 57                   | 8,374                |
|                             | Total cash and cash equivalents                                                                                                                               | 29,004               | 103,230              |
|                             | Securities available-for-sale                                                                                                                                 | 810,591              | 876,987              |
|                             | Securities held-to-maturity (fair market value \$14,162<br>and \$15,932 as of the periods presented)                                                          | 15,087               | 15,128               |
|                             | Equity securities                                                                                                                                             | 2,505                | 2,481                |
|                             | Loans held-for-sale                                                                                                                                           | -                    | 2,197                |
|                             | Loans, net of deferred fees                                                                                                                                   | 966,167              | 886,891              |
|                             | Allowance for loan and lease losses                                                                                                                           | (9,382)              | (9,605)              |
|                             | Net loans                                                                                                                                                     | 956,785              | 877,286              |
|                             | Bank premises and equipment, net                                                                                                                              | 32,140               | 32,627               |
|                             | Bank-owned life insurance                                                                                                                                     | 35,829               | 35,354               |
|                             | Goodwill                                                                                                                                                      | 9,018                | 9,018                |
|                             | Net deferred tax asset                                                                                                                                        | 30,956               | 4,461                |
|                             | Other assets                                                                                                                                                  | 20,374               | 13,969               |
|                             | <b>TOTAL ASSETS</b>                                                                                                                                           | <b>\$ 1,942,289</b>  | <b>\$ 1,972,738</b>  |
| <b>LIABILITIES</b>          | Deposits:                                                                                                                                                     |                      |                      |
|                             | Non-interest-bearing                                                                                                                                          | \$ 534,474           | \$ 522,725           |
|                             | Interest-bearing                                                                                                                                              | 1,264,154            | 1,268,481            |
|                             | Total deposits                                                                                                                                                | 1,798,628            | 1,791,206            |
|                             | Accounts payable and other liabilities                                                                                                                        | 21,996               | 22,901               |
|                             | FHLB borrowings                                                                                                                                               | 25,000               | -                    |
|                             | <b>TOTAL LIABILITIES</b>                                                                                                                                      | <b>1,845,624</b>     | <b>1,814,107</b>     |
| <b>SHAREHOLDERS' EQUITY</b> | Commitments and contingencies (Note 11)                                                                                                                       |                      |                      |
|                             | Common stock - \$10 par value per share, 8,000,000 shares<br>authorized; 4,275,328 and 4,317,306 shares issued<br>and outstanding as of the periods presented | 42,753               | 43,173               |
|                             | Retained earnings                                                                                                                                             | 132,905              | 119,507              |
|                             | Accumulated other comprehensive loss                                                                                                                          | (79,088)             | (4,144)              |
|                             | Total shareholders' equity attributable to First Farmers and<br>Merchants Corporation                                                                         | 96,570               | 158,536              |
|                             | Non-controlling interest – preferred stock of subsidiary                                                                                                      | 95                   | 95                   |
|                             | <b>TOTAL SHAREHOLDERS' EQUITY</b>                                                                                                                             | <b>96,665</b>        | <b>158,631</b>       |
|                             | <b>TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY</b>                                                                                                             | <b>\$ 1,942,289</b>  | <b>\$ 1,972,738</b>  |

*The accompanying notes are an integral part of the consolidated financial statements.*

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF INCOME**  
(Dollars in thousands, except per share data)

|                                             |                                                                       | Years ended December 31, |           |           |
|---------------------------------------------|-----------------------------------------------------------------------|--------------------------|-----------|-----------|
|                                             |                                                                       | 2022                     | 2021      | 2020      |
| <b>INTEREST AND<br/>DIVIDEND<br/>INCOME</b> | Interest and fees on loans                                            | \$ 38,962                | \$ 38,491 | \$ 40,316 |
|                                             | Income on investment securities                                       |                          |           |           |
|                                             | Taxable interest                                                      | 10,004                   | 6,789     | 4,852     |
|                                             | Exempt from federal income tax                                        | 2,025                    | 2,169     | 1,985     |
|                                             | Interest from federal funds sold and other                            | 232                      | 88        | 170       |
|                                             | Total interest income                                                 | 51,223                   | 47,537    | 47,323    |
| <b>INTEREST<br/>EXPENSE</b>                 | Interest on deposits                                                  | 2,829                    | 2,380     | 3,750     |
|                                             | Interest on other borrowings                                          | 410                      | 1         | 44        |
|                                             | Total interest expense                                                | 3,239                    | 2,381     | 3,794     |
|                                             | Net interest income                                                   | 47,984                   | 45,156    | 43,529    |
|                                             | (Provision credit) provision for loan and lease losses                | (320)                    | (150)     | 700       |
|                                             | Net interest income after provision                                   | 48,304                   | 45,306    | 42,829    |
| <b>NON-INTEREST<br/>INCOME</b>              | Mortgage banking activities                                           | 614                      | 1,442     | 1,362     |
|                                             | Trust service fees                                                    | 4,160                    | 4,045     | 3,643     |
|                                             | Service fees on deposit accounts                                      | 7,655                    | 7,093     | 6,617     |
|                                             | Investment services fee income                                        | 406                      | 341       | 371       |
|                                             | Earnings on bank-owned life insurance                                 | 475                      | 554       | 551       |
|                                             | (Loss) gain on sales of securities                                    | (5)                      | 621       | 129       |
|                                             | Gain on redemption of bank-owned life insurance                       | -                        | -         | 820       |
|                                             | Net change in fair value of equity securities                         | 25                       | 239       | 242       |
|                                             | Gain on sale of Visa class B stock                                    | -                        | 1,811     | -         |
|                                             | Other non-interest income                                             | 817                      | 637       | 712       |
|                                             | Total non-interest income                                             | 14,147                   | 16,783    | 14,447    |
| <b>NON-INTEREST<br/>EXPENSE</b>             | Salaries and employee benefits                                        | 23,115                   | 26,499    | 24,229    |
|                                             | Net occupancy expense                                                 | 2,663                    | 2,699     | 2,478     |
|                                             | Depreciation expense                                                  | 1,786                    | 2,033     | 2,074     |
|                                             | Core provider expense                                                 | 2,528                    | 3,034     | 3,132     |
|                                             | Software support and other computer expense                           | 3,821                    | 2,875     | 2,554     |
|                                             | Legal and professional fees                                           | 1,007                    | 794       | 927       |
|                                             | Audits and exams expense                                              | 730                      | 637       | 726       |
|                                             | Advertising and promotions                                            | 1,074                    | 1,004     | 894       |
|                                             | FDIC insurance premium expense                                        | 677                      | 636       | 365       |
|                                             | Other non-interest expense                                            | 2,767                    | 2,755     | 2,902     |
|                                             | Total non-interest expenses                                           | 40,168                   | 42,966    | 40,281    |
|                                             | Income before provision for income taxes                              | 22,283                   | 19,123    | 16,995    |
|                                             | Provision for income taxes                                            | 4,217                    | 3,488     | 2,785     |
|                                             | Net income                                                            | 18,066                   | 15,635    | 14,210    |
|                                             | Non-controlling interest – dividends on preferred stock of subsidiary | 16                       | 16        | 16        |
|                                             | Net income available to common shareholders                           | \$ 18,050                | \$ 15,619 | \$ 14,194 |
|                                             | Weighted average shares outstanding                                   | 4,305,557                | 4,345,665 | 4,363,539 |
|                                             | Earnings per share                                                    | \$ 4.19                  | \$ 3.59   | \$ 3.25   |

*The accompanying notes are an integral part of the consolidated financial statements.*

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**  
(Dollars in thousands)

|                                                                                                                                          | <b>Years ended December 31,</b> |                        |                         |
|------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------|------------------------|-------------------------|
|                                                                                                                                          | <u><b>2022</b></u>              | <u><b>2021</b></u>     | <u><b>2020</b></u>      |
| Net income                                                                                                                               | \$ 18,066                       | \$ 15,635              | \$ 14,210               |
| Other comprehensive (loss) income                                                                                                        |                                 |                        |                         |
| Unrealized (depreciation) appreciation on available-for-sale securities, net of taxes of \$(26,485), \$(3,952) and \$2,049, respectively | (74,998)                        | (11,189)               | 6,167                   |
| Reclassification adjustment for realized losses (gains) included in net income, net of taxes of \$1, (\$162) and (\$34), respectively    | 4                               | (459)                  | (95)                    |
| Adjustment for amortization of net actuarial gains, net of taxes of (\$40), (\$35) and (\$39), respectively                              | (112)                           | (101)                  | (109)                   |
| Adjustment for actuarial gains incurred in current year, net of taxes of \$58, \$24 and \$12, respectively                               | 166                             | 67                     | 33                      |
| Adjustment for amortization of prior year service costs, net of taxes of (\$1), (\$1) and (\$1), respectively                            | <u>(4)</u>                      | <u>(4)</u>             | <u>(4)</u>              |
| Other comprehensive (loss) income                                                                                                        | (74,944)                        | (11,685)               | 5,992                   |
| Total comprehensive (loss) income                                                                                                        | <u><u>\$ (56,878)</u></u>       | <u><u>\$ 3,950</u></u> | <u><u>\$ 20,202</u></u> |

*The accompanying notes are an integral part of the consolidated financial statements.*

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY**  
(Dollars in thousands, except per share data)

|                                           | Shares of | Non-controlling<br>interest -<br>Preferred stock<br>of subsidiary | Common<br>stock | Retained<br>earnings | Accumulated<br>other<br>comprehensive<br>income (loss) | Total      |
|-------------------------------------------|-----------|-------------------------------------------------------------------|-----------------|----------------------|--------------------------------------------------------|------------|
| <b>Balance at January 1, 2020</b>         | 4,379,871 | \$ 95                                                             | \$ 43,799       | \$ 98,945            | \$ 1,549                                               | \$ 144,388 |
| Net income                                |           |                                                                   |                 | 14,210               |                                                        | 14,210     |
| Other comprehensive income                |           |                                                                   |                 |                      | 5,992                                                  | 5,992      |
| Repurchase under stock repurchase plan    | (20,133)  |                                                                   | (202)           | (716)                |                                                        | (918)      |
| Cash dividends declared, \$0.84 per share |           |                                                                   |                 | (3,662)              |                                                        | (3,662)    |
| Preferred dividends paid                  |           |                                                                   |                 | (16)                 |                                                        | (16)       |
| <b>Balance at December 31, 2020</b>       | 4,359,738 | \$ 95                                                             | \$ 43,597       | \$ 108,761           | \$ 7,541                                               | \$ 159,994 |
| Net income                                |           |                                                                   |                 | 15,635               |                                                        | 15,635     |
| Other comprehensive income                |           |                                                                   |                 |                      | (11,685)                                               | (11,685)   |
| Repurchase under stock repurchase plan    | (42,432)  |                                                                   | (424)           | (1,229)              |                                                        | (1,653)    |
| Cash dividends declared, \$0.84 per share |           |                                                                   |                 | (3,644)              |                                                        | (3,644)    |
| Preferred dividends paid                  |           |                                                                   |                 | (16)                 |                                                        | (16)       |
| <b>Balance at December 31, 2021</b>       | 4,317,306 | \$ 95                                                             | \$ 43,173       | \$ 119,507           | \$ (4,144)                                             | \$ 158,631 |
| Net income                                |           |                                                                   |                 | 18,066               |                                                        | 18,066     |
| Other comprehensive loss                  |           |                                                                   |                 |                      | (74,944)                                               | (74,944)   |
| Repurchase under stock repurchase plan    | (41,978)  |                                                                   | (420)           | (870)                |                                                        | (1,290)    |
| Cash dividends declared, \$0.88 per share |           |                                                                   |                 | (3,782)              |                                                        | (3,782)    |
| Preferred dividends paid                  |           |                                                                   |                 | (16)                 |                                                        | (16)       |
| <b>Balance at December 31, 2022</b>       | 4,275,328 | \$ 95                                                             | \$ 42,753       | \$ 132,905           | \$ (79,088)                                            | \$ 96,665  |

*The accompanying notes are an integral part of the consolidated financial statements.*

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(Dollars in thousands)

|                             |                                                                                  | Years ended December 31, |            |            |
|-----------------------------|----------------------------------------------------------------------------------|--------------------------|------------|------------|
|                             |                                                                                  | 2022                     | 2021       | 2020       |
| <b>OPERATING ACTIVITIES</b> |                                                                                  |                          |            |            |
|                             | Net income                                                                       | \$ 18,066                | \$ 15,635  | \$ 14,210  |
|                             | Adjustments to reconcile net income to net cash provided by operating activities |                          |            |            |
|                             | (Provision credit) provision for loan and lease losses                           | (320)                    | (150)      | 700        |
|                             | Depreciation of premises and equipment                                           | 1,786                    | 2,033      | 2,074      |
|                             | Deferred tax benefit                                                             | (27)                     | (282)      | (954)      |
|                             | Net (losses) gains on sales of securities                                        | 5                        | (621)      | (129)      |
|                             | Net change in fair value of equity securities                                    | (25)                     | (239)      | (242)      |
|                             | Net (gains) losses on sales of premises and equipment                            | (91)                     | 14         | (102)      |
|                             | Gains on mortgage loans sold                                                     | (614)                    | (1,442)    | (1,364)    |
|                             | Gain on redemption of bank-owned life insurance                                  | -                        | -          | (820)      |
|                             | Proceeds from sale of mortgage loans held-for-sale                               | 23,485                   | 55,465     | 53,226     |
|                             | Funding of mortgage loans held-for-sale                                          | (25,068)                 | (55,505)   | (55,541)   |
|                             | Amortization of investment security premiums, net of accretion of discounts      | 5,599                    | 6,404      | 3,019      |
|                             | Increase in cash surrender value of life insurance contracts                     | (475)                    | (554)      | (551)      |
|                             | Changes in:                                                                      |                          |            |            |
|                             | Other assets                                                                     | (6,647)                  | 1,058      | 637        |
|                             | Other liabilities                                                                | (835)                    | 773        | 152        |
|                             | Net cash provided by operating activities                                        | 14,839                   | 22,589     | 14,315     |
| <b>INVESTING ACTIVITIES</b> |                                                                                  |                          |            |            |
|                             | Proceeds from sales of securities                                                | 1,346                    | 186,368    | 3,690      |
|                             | Proceeds from maturities and calls of securities                                 | 99,749                   | 104,150    | 130,815    |
|                             | Purchases of available-for-sale investment securities                            | (141,739)                | (592,269)  | (393,685)  |
|                             | Gain on sale of Visa class B stock                                               | -                        | (1,811)    | -          |
|                             | Net (increase) decrease in loans                                                 | (74,785)                 | 80,808     | (27,330)   |
|                             | Proceeds from sale of premises and equipment                                     | 145                      | 454        | 154        |
|                             | Purchases of premises and equipment                                              | (1,112)                  | (664)      | (1,069)    |
|                             | Purchase of life insurance policies                                              | -                        | (784)      | (2,657)    |
|                             | Proceeds from redemption of life insurance policies                              | -                        | -          | 2,210      |
|                             | Net cash used in investing activities                                            | (116,396)                | (223,748)  | (287,872)  |
| <b>FINANCING ACTIVITIES</b> |                                                                                  |                          |            |            |
|                             | Net increase in deposits                                                         | 7,422                    | 183,032    | 387,933    |
|                             | Net decrease in securities sold under agreements to repurchase                   | -                        | (11,691)   | (51)       |
|                             | Increase (decrease) in FHLB and other borrowings                                 | 25,000                   | -          | (5,500)    |
|                             | Repurchase of common stock under stock repurchase plan                           | (1,290)                  | (1,653)    | (918)      |
|                             | Cash dividends paid on common stock                                              | (3,785)                  | (3,653)    | (3,666)    |
|                             | Cash dividends paid on preferred stock of subsidiary                             | (16)                     | (16)       | (16)       |
|                             | Net cash provided by financing activities                                        | 27,331                   | 166,019    | 377,782    |
|                             | (Decrease) increase in cash and cash equivalents                                 | (74,226)                 | (35,140)   | 104,225    |
|                             | Cash and cash equivalents at beginning of period                                 | 103,230                  | 138,370    | 34,145     |
|                             | Cash and cash equivalents at end of period                                       | \$ 29,004                | \$ 103,230 | \$ 138,370 |

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS (Continued)**  
(Dollars in thousands)

| Supplemental disclosures of cash flow information:                      | Years ended December 31, |           |            |
|-------------------------------------------------------------------------|--------------------------|-----------|------------|
|                                                                         | 2022                     | 2021      | 2020       |
| Cash paid during the period for:                                        |                          |           |            |
| Interest on deposits and borrowed funds                                 | \$ 3,360                 | \$ 2,686  | \$ 4,410   |
| Income taxes                                                            | \$ 4,176                 | \$ 3,640  | \$ 3,603   |
| Noncash investing activities:                                           |                          |           |            |
| Change in fair value of securities                                      |                          |           |            |
| available-for-sale, net of tax                                          | \$ 74,994                | \$ 11,648 | \$ (6,072) |
| Minimum pension liability adjustment, net of taxes                      | \$ (50)                  | \$ (38)   | \$ (80)    |
| Common dividends declared                                               | \$ 3,782                 | \$ 3,644  | \$ 3,662   |
| Cash paid for amounts included in the measurement of lease liabilities: |                          |           |            |
| Operating cash flows related to operating leases                        | \$ 57                    | \$ 51     | \$ 51      |
| Operating cash flows related to finance leases                          | 552                      | 505       | 552        |
| Financing cash flows related to finance leases                          | 113                      | 127       | 141        |

*The accompanying notes are an integral part of the consolidated financial statements.*

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 – GENERAL AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Accounting Policies**

The accounting principles followed and the methods of applying those principles conform with accounting principles generally accepted in the United States (“GAAP”) and to general practices in the banking industry. The significant accounting policies applicable to First Farmers and Merchants Corporation (the “Company”) are summarized as follows.

**Nature of Operations**

The Company’s stock is traded on the OTC Pink Markets under ticker “FFMH”, and the Company has verified its profile and meets the new Rule 15c2-11 under the Securities and Exchange Act of 1934. The Company is a bank holding company whose principal activity is the ownership and management of its wholly-owned subsidiary, First Farmers and Merchants Bank (the “Bank”). The Bank is primarily engaged in providing a full range of banking and financial services, including lending, investing of funds, obtaining deposits, trust and wealth management operations, and other financing activities to individual and corporate customers in the Middle Tennessee area. The Bank is subject to competition from other financial institutions. The Company and the Bank are subject to the regulation of certain federal and state agencies and undergo periodic examinations by those regulatory authorities.

As of December 31, 2022, the Company had 989 holders of record of its common stock and pursuant to Section 13 of the Exchange Act does not file financial reports with the Securities and Exchange Commission.

During May 2021, the Company recorded a gain on the sale of its Visa Class B stock (“Visa Stock”) totaling \$1.3 million, net of tax. See Note 3 – Securities for additional information. In December 2021, the Company recorded a one-time adjustment for one of its supplemental executive retirement plan (“SERP”) agreements of \$1.1 million, net of tax, in relation to the retirement of a key executive. See Note 16 – Employee Benefit Plans for additional information.

**Basis of Presentation**

The accompanying consolidated financial statements present the accounts of the Company and its wholly-owned subsidiary, the Bank. The preferred shares in Maury Tenn Properties, Inc., a subsidiary of the Bank, receive dividends, which are included in the consolidated statements of income shown as income to non-controlling interest. Intercompany accounts and transactions have been eliminated in consolidation.

Certain items in prior financial statements have been reclassified to conform to the current presentation. These reclassifications had no effect on net income or shareholders’ equity.

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 – GENERAL AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, (CONTINUED)**

**Use of Estimates in the Preparation of Financial Statements**

The preparation of financial statements in conformity with GAAP requires management of the Company and the Bank to make estimates and assumptions that affect the reported amounts of assets and liabilities. Those estimates and assumptions also affect disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near-term relate to the determination of the allowance for loan and lease losses, the fair value of financial instruments, valuation of goodwill, valuation of deferred tax assets, the liability related to post-retirement benefits, and reserves for stop loss re-insurance and claims incurred but not reported under the self-insured employee health benefits plans.

**Concentrations of Credit Risk**

The Company's banking activities include granting commercial, residential, and consumer loans to customers primarily located in Middle Tennessee and northern Alabama. The Company manages its portfolio and product mix in a manner to reduce economic risk. Concentrations of credit, as defined for regulatory purposes, are reviewed quarterly by management to ensure that internally established limits are not exceeded. As of December 31, 2022, our concentrations of commercial real estate loans were 227.4% of Tier 1 Capital plus the allowance for loan and lease losses while our construction loans were 61.4%. These percentages are within our internally established limits regarding concentrations of credit.

**Cash and Due From Banks**

Included in cash and due from banks are balances due from the Federal Reserve Bank and other banks. From time to time throughout the year, the Bank's balances due from other financial institutions exceeded Federal Deposit Insurance Corporation ("FDIC") insurance limits. The Bank had \$57,000 of federal funds sold as of December 31, 2022. Federal funds sold are essentially uncollateralized loans to other financial institutions.

**Cash Equivalents**

The Company considers all liquid investments with original maturities of three months or less to be cash equivalents. Cash equivalents include cash on hand, cash due from banks, and federal funds sold. Federal funds are sold for one-day periods.

**Securities**

Certain debt securities that management has the intent and ability to hold to maturity are classified as "held-to-maturity" and recorded at amortized cost. Securities not classified as held-to-maturity are classified as "available-for-sale" and recorded at fair value, with unrealized gains and losses excluded from earnings and reported in other comprehensive income, net of tax. Purchase premiums and discounts are amortized or accreted to interest income over the expected lives of the securities using the interest method with a constant effective yield. Callable debt securities held at a premium are amortized to the earliest call date instead of maturity. Gains and losses on the sale of securities are recorded on the trade date and are determined using the specific identification method.

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 – GENERAL AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, (CONTINUED)**

**Securities, (continued)**

A decline in the fair value of any available-for-sale or held-to-maturity security below cost that is deemed to be other-than-temporary results in a reduction in the carrying amount of the security. To determine whether impairment is other-than-temporary, management considers whether the entity expects to recover the entire amortized cost basis of the security by reviewing the present value of the future cash flows associated with the security. The shortfall of the present value of the cash flows expected to be collected in relation to the amortized cost basis is referred to as a credit loss and is deemed to be other-than-temporary impairment. If a credit loss is identified, the credit loss is recognized as a charge to earnings and a new cost basis for the security is established. If management concludes that a decline in fair value of a security is temporary and, a full recovery of principal and interest is expected and it is not more-likely-than-not that it will be required to sell the security before recovery of their amortized cost basis, then the security is not other-than-temporarily impaired and the shortfall is recorded as a component of equity.

Equity securities are accounted for at fair value with changes in fair value recognized in net income. The Company held equity securities in the amount of \$2.5 million as of December 31, 2022 and 2021.

**Loans**

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff is reported at their outstanding principal balances adjusted for unearned income, charge-offs, the allowance for loan and lease losses, any unamortized deferred fees or costs on originated loans, and unamortized premiums or discounts on purchased loans.

For loans amortized at cost, interest income is accrued based on the unpaid principal balance. Loan origination fees, net of certain direct origination costs, as well as premiums and discounts, are deferred and amortized on a level yield basis over the respective term of the loan.

The accrual of interest on retail and commercial loans is discontinued at the time the loan is 90 days past due unless the credit is well-secured and in process of collection. Past-due status is based on contractual terms of the loan. In all cases, loans are placed on nonaccrual or charged off at an earlier date if collection of principal or interest is considered doubtful.

All interest accrued but not collected for loans that are placed on nonaccrual or charged off is reversed against interest income. The interest on these loans is accounted for on the cash-basis or cost-recovery method, until qualifying for return to accrual. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current, the borrower has not missed a payment for six months, and future payments are reasonably assured.

Discounts and premiums on purchased commercial loans are amortized to income using the interest method over the remaining period to contractual maturity and adjusted for anticipated prepayments.

**Allowance for Loan and Lease Losses**

The allowance for loan and lease losses is established through provisions for loan and lease losses charged against income. Loan losses are charged against the allowance when management determines that the uncollectibility of a loan has been confirmed. Subsequent recoveries, if any, are credited to the allowance in the period received.

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 – GENERAL AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, (CONTINUED)**

**Allowance for Loan and Lease Losses, (continued)**

The adequacy of the allowance for loan and lease losses is evaluated quarterly in conjunction with loan review reports and evaluations that are discussed in meetings with loan officers, credit administration, and the Bank's Board of Directors. The Bank's past loan loss experience, known and inherent risks in the portfolio, adverse situations that may affect a borrower's ability to repay (including the timing of future payments), the estimated value of any underlying collateral, composition of the loan portfolio, current economic conditions and other relevant factors are considered in this evaluation. This process is inherently subjective as it requires material estimates that are susceptible to significant change, including the amounts and timing of future cash flows expected to be received on impaired loans. The allowance for loan and lease losses is maintained at a level believed by management to be adequate to absorb estimated losses inherent in the loan portfolio.

A loan is considered impaired when it is probable that the Bank will be unable to collect all amounts due (principal and interest) according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan-by-loan basis for commercial and commercial real estate loans by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price, or the fair value of the collateral if the loan is collateral dependent.

Groups of loans with similar risk characteristics are collectively evaluated for impairment based on the group's historical loss experience adjusted for changes in trends, conditions, and other relevant factors that affect repayment of the loans. Accordingly, the Bank does not separately identify individual consumer and residential loans for impairment measurements, unless such loans are the subject of a restructuring agreement due to financial difficulties of the borrower where economic concessions have been granted.

When any collateral dependent commercial loan is considered uncollectable, whether past due or not, a current assessment of the value of the underlying collateral is made. The loan is placed on nonaccrual and the loan is charged down to the value of the collateral less estimated cost to sell or a specific reserve equal to the difference between book value of the loan and the fair value assigned to the collateral is created until such time as the loan is foreclosed. When the foreclosed collateral has been legally assigned to the Bank, a charge off is taken, if necessary, in order that the remaining balance reflects the fair value estimated less costs to sell the collateral then transferred to other real estate owned or other repossessed assets. When any unsecured commercial loan is considered uncollectable the loan is charged off no later than at 90 days past due.

All closed-end consumer loans (excluding conventional 1-4 family residential installment and revolving loans secured by real estate) are charged off upon reaching no later than 120 days (4 monthly payments) delinquent. If a loan is considered uncollectable, it is charged off earlier than 120 days delinquent. For conventional 1-4 family residential, installment and revolving loans secured by real estate, when a loan is 90 days past due, a current assessment of the value of the real estate is made. If the balance of the loan exceeds the fair value of the property, the loan is placed on nonaccrual and foreclosure proceedings are initiated. When the foreclosed property has been legally assigned to the Bank, a charge-off is taken with the remaining balance, reflecting the fair value less estimated costs to sell, transferred to other real estate owned.

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 – GENERAL AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, (CONTINUED)**

**Loans Held-for-Sale**

Mortgage loans originated and intended for sale in the secondary market are carried at the lower of cost or fair value. Net unrealized losses, if any, are recognized through a valuation allowance by charges to non-interest income. Gains and losses on loan sales are recorded in non-interest income. The Company does not retain servicing rights on loans sold. Loans held-for-sale as of December 31, 2022 and 2021 totaled \$0 and \$2.2 million, respectively.

**Other Real Estate**

Assets acquired through, or in lieu of, loan foreclosure are held-for-sale and are initially recorded at fair value less cost to sell at the date of foreclosure, establishing a new cost basis. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of carrying amount or fair value less cost to sell. Revenue and expenses from operations and changes in the valuation allowance are included in net income or expense from foreclosed assets.

When foreclosed properties are acquired current appraisals are obtained on the properties. Additionally, periodic updated appraisals are obtained on unsold foreclosed properties. When an updated appraisal reflects a market value below the current book value, a charge is booked to current earnings to reduce the property to its new market value less expected selling costs. Our policy for determining the frequency of periodic reviews is based upon consideration of the specific properties and the known or perceived market fluctuations in a particular market. The Company did not hold any other real estate repossessed as of December 2022 and 2021.

**Premises and Equipment**

Premises, equipment, and leasehold improvements are stated at cost, less accumulated depreciation and amortization. The provision for depreciation is computed principally on an accelerated method over the estimated useful life of an asset, which ranges from 15 to 39 years for buildings, from three to seven years for equipment, and the expected lease terms for leasehold improvements. Costs of major additions and improvements are capitalized. Expenditures for maintenance and repairs are charged to operations as incurred. Gains or losses from the disposition of property are reflected in operations, and the asset accounts and related allowances for depreciation are reduced.

Right-of-use assets associated with financing leases are included in premises and equipment on the consolidated balance sheets and stated at the estimated present value of lease payments over the lease term. Disclosures about the Company's leasing activities are presented in Note 8 – Leases.

**Federal Reserve and Federal Home Loan Bank Stock**

Federal Reserve and Federal Home Loan Bank stock are required investments for institutions that are members of the Federal Reserve and Federal Home Loan Bank systems. The required investment in the common stock is based on a predetermined formula, carried at cost and evaluated for impairment. As of December 31, 2022 and 2021 Federal Reserve and Federal Home Loan Bank stock totaled \$6.1 million and \$4.1 million, respectively, and is recorded in other assets on the consolidated balance sheet.

**Bank-owned Life Insurance**

The Bank has purchased life insurance policies on certain key officers. Bank-owned life insurance is recorded at its cash surrender value, or the amount that can be realized upon immediate liquidation.

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 – GENERAL AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, (CONTINUED)**

**Goodwill**

Goodwill is evaluated annually for impairment. Quantitative and qualitative assessments are performed to determine whether the existence of events or circumstances leads to a determination that it is more-likely-than-not the fair value is less than the carrying amount, including goodwill. If, based on the evaluation, it is determined to be more-likely-than-not that the fair value is less than the carrying value, then goodwill is tested further for impairment. If the implied fair value of goodwill is lower than its carrying amount, a goodwill impairment is indicated and goodwill is written down to its implied fair value. Subsequent increases in goodwill value are not recognized in the financial statements.

**Transfers of Financial Assets**

Transfers of financial assets are accounted for as sales when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the Company—put presumptively beyond the reach of the transferor and its creditors, even in bankruptcy or other receivership, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets and (3) the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity or the ability to unilaterally cause the holder to return specific assets.

**Revenue from Contracts with Customers**

The Company records revenue from contracts with customers in accordance with Financial Accounting Standards Board (“FASB”) Accounting Standards Codification (“ASC”) Topic 606, Revenue from Contracts with Customers (“Topic 606”). Under Topic 606, we must identify the contract with a customer, identify the performance obligations in the contract, determine the transaction price, allocate the transaction price to the performance obligations in the contract, and recognize revenue when, or as we satisfy a performance obligation.

Our primary sources of revenue are derived from financial instruments, namely loans, investment securities, and other financial instruments that are not within the scope of Topic 606. We have evaluated the nature of the Company’s contracts with customers and determined that further disaggregation of revenue from contracts with customers into more granular categories beyond what is presented in the consolidated statements of income was not necessary. The Company generally fully satisfies its performance obligations on its contracts with customers as services are rendered and the transaction prices are typically fixed; charged either on a periodic basis or based on activity. Because performance obligations are satisfied as services are rendered and the transaction prices are fixed, there is little judgement involved in applying Topic 606 that significantly affects the determination of the amount and timing of revenue from contracts with customers.

**Leases**

The Company leases certain properties and equipment under both finance and operating leases. Leases are classified as operating or finance leases at the lease commencement date. Lease expense for operating leases and short-term leases is recognized on a straight-line basis over the lease term. Right-of-use assets represent our right to use an underlying asset for the lease term and lease liabilities represent our obligation to make lease payments arising from the lease. Right-of-use assets and lease liabilities are recognized at the lease commencement date based on the estimated present value of lease payments over the lease term.

The Company includes lease extension and termination options in the lease term if, after considering relevant economic factors, it is reasonably certain the Company will exercise the option. In addition, the Company has elected not to recognize leases with original lease terms of 12 months or less (short-term leases) on the Company’s balance sheet.

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 – GENERAL AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, (CONTINUED)**

The Company uses its incremental borrowing rate at lease commencement to calculate the present value of lease payments when the rate implicit in a lease is not known. The Company's incremental borrowing rate is based on the FHLB advance rate.

**Income Taxes**

The Company files consolidated income tax returns with its subsidiaries. The Company accounts for income taxes in accordance with income tax accounting guidance (ASC 740, *Income Taxes*). The income tax accounting guidance requires two components of income tax expense which are current and deferred. Current income tax expense reflects taxes to be paid or refunded for the current period by applying the provisions of the enacted tax law to the taxable income or excess of deductions over revenues. The Company determines deferred income taxes using the liability or balance sheet method. Under this method, the net deferred tax asset or liability is based on the tax effects of the differences between the book and tax bases of assets and liabilities, and enacted changes in tax rates and laws are recognized in the period in which they occur. Deferred income tax expense results from changes in deferred tax assets and liabilities between periods. Deferred tax assets are reduced by a valuation allowance if, based on the weight of evidence available, it is more-likely-than-not that some portion or all of a deferred tax asset will not be realized.

Tax positions are recognized if it is more-likely-than-not, based on the technical merits that the tax position will be realized or sustained upon examination. The term more-likely-than-not means a likelihood of more than 50%; the terms examined and upon examination also include resolution of the related appeals or litigation processes, if any. A tax position that meets the more-likely-than-not recognition threshold is initially and subsequently measured as the largest amount of tax benefit that has a greater than 50% likelihood of being realized upon settlement with a taxing authority that has full knowledge of all relevant information. The determination of whether or not a tax position has met the more-likely-than-not recognition threshold considers the facts, circumstances and information available at the reporting date and is subject to management's judgment. With a few exceptions, the Company is no longer subject to U.S. federal tax examinations and state and local tax examinations by tax authorities for years prior to 2019.

The Company recognizes interest and penalties on income taxes as a component of income tax expense. As of December 31, 2022, the Company has not accrued any interest or penalties related to uncertain tax positions.

**Securities Sold Under Agreements to Repurchase**

Securities sold under agreements to repurchase, which are classified as secured borrowings, generally mature within one to four days from the transaction date. Securities sold under agreements to repurchase are reflected at the amount of cash received in connection with the transaction.

**Fair Value Measurements**

Fair value of financial instruments are estimated using relevant market information and other assumptions. Fair value estimates involve uncertainties and matters of significant judgment regarding interest rates, credit risk, prepayments, and other factors, especially in the absence of broad markets for particular items. Changes in assumptions or in market conditions could significantly affect these estimates. See Note 12 – Fair Value Measurement.

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 – GENERAL AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, (CONTINUED)**

**Earnings Per Share**

Earnings per share represents income available to shareholders divided by the weighted average number of shares of the Company's common stock outstanding during the period. Fully diluted earnings per share is not presented as there are no common stock equivalents.

The following is a summary of the earnings per share calculation for the periods presented:

|                                                              | <b>Years ended December 31,</b>               |                |                |
|--------------------------------------------------------------|-----------------------------------------------|----------------|----------------|
|                                                              | <b>2022</b>                                   | <b>2021</b>    | <b>2020</b>    |
|                                                              | (dollars in thousands, except per share data) |                |                |
| Earnings per share calculation:                              |                                               |                |                |
| Numerator – Net income available to common shareholders      | \$ 18,050                                     | \$ 15,619      | \$ 14,194      |
| Denominator – Weighted average common shares outstanding     | 4,305,557                                     | 4,345,665      | 4,363,539      |
| Net income per common share available to common shareholders | <u>\$ 4.19</u>                                | <u>\$ 3.59</u> | <u>\$ 3.25</u> |

Upon annual evaluation in 2022, the Company reauthorized a plan to repurchase up to 200,000 shares of its common stock. As of December 31, 2022, no shares had been repurchased under the reauthorized plan and all 200,000 shares were available for repurchase in 2023.

**Other Comprehensive Income (Loss)**

Comprehensive income (loss) consists of net income and other comprehensive income (loss), net of applicable income tax expenses or benefits. Other comprehensive income (loss) includes unrealized appreciation or depreciation on available-for-sale securities and changes in the net actuarial gain or loss of the post-retirement benefit obligation.

**Segment Reporting**

Management analyzes the operations of the Company assuming one operating segment, community lending services.

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 – GENERAL AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, (CONTINUED)**

**Recent Accounting Pronouncements**

In June of 2016, the FASB issued *ASU 2016-13, Financial Instruments – Credit Losses: Measurement of Credit Losses on Financial Instruments (Topic 326)*, and has issued subsequent amendments there to, which introduces the current expected credit losses (“CECL”) methodology. Among other things, the ASU requires the measurement of all expected credit losses for financial assets, including loans and available-for-sale debt securities, held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts that affect the collectability of the reported amount. The new model will require institutions to calculate all probable and estimable losses that are expected to be incurred through the loan’s entire life. ASU 2016-13 also requires the allowance for credit losses for purchased financial assets with credit deterioration since origination to be determined in a manner similar to that of other financial assets measured at amortized cost; however, the initial allowance will be added to the purchase price rather than recorded as credit loss expense. The CECL model is applicable to the measurement of credit losses on financial assets measured at amortized cost, including loan receivables and held-to-maturity debt securities. It also applies to off-balance sheet credit exposures not accounted for as insurance such as loan commitments, standby letters of credit, financial guarantees, and other similar instruments. The disclosure of credit quality indicators related to the amortized cost of financing receivables will be further disaggregated by year of origination or vintage. Institutions are to apply the changes through a cumulative-effect adjustment to their retained earnings as of the beginning of the first reporting period in which the standard is effective. In November of 2019, FASB issued *ASU 2019-10, Financial Instruments – Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842): Effective Dates*. The guidance extended the adoption date of ASU 2016-13 for the Company from fiscal years beginning after December 15, 2020 to fiscal years beginning after December 15, 2022. The Company has a working CECL model that has been validated by an independent third party and received a satisfactory rating. Management is prepared to adopt the CECL methodology using a cumulative-effect adjustment to retained earnings as of the beginning of fiscal year 2023.

In May of 2019, FASB issued *ASU 2019-05, Financial Instruments – Credit Losses (“Topic 326”)*. The amendments in this Update provide entities that have certain instruments within the scope of *Subtopic 326-20, Financial Instruments – Credit Losses – Measured at Amortized Cost*, with an option to irrevocably elect the fair value option in *Subtopic 825-10, Financial Instruments – Overall*, applied on an instrument-by-instruments basis for eligible instruments, upon adoption of Topic 326. The fair value option election does not apply to held-to-maturity debt securities. The amendments in this update are the same as in ASU 2016-13, or for fiscal years beginning after December 15, 2022. The guidance is not expected to have a significant impact on the Company’s financial position, results of operations, or disclosures.

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 – GENERAL AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, (CONTINUED)**

**Recent Accounting Pronouncements**

In March of 2020, the FASB issued *ASU 2020-04, Reference Rate Reform (Topic 848): Facilitation of the Effects of Reference Rate Reform on Financial Reporting*. The update provides temporary optional guidance to ease the potential burden in accounting for reference rate reform. The guidance provides optional expedients and exceptions for applying generally accepted accounting principles to contract modifications and hedging relationships, subject to meeting certain criteria, that reference LIBOR or other reference rates expected to be discontinued. The guidance is expected to help stakeholders during the global market-wide reference rate transition period. ASU 2020-04 was effective upon issuance and generally can be applied through December 31, 2022. In January of 2021, the FASB issued ASU 2021-01 which clarified that all derivative instruments affected by the changes to interest rates used for discounting, margining or contract price alignment, regardless of whether they reference LIBOR or another rate expected to be discontinued as a result of reference rate reform, an entity may apply certain practical expedients in Topic 848. The Company is in the process of modifying its loans that use LIBOR assisting with the selection of a new index rate. The guidance is not expected to have a significant impact on the Company's financial position, results of operations, or disclosures.

In July of 2021, the FASB issued *ASU 2021-05, Leases (Topic 82): Lessors – Certain Leases with Variable Lease Payments*. The update amends the lease classification requirements for lessors to align them with practice under ASC Topic 840. Lessors should classify and account for a lease with variable lease payments that do not depend on a reference index or a rate as an operating lease if both of the following criteria are met: (1) the lease would have been classified as a sales-type lease or a direct financing lease in accordance with the classification criteria in ASC paragraphs 842-10-25-2 through 25-3 and (2) the lessor would have otherwise recognized a day-one loss. When a lease is classified as operating, the lessor does not recognize a net investment in the lease, does not derecognize the underlying asset, and therefore, does not recognize a selling profit or loss. An entity within the scope of ASC paragraph 842-10-65-1(b) that has adopted ASU No. 2016-02 as of July 19, 2021, should apply ASU No. 2021-05 for fiscal years beginning after December 15, 2021, and interim periods within fiscal years beginning after December 15, 2022. Our Company adopted ASU No. 2016-02 on January 1, 2019. The update in ASU 2021-05 that amends ASC Topic 840 is not expected to have a significant impact on the Company's financial position, results of operations, or disclosures.

In March of 2022, the FASB issued *ASU 2022-02, Financial Instruments – Credit Losses (Topic 326): Troubled Debt Restructurings and Vintage Disclosures*. The update eliminates the recognition and measurement guidance for troubled debt restructurings ("TDRs") by creditors in ASC 310-40. This update also enhances disclosure requirements for certain loan restructurings by creditors when a borrower is experiencing financial difficulty. Specifically, rather than applying the recognition and measurement guidance for TDRs, an entity will apply the loan refinancing and restructuring guidance to determine whether a modification or other form of restructuring results in a new loan or a continuation of an existing loan. Additionally, the amendments in this ASU require a public business entity to disclose current-period gross write-offs by year of origination for financing receivables and net investments in leases in the existing vintage disclosures. The amendments of this update are effective for the entities that have adopted the amendments in Update 2016-13 for fiscal years beginning after December 15, 2022. The guidance is not expected to have a significant impact on the Company's financial position, results of operations, or disclosures.

In June of 2022, the FASB issued *ASU 2022-03, Fair Value Measurement (Topic 820): Fair Value Measurement of Equity Securities Subject to Contractual Sale Restrictions*. The amendments in this update clarify that a contractual restriction on the sale of an equity security is not considered part of the unit of account of the equity security and, therefore is not considered in measuring fair value. The amendments also clarify that an entity cannot, as a separate unit of account, recognize and measure a contractual sale restriction. The amendments also require certain disclosures for equity securities subject to contractual sale restrictions. For public business entities, the amendments in this Update are effective for fiscal years beginning after December 15, 2023. The guidance is not expected to have a significant impact on the Company's financial position, results of operations, or disclosures.

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 2 – ACCUMULATED OTHER COMPREHENSIVE INCOME (“AOCI”)**

The components of accumulated other comprehensive income (loss), included in shareholder’s equity, are as follows:

|                                                                              | <b>Years ended December 31,</b> |                   |                 |
|------------------------------------------------------------------------------|---------------------------------|-------------------|-----------------|
|                                                                              | <b>2022</b>                     | <b>2021</b>       | <b>2020</b>     |
|                                                                              | (dollars in thousands)          |                   |                 |
| Net unrealized (losses) gains                                                |                                 |                   |                 |
| on available-for-sale securities                                             | \$ (108,345)                    | \$ (6,866)        | \$ 8,896        |
| Net actuarial gain on unfunded portion of post-retirement benefit obligation | 1,325                           | 1,258             | 1,308           |
| Total                                                                        | (107,020)                       | (5,608)           | 10,206          |
| Tax benefit (provision)                                                      | 27,932                          | 1,464             | (2,663)         |
| Accumulated other comprehensive (loss) income                                | <u>\$ (79,088)</u>              | <u>\$ (4,144)</u> | <u>\$ 7,541</u> |

Amounts reclassified from AOCI and the affected line items in the statements of income during the periods presented are as follows:

|                                               | Amounts reclassified from AOCI |               |               |                                   |
|-----------------------------------------------|--------------------------------|---------------|---------------|-----------------------------------|
|                                               | Years ended December 31,       |               |               | Affected line item in the         |
|                                               | 2022                           | 2021          | 2020          | Statements of income              |
| Realized (losses) gains on securities         | \$ (5)                         | \$ 621        | \$ 129        | (Loss) gain on sale of securities |
| Tax benefit (provision)                       | 1                              | (162)         | (34)          | Provision for income taxes        |
| Net realized (losses) gains on securities     | <u>\$ (4)</u>                  | <u>\$ 459</u> | <u>\$ 95</u>  | Net reclassified amount           |
| Amortization of defined benefit pension items | \$ 152                         | \$ 136        | \$ 148        | Other non-interest expense        |
| Tax provision                                 | <u>(40)</u>                    | <u>(35)</u>   | <u>(39)</u>   | Provision for income taxes        |
| Net amortization of defined benefit pension   | <u>\$ 112</u>                  | <u>\$ 101</u> | <u>\$ 109</u> | Net reclassified amount           |
| Amortization of prior year service costs      | \$ 5                           | \$ 5          | \$ 5          | Other non-interest expense        |
| Tax provision                                 | <u>(1)</u>                     | <u>(1)</u>    | <u>(1)</u>    | Provision for income taxes        |
| Net amortization of prior year service costs  | <u>4</u>                       | <u>4</u>      | <u>4</u>      | Net reclassified amount           |
| Total reclassifications out of AOCI           | \$ 112                         | \$ 564        | \$ 208        |                                   |

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 3 – SECURITIES**

The amortized cost and fair value of securities available-for-sale and held-to-maturity at December 31, 2022 and 2021 are summarized as follows:

|                                                             | <u>Amortized<br/>cost</u> | <u>Gross<br/>unrealized<br/>gains</u> | <u>Gross<br/>unrealized<br/>losses</u> | <u>Fair<br/>value</u> |
|-------------------------------------------------------------|---------------------------|---------------------------------------|----------------------------------------|-----------------------|
| <b>December 31, 2022</b>                                    | (dollars in thousands)    |                                       |                                        |                       |
| Available-for-sale securities:                              |                           |                                       |                                        |                       |
| U.S. treasuries securities                                  | \$ 73,017                 | \$ -                                  | \$ (3,332)                             | \$ 69,685             |
| U.S. government sponsored agencies                          | 262,152                   | -                                     | (33,131)                               | 229,021               |
| U.S. government sponsored agency mortgage-backed securities | 439,175                   | -                                     | (56,115)                               | 383,060               |
| States and political subdivisions                           | 127,870                   | 12                                    | (14,683)                               | 113,199               |
| Corporate bonds                                             | 16,722                    | 1                                     | (1,097)                                | 15,626                |
| Total                                                       | <u>\$ 918,936</u>         | <u>\$ 13</u>                          | <u>\$ (108,358)</u>                    | <u>\$ 810,591</u>     |
| Held-to-maturity securities:                                |                           |                                       |                                        |                       |
| States and political subdivisions                           | <u>\$ 15,087</u>          | <u>\$ -</u>                           | <u>\$ (925)</u>                        | <u>\$ 14,162</u>      |
| <b>December 31, 2021</b>                                    |                           |                                       |                                        |                       |
| Available-for-sale securities:                              |                           |                                       |                                        |                       |
| U.S. treasuries securities                                  | \$ 18,051                 | \$ -                                  | \$ (198)                               | \$ 17,853             |
| U.S. government sponsored agencies                          | 266,709                   | 480                                   | (5,787)                                | 261,402               |
| U.S. government sponsored agency mortgage-backed securities | 448,528                   | 1,929                                 | (3,737)                                | 446,720               |
| States and political subdivisions                           | 133,435                   | 1,788                                 | (1,175)                                | 134,048               |
| Corporate bonds                                             | 17,130                    | 10                                    | (176)                                  | 16,964                |
| Total                                                       | <u>\$ 883,853</u>         | <u>\$ 4,207</u>                       | <u>\$ (11,073)</u>                     | <u>\$ 876,987</u>     |
| Held-to-maturity securities:                                |                           |                                       |                                        |                       |
| States and political subdivisions                           | <u>\$ 15,128</u>          | <u>\$ 804</u>                         | <u>\$ -</u>                            | <u>\$ 15,932</u>      |

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 3 – SECURITIES, (CONTINUED)**

The following table shows the Company's investments' gross unrealized losses and fair value of the Company's investments with unrealized losses that were not deemed to be other-than-temporarily impaired, aggregated by investment class and length of time that individual securities had been in a continuous unrealized loss position at December 31, 2022 and 2021:

|                                                             | <u>Less than 12 months</u> |                          | <u>12 months or more</u> |                          | <u>Total</u>      |                          |
|-------------------------------------------------------------|----------------------------|--------------------------|--------------------------|--------------------------|-------------------|--------------------------|
|                                                             | <u>Fair value</u>          | <u>Unrealized losses</u> | <u>Fair value</u>        | <u>Unrealized losses</u> | <u>Fair value</u> | <u>Unrealized losses</u> |
|                                                             | (dollars in thousands)     |                          |                          |                          |                   |                          |
| <b>December 31, 2022</b>                                    |                            |                          |                          |                          |                   |                          |
| Available-for-sale securities:                              |                            |                          |                          |                          |                   |                          |
| U.S. treasuries securities                                  | \$ 53,200                  | \$ (1,782)               | \$ 16,485                | \$ (1,550)               | \$ 69,685         | \$ (3,332)               |
| U.S. government sponsored agencies                          | 22,270                     | (3,626)                  | 206,751                  | (29,505)                 | 229,021           | (33,131)                 |
| U.S. government sponsored agency mortgage backed securities | 131,532                    | (14,697)                 | 251,528                  | (41,418)                 | 383,060           | (56,115)                 |
| States and political subdivisions                           | 56,952                     | (6,121)                  | 51,994                   | (8,562)                  | 108,946           | (14,683)                 |
| Corporate bonds                                             | 2,967                      | (46)                     | 12,408                   | (1,051)                  | 15,375            | (1,097)                  |
| Total                                                       | <u>\$ 266,921</u>          | <u>\$ (26,272)</u>       | <u>\$ 539,166</u>        | <u>\$ (82,086)</u>       | <u>\$ 806,087</u> | <u>\$ (108,358)</u>      |
| Held-to-maturity securities:                                |                            |                          |                          |                          |                   |                          |
| States and political subdivisions                           | <u>\$ 14,162</u>           | <u>\$ (925)</u>          | <u>\$ -</u>              | <u>\$ -</u>              | <u>\$ 14,162</u>  | <u>\$ (925)</u>          |
| <b>December 31, 2021</b>                                    |                            |                          |                          |                          |                   |                          |
| Available-for-sale securities:                              |                            |                          |                          |                          |                   |                          |
| U.S. treasuries securities                                  | \$ 17,853                  | \$ (198)                 | \$ -                     | \$ -                     | \$ 17,853         | \$ (198)                 |
| U.S. government sponsored agencies                          | 173,548                    | (3,464)                  | 58,195                   | (2,323)                  | 231,743           | (5,787)                  |
| U.S. government sponsored agency mortgage backed securities | 334,800                    | (3,737)                  | -                        | -                        | 334,800           | (3,737)                  |
| States and political subdivisions                           | 54,364                     | (973)                    | 6,771                    | (202)                    | 61,135            | (1,175)                  |
| Corporate bonds                                             | 13,268                     | (161)                    | 671                      | (15)                     | 13,939            | (176)                    |
| Total                                                       | <u>\$ 593,833</u>          | <u>\$ (8,533)</u>        | <u>\$ 65,637</u>         | <u>\$ (2,540)</u>        | <u>\$ 659,470</u> | <u>\$ (11,073)</u>       |
| Held-to-maturity securities:                                |                            |                          |                          |                          |                   |                          |
| States and political subdivisions                           | \$ -                       | \$ -                     | \$ -                     | \$ -                     | \$ -              | \$ -                     |

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 3 – SECURITIES, (CONTINUED)**

As shown in the tables above, as of December 31, 2022, the Company had \$108 million in unrealized losses on \$918.9 million of securities. The level of unrealized loss positions impacted all types of securities owned by the Company with the largest balance of unrealized losses recorded in U.S. government sponsored agency mortgage-backed securities. The mortgage-backed securities owned by the Company are issued by government agencies or government-sponsored enterprises which have an implied guarantee by the U.S. government. The unrealized losses associated with these investment securities are driven by changes in interest rates and the unrealized loss is recorded as a component of equity. These securities will continue to be monitored as a part of our ongoing impairment analysis but are expected to perform even if the rating agencies reduce the credit rating of the bond issuers. Management evaluates the financial performance of the issuers on a quarterly basis to determine if it is probable that the issuers can make all contractual principal and interest payments. If a shortfall in future cash flows is identified, a credit loss will be deemed to have occurred and will be recognized as a charge to earnings and a new cost basis for the security will be established. No other-than-temporary impairment was recorded during the years ended 2022 and 2021.

The amortized cost and fair value of available-for-sale and held-to-maturity securities as of December 31, 2022 and 2021, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties. Securities not due at a single maturity date are shown separately.

|                            | <b>Available-for-sale</b> |                   | <b>Held-to-maturity</b> |                   |
|----------------------------|---------------------------|-------------------|-------------------------|-------------------|
|                            | <b>Amortized Cost</b>     | <b>Fair value</b> | <b>Amortized cost</b>   | <b>Fair value</b> |
| <b>December 31, 2022</b>   |                           |                   |                         |                   |
|                            | (dollars in thousands)    |                   |                         |                   |
| Within one year            | \$ 70,114                 | \$ 68,692         | \$ -                    | \$ -              |
| One to five years          | 198,201                   | 182,043           | 1,320                   | 1,280             |
| Five to ten years          | 155,087                   | 129,994           | 5,168                   | 4,903             |
| After ten years            | 56,358                    | 46,802            | 8,599                   | 7,979             |
| Mortgage-backed securities | 439,176                   | 383,060           | -                       | -                 |
| Total                      | <u>\$ 918,936</u>         | <u>\$ 810,591</u> | <u>\$ 15,087</u>        | <u>\$ 14,162</u>  |
|                            |                           |                   |                         |                   |
|                            | <b>Available-for-sale</b> |                   | <b>Held-to-maturity</b> |                   |
|                            | <b>Amortized cost</b>     | <b>Fair value</b> | <b>Amortized cost</b>   | <b>Fair Value</b> |
| <b>December 31, 2021</b>   |                           |                   |                         |                   |
|                            | (dollars in thousands)    |                   |                         |                   |
| Within one year            | \$ 8,241                  | \$ 8,271          | \$ -                    | \$ -              |
| One to five years          | 189,304                   | 186,875           | 321                     | 332               |
| Five to ten years          | 174,917                   | 171,801           | 2,993                   | 3,104             |
| After ten years            | 62,865                    | 63,320            | 11,814                  | 12,496            |
| Mortgage-backed securities | 448,526                   | 446,720           | -                       | -                 |
| Total                      | <u>\$ 883,853</u>         | <u>\$ 876,987</u> | <u>\$ 15,128</u>        | <u>\$ 15,932</u>  |

The carrying value of securities pledged as collateral to secure public deposits and for other purposes was \$431.2 million and \$350.5 million at December 31, 2022 and 2021, respectively. There were no securities sold under repurchase agreements as of December 31, 2022 and 2021.

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 3 – SECURITIES, (CONTINUED)**

There were no securities sold under repurchase agreements as of December 31, 2022 and 2021.

|                                                    | <b>Years ended December 31,</b> |               |               |
|----------------------------------------------------|---------------------------------|---------------|---------------|
|                                                    | <b>2022</b>                     | <b>2021</b>   | <b>2020</b>   |
|                                                    | (dollars in thousands)          |               |               |
| Gross gains recognized on sales of securities      | \$ -                            | \$ 922        | \$ 129        |
| Gross losses recognized on sales of securities     | (5)                             | (301)         | -             |
| Net realized (losses) gains on sales of securities | <u>\$ (5)</u>                   | <u>\$ 621</u> | <u>\$ 129</u> |

The Corporation held equity securities in the amount of \$2.5 million at December 31, 2022 and 2021. There have been no sales of equity securities during 2022, 2021, and 2020.

On March 18, 2008, the company participated in a Visa IPO as a financial institution customer and was granted shares of Visa Stock at no cost. Because of certain restrictions on the Visa Stock, the Company elected to account for this investment at cost minus impairment. On May 20, 2021, the Company sold all of its holdings and recorded a gain on the sale of its Visa Stock of \$1.8 million.

During 2021, the company transferred two held-to-maturity securities with a net carrying value of \$664,000 to available-for-sale classification. Under ASC 320-10-25-6, the Company concluded that there was sufficient evidence of a significant deterioration in the issuer's credit worthiness. Immediately following the reclassification, the Company sold the securities recognizing a realized gain of \$46,000 as of December 31, 2021.

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 4 – LOANS**

The following table presents the Bank’s loans by category as of the periods presented:

|                                         | <b>December 31,<br/>2022</b> | <b>December 31,<br/>2021</b> |
|-----------------------------------------|------------------------------|------------------------------|
|                                         | (dollars in thousands)       |                              |
| <b><u>Commercial</u></b>                |                              |                              |
| Commercial and industrial               | \$ 83,717                    | \$ 86,240                    |
| Non-farm, non-residential real estate   | 323,006                      | 262,854                      |
| Construction and development            | 90,120                       | 105,580                      |
| Commercial loans secured by real estate | 102,645                      | 74,963                       |
| Other commercial loans                  | 54,269                       | 42,292                       |
| Total commercial loans                  | <u>653,757</u>               | <u>571,929</u>               |
| <b><u>Retail</u></b>                    |                              |                              |
| Consumer loans                          | 6,502                        | 6,553                        |
| Single family residential               | 296,838                      | 296,453                      |
| Other retail loans                      | 9,070                        | 11,956                       |
| Total retail loans                      | <u>312,410</u>               | <u>314,962</u>               |
| Total loans, net of deferred fees       | \$ 966,167                   | \$ 886,891                   |
| Less:                                   |                              |                              |
| Allowance for loan and lease losses     | (9,382)                      | (9,605)                      |
| Total net loans                         | <u>\$ 956,785</u>            | <u>\$ 877,286</u>            |

The amount of net capitalized fees, calculated in accordance with accounting guidance included in the above loan totals were \$651,000 and \$1.3 million as of December 31, 2022 and 2021, respectively.

The Company prioritized assisting its customers with the Coronavirus Aid, Relief, and Economic Security Act using the Small Business Administration Paycheck Protection Program (“SBA PPP”) loans to be made by banks to employers with less than 500 employees if they continue to employ their existing workers. Since the inception of the program, the Company funded over 1,500 loans for a total amount of \$115.8 million under the SBA PPP and processed \$115.2 million in loan redemptions for customers. As of December 31, 2022, the Company held \$517,000 of SBA PPP loans. SBA PPP loan fees recorded as an adjustment to loan yield were \$6,800 and \$3.6 million as of December 31, 2022 and 2021, respectively. These SBA PPP loans are included within the commercial and industrial and other commercial loan categories in the table above.

*Loan Origination/Risk Management.* The Company has certain lending policies and procedures in place that are designed to maximize loan income within an acceptable level of risk. Management reviews and approves these policies and procedures on a regular basis. A reporting system supplements the review process by providing management with frequent reports related to loan production, loan quality, concentrations of credit, loan delinquencies, non-performing and potential problem loans. Diversification in the loan portfolio is a means of managing risk associated with fluctuations in economic conditions.

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 4 – LOANS, (CONTINUED)**

Commercial and industrial loans are underwritten after evaluating and understanding the borrower's ability to operate profitably and prudently expand its business. Underwriting standards are designed to promote relationship banking rather than transactional banking. Once it is determined that the borrower's management possesses sound ethics and solid business acumen, the Company's management examines current and projected cash flows to determine the ability of the borrower to repay their obligations as agreed. Commercial and industrial loans are primarily made based on the identified cash flows of the borrower and secondarily on the underlying collateral provided by the borrower. The cash flows of borrowers, however, may not be as expected and the collateral securing these loans may fluctuate in value. Most commercial and industrial loans are secured by the assets being financed or other business assets such as accounts receivable or inventory and may incorporate a personal guarantee; however, some short-term loans may be made on an unsecured basis. In the case of loans secured by accounts receivable, the availability of funds for the repayment of these loans may be substantially dependent on the ability of the borrower to collect amounts due from its customers.

Commercial real estate loans are subject to underwriting standards and processes similar to commercial and industrial loans, in addition to those of real estate loans. These loans are viewed primarily as loans secured by real estate. Commercial real estate lending typically involves higher loan principal amounts and the repayment of these loans is largely dependent on the successful operation of the property securing the loan or the business conducted on the property securing the loan. Commercial real estate loans may be more adversely affected by conditions in the real estate markets or in the general economy. Management monitors and evaluates commercial real estate loans based on collateral, geography, and risk grade criteria. As a general rule, the Company avoids financing single-purpose projects unless other underwriting factors are present to help mitigate the risk. The Company also utilizes third-party experts to provide insight and guidance about economic conditions and trends affecting market areas it serves. In addition, management tracks the level of owner-occupied commercial real estate loans versus non-owner occupied loans.

At December 31, 2022, 24.6% of the outstanding principal balance of the Company's commercial real estate loans was secured by owner-occupied properties, compared to 33.0% at December 31, 2021. With respect to loans to developers and builders that are secured by non-owner occupied properties that the Company may originate from time to time, the Company generally requires the borrower to have had an existing relationship with the Company and have a proven record of success. Construction loans are underwritten utilizing feasibility studies, independent appraisal reviews, sensitivity analysis of absorption, and lease rates and financial analysis of the developers and property owners. Construction loans are generally based upon estimates of costs and value associated with the complete project. Construction loans often involve the disbursement of substantial funds with repayment substantially dependent on the success of the ultimate project. Sources of repayment for these types of loans may be pre-committed permanent loans from approved long-term lenders, sales of developed property, or an interim loan commitment from the company until permanent financing is obtained. These loans are closely monitored by on-site inspections and are considered to have higher risks than other real estate loans due to their ultimate repayment being sensitive to interest rate changes, governmental regulation of real property, general economic conditions, and the availability of long-term financing.

The Company originates residential and consumer loans utilizing a computer-based credit scoring analysis to supplement the underwriting process. To monitor and manage consumer loan risk, policies and procedures are developed and modified, as needed, jointly by line and staff personnel. This activity, coupled with relatively small loan amounts that are spread across many individual borrowers, minimizes risk. Additionally, trend and outlook reports are reviewed by management on a regular basis. Underwriting standards for home equity loans are heavily influenced by statutory requirements, which include, but are not limited to, a maximum loan-to-value percentage of 80%, collection remedies, the number of such loans a borrower can have at one time and documentation requirements.

The Company engages a third party vendor to perform loan reviews. The Company reviews and validates the credit risk program on an annual basis. Results of these reviews are presented to management and the Company's Audit Committee. The loan review process complements and reinforces the risk identification and assessment decisions made by lenders and credit personnel, as well as the Company's policies and procedures.

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 4 – LOANS, (CONTINUED)**

The goal of the Bank is to diversify loans to avoid a concentration of credit in a specific industry, person, entity, product, service, or any area vulnerable to a tax law change or an economic event. A concentration of credit occurs when obligations, direct or indirect, of the same or affiliated interests represent 25% or more of the Bank's capital structure. Commercial real estate rental and leasing represented the highest concentration at 228% of tier 1 capital. The Board of Directors recognizes that the Bank's geographic trade area imposes some limitations regarding loan diversification if the Bank is to perform the function for which it has been chartered. Specifically, lending to qualified borrowers within the Bank's trade area will naturally cause concentrations of real estate loans in the primary communities served by the Bank and loans to employees of major employers in the area.

The following table provides details regarding the aging of the Bank's loan portfolio:

| <b>December 31, 2022</b>                | <b>30-59<br/>days<br/>past due</b> | <b>60-89<br/>days<br/>past due</b> | <b>90 days<br/>and greater<br/>past due</b> | <b>Total<br/>past<br/>due</b> | <b>Current</b>    | <b>Total<br/>loans</b> |
|-----------------------------------------|------------------------------------|------------------------------------|---------------------------------------------|-------------------------------|-------------------|------------------------|
| (dollars in thousands)                  |                                    |                                    |                                             |                               |                   |                        |
| <b>Commercial</b>                       |                                    |                                    |                                             |                               |                   |                        |
| Commercial and industrial               | \$ -                               | \$ -                               | \$ -                                        | \$ -                          | \$ 83,717         | \$ 83,717              |
| Non-farm, non-residential real estate   | -                                  | -                                  | -                                           | -                             | 323,006           | 323,006                |
| Construction and development            | 360                                | -                                  | -                                           | 360                           | 89,760            | 90,120                 |
| Commercial loans secured by real estate | -                                  | -                                  | -                                           | -                             | 102,645           | 102,645                |
| Other commercial loans                  | 525                                | -                                  | -                                           | 525                           | 53,744            | 54,269                 |
| Total commercial loans                  | 885                                | -                                  | -                                           | 885                           | 652,872           | 653,757                |
| <b>Retail</b>                           |                                    |                                    |                                             |                               |                   |                        |
| Consumer                                | 23                                 | 4                                  | 11                                          | 38                            | 6,464             | 6,502                  |
| Single family residential               | 1,368                              | 247                                | 197                                         | 1,812                         | 295,026           | 296,838                |
| Other retail loans                      | 1                                  | -                                  | -                                           | 1                             | 9,069             | 9,070                  |
| Total retail loans                      | 1,392                              | 251                                | 208                                         | 1,851                         | 310,559           | 312,410                |
| <b>Total</b>                            | <b>\$ 2,277</b>                    | <b>\$ 251</b>                      | <b>\$ 208</b>                               | <b>\$ 2,736</b>               | <b>\$ 963,431</b> | <b>\$ 966,167</b>      |

  

| <b>December 31, 2021</b>                | <b>30-59<br/>days<br/>past due</b> | <b>60-89<br/>days<br/>past due</b> | <b>90 days<br/>and greater<br/>past due</b> | <b>Total<br/>past<br/>due</b> | <b>Current</b>    | <b>Total<br/>loans</b> |
|-----------------------------------------|------------------------------------|------------------------------------|---------------------------------------------|-------------------------------|-------------------|------------------------|
| (dollars in thousands)                  |                                    |                                    |                                             |                               |                   |                        |
| <b>Commercial</b>                       |                                    |                                    |                                             |                               |                   |                        |
| Commercial and industrial               | \$ 15                              | \$ -                               | \$ 12                                       | \$ 27                         | \$ 86,213         | \$ 86,240              |
| Non-farm, non-residential real estate   | -                                  | -                                  | -                                           | -                             | 262,854           | 262,854                |
| Construction and development            | -                                  | -                                  | -                                           | -                             | 105,580           | 105,580                |
| Commercial loans secured by real estate | -                                  | -                                  | -                                           | -                             | 74,963            | 74,963                 |
| Other commercial loans                  | -                                  | -                                  | -                                           | -                             | 42,292            | 42,292                 |
| Total commercial loans                  | 15                                 | -                                  | 12                                          | 27                            | 571,902           | 571,929                |
| <b>Retail</b>                           |                                    |                                    |                                             |                               |                   |                        |
| Consumer                                | 9                                  | -                                  | 4                                           | 13                            | 6,540             | 6,553                  |
| Single family residential               | 459                                | 390                                | 104                                         | 953                           | 295,500           | 296,453                |
| Other retail loans                      | 34                                 | -                                  | 2                                           | 36                            | 11,920            | 11,956                 |
| Total retail loans                      | 502                                | 390                                | 110                                         | 1,002                         | 313,960           | 314,962                |
| <b>Total</b>                            | <b>\$ 517</b>                      | <b>\$ 390</b>                      | <b>\$ 122</b>                               | <b>\$ 1,029</b>               | <b>\$ 885,860</b> | <b>\$ 886,891</b>      |

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 4 – LOANS, (CONTINUED)**

A loan is considered impaired, in accordance with the impairment accounting guidance, when based on current information and events, it is probable the Company will be unable to collect all amounts due from the borrower in accordance with the contractual terms of the loan. Impaired loans include non-performing loans, but also include loans modified in troubled debt restructurings. The Company had no loans that were 90 days or more past due that were not included in nonaccrual loans as of December 31, 2022 and 2021.

The following table summarizes the impaired loans by loan type:

|                                       | Unpaid<br>contractual<br>principal<br>balance | Recorded<br>investment<br>with no<br>allowance | Recorded<br>investment<br>with<br>allowance | Total<br>recorded<br>investment | Related<br>allowance | Average<br>recorded<br>investment<br>year to date | Interest<br>received | Interest<br>recognized |
|---------------------------------------|-----------------------------------------------|------------------------------------------------|---------------------------------------------|---------------------------------|----------------------|---------------------------------------------------|----------------------|------------------------|
| <b>December 31, 2022</b>              |                                               |                                                |                                             |                                 |                      |                                                   |                      |                        |
| (dollars in thousands)                |                                               |                                                |                                             |                                 |                      |                                                   |                      |                        |
| <b>Commercial:</b>                    |                                               |                                                |                                             |                                 |                      |                                                   |                      |                        |
| Commercial and industrial             | \$ -                                          | \$ -                                           | \$ -                                        | \$ -                            | \$ -                 | \$ -                                              | \$ -                 | \$ -                   |
| Non-farm, non-residential real estate | 73                                            | 73                                             | -                                           | 73                              | -                    | 74                                                | 7                    | 7                      |
| Commercial total                      | 73                                            | 73                                             | -                                           | 73                              | -                    | 74                                                | 7                    | 7                      |
| <b>Retail:</b>                        |                                               |                                                |                                             |                                 |                      |                                                   |                      |                        |
| Consumer loans                        | 11                                            | -                                              | 11                                          | 11                              | -                    | 13                                                | 1                    | 1                      |
| Single family residential             | 1,030                                         | -                                              | 910                                         | 910                             | 1                    | 953                                               | 38                   | 41                     |
| Other retail                          | 79                                            | 74                                             | -                                           | 74                              | -                    | 81                                                | 5                    | 5                      |
| Retail total                          | 1,120                                         | 74                                             | 921                                         | 995                             | 1                    | 1,047                                             | 44                   | 47                     |
| <b>Total</b>                          | <u>\$ 1,193</u>                               | <u>\$ 147</u>                                  | <u>\$ 921</u>                               | <u>\$ 1,068</u>                 | <u>\$ 1</u>          | <u>\$ 1,121</u>                                   | <u>\$ 51</u>         | <u>\$ 54</u>           |
|                                       |                                               |                                                |                                             |                                 |                      |                                                   |                      |                        |
|                                       | Unpaid<br>contractual<br>principal<br>balance | Recorded<br>investment<br>with no<br>allowance | Recorded<br>investment<br>with<br>allowance | Total<br>recorded<br>investment | Related<br>allowance | Average<br>recorded<br>investment<br>year to date | Interest<br>received | Interest<br>recognized |
| <b>December 31, 2021</b>              |                                               |                                                |                                             |                                 |                      |                                                   |                      |                        |
| (dollars in thousands)                |                                               |                                                |                                             |                                 |                      |                                                   |                      |                        |
| <b>Commercial:</b>                    |                                               |                                                |                                             |                                 |                      |                                                   |                      |                        |
| Commercial and industrial             | \$ 55                                         | \$ -                                           | \$ 18                                       | \$ 18                           | \$ -                 | \$ 24                                             | \$ 1                 | \$ 4                   |
| Non-farm, non-residential real estate | 169                                           | 86                                             | -                                           | 86                              | -                    | 191                                               | 29                   | 15                     |
| Commercial total                      | 224                                           | 86                                             | 18                                          | 104                             | -                    | 215                                               | 30                   | 19                     |
| <b>Retail:</b>                        |                                               |                                                |                                             |                                 |                      |                                                   |                      |                        |
| Consumer loans                        | 5                                             | -                                              | 2                                           | 2                               | -                    | 6                                                 | 1                    | 1                      |
| Single family residential             | 1,756                                         | 325                                            | 1,157                                       | 1,482                           | 1                    | 1,486                                             | 60                   | 61                     |
| Other retail                          | 4                                             | -                                              | 2                                           | 2                               | -                    | 5                                                 | -                    | -                      |
| Retail total                          | 1,765                                         | 325                                            | 1,161                                       | 1,486                           | 1                    | 1,497                                             | 61                   | 62                     |
| <b>Total</b>                          | <u>\$ 1,989</u>                               | <u>\$ 411</u>                                  | <u>\$ 1,179</u>                             | <u>\$ 1,590</u>                 | <u>\$ 1</u>          | <u>\$ 1,712</u>                                   | <u>\$ 91</u>         | <u>\$ 81</u>           |

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 4 – LOANS, (CONTINUED)**

Non-accrual loans, segregated by class of loans, were as follows:

|                                       | <u>December 31, 2022</u> | <u>December 31, 2021</u> |
|---------------------------------------|--------------------------|--------------------------|
|                                       | (dollars in thousands)   |                          |
| <b><u>Commercial</u></b>              |                          |                          |
| Commercial and industrial             | \$ -                     | \$ 18                    |
| Non-farm, non-residential real estate | -                        | 12                       |
| Total commercial loans                | -                        | 30                       |
| <b><u>Retail</u></b>                  |                          |                          |
| Consumer loans                        | 11                       | 2                        |
| Single family residential             | 620                      | 1,180                    |
| Other retail                          | 74                       | 2                        |
| Total retail loans                    | 705                      | 1,184                    |
| <b>Total non-accrual loans</b>        | <b>\$ 705</b>            | <b>\$ 1,214</b>          |

Included in certain loan categories of impaired loans are certain loans that have been modified in a troubled debt restructuring where economic concessions have been granted to borrowers who have experienced financial difficulties. These concessions typically result from our loss mitigation activities and could include reductions in the interest rate, payment extensions, forgiveness of principal, forbearance or other actions. Modifications of terms for our loans and their inclusion as troubled debt restructurings are based on individual facts and circumstances. Loan modifications that are included as troubled debt restructurings may involve either an increase or reduction of the interest rate, extension of the term of the loan, or deferral of principal and/or interest payments, regardless of the period of the modification. All of the loans identified as troubled debt restructurings were modified due to financial stress of the borrower. In order to determine if a borrower is experiencing financial difficulty, an evaluation is performed to determine the probability that the borrower will be in payment default on any of its debt in the foreseeable future with the modification. This evaluation is performed under the Company's internal underwriting policy.

When the Company modifies loans in a troubled debt restructuring, the Company evaluates any possible impairment similar to other impaired loans based on the present value of expected future cash flows, discounted at the contractual interest rate of the original loan or lease agreement, or the current fair value of the collateral, less selling costs for collateral dependent loans. If the Company determined that the value of the modified loan is less than the recorded investment in the loan, impairment is recognized through an allowance estimate or a charge-off to the allowance. In periods subsequent to modification, the Company evaluates all troubled debt restructurings, including those that have payment defaults, for possible impairment and recognize impairment through the allowance.

Outstanding principal balances of troubled debt restructured loans were \$347,000 and \$624,000 as of December 31, 2022 and 2021, respectively. As of December 31, 2022, the Company did not have any commitments to extend additional funds to borrowers with loans modified and included as a troubled debt restructuring. During 2022, one loan was modified in troubled debt restructuring, where economic concessions were granted to borrowers consisting of reductions in the interest rates, payment extensions, forgiveness of principal, and forbearances.

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 4 – LOANS, (CONTINUED)**

Presented below, segregated by class of loans, are troubled debt restructurings:

| <b>Twelve months ended December 31, 2022</b> |                                                      |                                                          |      |
|----------------------------------------------|------------------------------------------------------|----------------------------------------------------------|------|
| <b>Number of<br/>modifications</b>           | <b>Post-modification<br/>outstanding<br/>balance</b> | <b>Net charge-offs<br/>resulting in<br/>modification</b> |      |
|                                              | (dollars in thousands)                               |                                                          |      |
| <b><u>Retail</u></b>                         |                                                      |                                                          |      |
| Consumer loans                               | 1                                                    | \$ 10                                                    | \$ - |

| <b>Twelve months ended December 31, 2021</b> |                                                      |                                                          |      |
|----------------------------------------------|------------------------------------------------------|----------------------------------------------------------|------|
| <b>Number of<br/>modifications</b>           | <b>Post-modification<br/>outstanding<br/>balance</b> | <b>Net charge-offs<br/>resulting in<br/>modification</b> |      |
|                                              | (dollars in thousands)                               |                                                          |      |
| <b><u>Retail</u></b>                         |                                                      |                                                          |      |
| Single family residential                    | 1                                                    | \$ 37                                                    | \$ - |

The loan's accrual status is assessed at the time of its modification. As a result of the assessment, the accrual status may be modified. The Company had loans modified in troubled debt restructurings that are in accrual status with outstanding balances of \$347,000 and \$357,000, as of December 31, 2022 and 2021, respectively. Loans modified in a troubled debt restructuring are closely monitored for delinquency as an early indicator of possible future default. If loans modified in a troubled debt restructuring subsequently default, the Company evaluates the loan for possible further impairment. The allowance for loan and lease losses may be increased, adjustments may be made in the allocation of the allowance, or partial charge-offs may be taken to further write-down the carrying value of the loan. The Company considers a loan in default when it is 90 days or more past due or transferred to non-accrual.

As of December 31, 2022 and 2021, the Company did not have any loans that were modified in troubled debt restructurings during the past twelve months that have subsequently defaulted.

As of December 31, 2022 and 2021, the Company held no foreclosed real estate. In addition, the Company had no consumer mortgage loans secured by residential real estate properties for which formal foreclosure proceedings are in process according to location requirement of the applicable jurisdiction.

*Credit Quality Indicators.* As part of the on-going monitoring of the credit quality of the Company's loan portfolio, management tracks certain credit quality indicators including trends related to (i) the weighted-average risk grade of commercial loans, (ii) the level of classified commercial loans, (iii) net charge-offs, (iv) non-performing loans, and (v) the general economic conditions in the State of Tennessee.

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 4 – LOANS, (CONTINUED)**

The Company uses a risk grading matrix to assign a risk grade to each of its commercial loans. Loans are graded on a scale of 1 through 8. A description of the general characteristics of the eight risk grades is as follows:

**Risk Rating 1 – Minimal Risk** – Loans in this category are secured by a cash deposit or fully guaranteed by the SBA and are substantially risk free.

**Risk Rating 2 – Modest Risk** – Loans in this category have borrowers that show profitability, liquidity, and capitalization better than industry norms and a strong market position in the region. The borrower of these loans have a proven history of profitability and financial stability, along with an abundance of financeable assets available to protect the Bank's position.

**Risk Rating 3 – Average Risk** – Loans in this category have borrowers that show a stable earnings history and financial condition in line with industry norms. The borrower's liquidity and leverage are in line with industry norms. The credit extension is considered sound; however, elements may be present which suggest the borrower may not be free from temporary impairments in the future.

**Risk Rating 4 – Acceptable Risk** – Loans in this category have sound risk profiles, in which the borrower shows satisfactory asset quality and liquidity, good debt capacity and coverage, and good management in critical positions.

**Risk Rating 5 – Pass/Watch** – Loans in this category require a heightened level of supervision. The borrower may exhibit declining earnings, strained cash flow, increasing leverage, or weakening market positions that indicate a trend toward an unacceptable risk. The borrowers liquidity, leverage, and earnings performance is below or trending below industry norms.

**Risk Rating 6 – Special Mention** – Loans in this category are not currently adequate. These loans have 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 institution's credit position at some future date. Special mention loans are not adversely classified and do not expose an institution to sufficient risk to warrant adverse classification.

**Risk Rating 7 – Substandard** – Loans in this category are inadequately protected by the current sound worth and paying capacity of the obligor of the collateral pledged, if any. These loans must have a well-defined weakness, or weaknesses, that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the Bank will sustain some loss if the deficiencies are not corrected.

**Risk Rating 8 – Doubtful** – Loans in this category have all the weaknesses inherent in one classified substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of current existing facts, conditions, and values, highly questionable and improbable.

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 4 – LOANS, (CONTINUED)**

The following table presents risk grades and classified loans by class:

**December 31, 2022**

Commercial loan portfolio:  
Credit risk profile by internally  
assigned grade

|                                 | Commercial<br>and industrial | Non-farm, non-<br>residential real<br>estate | Construction<br>and<br>development | Commercial<br>loans secured<br>by real estate | Other<br>commercial | Commercial<br>loan totals |
|---------------------------------|------------------------------|----------------------------------------------|------------------------------------|-----------------------------------------------|---------------------|---------------------------|
|                                 | (dollars in thousands)       |                                              |                                    |                                               |                     |                           |
| Risk rating 1 – minimal risk    | \$ 2,275                     | \$ 537                                       | \$ -                               | \$ -                                          | \$ 85               | \$ 2,897                  |
| Risk rating 2 – modest risk     | 611                          | -                                            | -                                  | -                                             | 43,695              | 44,306                    |
| Risk rating 3 – average risk    | 18,806                       | 52,975                                       | 9,997                              | 6,366                                         | 4,098               | 92,242                    |
| Risk rating 4 – acceptable risk | 53,157                       | 254,523                                      | 80,123                             | 94,045                                        | 6,391               | 488,239                   |
| Risk rating 5 – pass/watch      | 8,428                        | 9,200                                        | -                                  | 2,234                                         | -                   | 19,862                    |
| Risk rating 6 – special mention | -                            | -                                            | -                                  | -                                             | -                   | -                         |
| Risk rating 7 – substandard     | 440                          | 5,771                                        | -                                  | -                                             | -                   | 6,211                     |
| Totals                          | <u>\$ 83,717</u>             | <u>\$ 323,006</u>                            | <u>\$ 90,120</u>                   | <u>\$ 102,645</u>                             | <u>\$ 54,269</u>    | <u>\$ 653,757</u>         |

Retail loan portfolio: Credit risk  
profiles based on delinquency  
status classification

|                                 | Consumer               | Single family<br>residential ** | Other retail    | Retail loan<br>totals |
|---------------------------------|------------------------|---------------------------------|-----------------|-----------------------|
|                                 | (dollars in thousands) |                                 |                 |                       |
| Performing – risk ratings 1 – 6 | \$ 6,481               | \$ 295,752                      | \$ 9,070        | \$ 311,303            |
| Risk rated 7*                   | 21                     | 1,086                           | -               | 1,107                 |
| Totals                          | <u>\$ 6,502</u>        | <u>\$ 296,838</u>               | <u>\$ 9,070</u> | <u>\$ 312,410</u>     |

\*Loans are classified as nonperforming loans and are automatically placed on nonaccrual status once they reach 90 days past due. For the purposes of this table, the total includes all risk rated 7 loans, of which may be performing or nonperforming.

\*\*Single family residential loans includes first mortgages, closed-end second mortgages, residential construction loans, and home equity lines of credit (HELOCs).

**December 31, 2021**

Commercial loan portfolio:  
Credit risk profile by internally  
assigned grade

|                                 | Commercial<br>and industrial | Non-farm, non-<br>residential real<br>estate | Construction<br>and<br>development | Commercial<br>loans secured<br>by real estate | Other<br>commercial | Commercial<br>loan totals |
|---------------------------------|------------------------------|----------------------------------------------|------------------------------------|-----------------------------------------------|---------------------|---------------------------|
|                                 | (dollars in thousands)       |                                              |                                    |                                               |                     |                           |
| Risk rating 1 – minimal risk    | \$ 1,271                     | \$ 27                                        | \$ -                               | \$ -                                          | \$ 92               | \$ 1,390                  |
| Risk rating 2 – modest risk     | 8,345                        | -                                            | -                                  | -                                             | 32,540              | 40,885                    |
| Risk rating 3 – average risk    | 12,936                       | 40,246                                       | 14,248                             | 3,169                                         | 2,755               | 73,354                    |
| Risk rating 4 – acceptable risk | 58,870                       | 200,082                                      | 90,702                             | 71,094                                        | 6,905               | 427,653                   |
| Risk rating 5 – pass/watch      | 398                          | 5,834                                        | 630                                | 700                                           | -                   | 7,562                     |
| Risk rating 6 – special mention | -                            | 10,545                                       | -                                  | -                                             | -                   | 10,545                    |
| Risk rating 7 – substandard     | 4,420                        | 6,120                                        | -                                  | -                                             | -                   | 10,540                    |
| Totals                          | <u>\$ 86,240</u>             | <u>\$ 262,854</u>                            | <u>\$ 105,580</u>                  | <u>\$ 74,963</u>                              | <u>\$ 42,292</u>    | <u>\$ 571,929</u>         |

Retail loan portfolio: Credit risk  
profiles based on delinquency  
status classification

|                                 | Consumer               | Single family<br>residential ** | Other retail     | Retail loan<br>totals |
|---------------------------------|------------------------|---------------------------------|------------------|-----------------------|
|                                 | (dollars in thousands) |                                 |                  |                       |
| Performing – risk ratings 1 – 6 | \$ 6,549               | \$ 294,816                      | \$ 11,954        | \$ 313,319            |
| Risk rated 7*                   | 4                      | 1,637                           | 2                | 1,643                 |
| Totals                          | <u>\$ 6,553</u>        | <u>\$ 296,453</u>               | <u>\$ 11,956</u> | <u>\$ 314,962</u>     |

\*Loans are classified as nonperforming loans and are automatically placed on nonaccrual status once they reach 90 days past due. For the purposes of this table, the total includes all risk rated 7 loans, of which may be performing or nonperforming.

\*\*Single family residential loans includes first mortgages, closed-end second mortgages, residential construction loans, and home equity lines of credit (HELOCs).

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 5 – ALLOWANCE FOR LOAN AND LEASE LOSSES**

The allowance for loan and lease losses (“ALLL” or the “allowance”) is a reserve established through a provision for loan and lease losses charged to expense, which represents management’s best estimate of probable losses that have been incurred within the existing portfolio of loans. The allowance, in the judgment of management, is necessary to reserve for estimated loan losses and risks inherent in the loan portfolio. The Company’s allowance for loan and lease loss methodology includes allowance allocations calculated in accordance with ASC Topic 310, “Receivables” and allowance allocations calculated in accordance with ASC Topic 450, “Contingencies.” Accordingly, the methodology is based on historical loss experience by type of credit and internal risk grade, specific homogeneous risk pools and specific loss allocations, with adjustments for current events and conditions. The Company’s process for determining the appropriate level of the allowance for loan losses is designed to account for credit deterioration as it occurs. The provision for loan and lease losses reflects loan quality trends, including the levels of and trends related to nonaccrual loans, past due loans, potential problem loans, criticized loans, and net charge-offs or recoveries, among other factors. The provision for loan and lease losses also reflects the totality of actions taken on all loans for a particular period. In other words, the amount of the provision reflects not only the necessary increases in the allowance for loan losses related to newly identified criticized loans, but it also reflects actions taken related to other loans including, among other things, any necessary increases or decreases in required allowances for specific loans or loan pools.

The level of the allowance reflects management’s continuing evaluation of industry concentrations, specific credit risks, loan loss experience, current loan portfolio quality, present economic, political and regulatory conditions, and unidentified losses inherent in the current loan portfolio. Portions of the allowance may be allocated for specific credits; however, the entire allowance is available for any credit that, in management’s judgment, should be charged off. While management utilizes its best judgment and information available, the ultimate adequacy of the allowance is dependent upon a variety of factors beyond the Company’s control, including, among other things, the performance of the Company’s loan portfolio, the economy, changes in interest rates, and the view of the regulatory authorities toward loan classifications.

The Company’s allowance for loan losses consists of three elements: (i) specific valuation allowances determined in accordance with ASC Topic 310 based on probable losses on specific loans; (ii) historical valuation allowances determined in accordance with ASC Topic 450 based on historical loan loss experience for similar loans with similar characteristics and trends, adjusted, as necessary, to reflect the impact of current conditions; and (iii) general valuation allowances determined in accordance with ASC Topic 450 based on general economic conditions and other qualitative risk factors both internal and external to the Company.

The allowances established for probable losses on specific loans are based on a regular analysis and evaluation of problem loans. Commercial loans are classified based on an internal credit risk grading process that evaluates, among other things: (i) the obligor’s ability to repay; (ii) the underlying collateral, if any; and (iii) the economic environment and industry in which the borrower operates. This analysis is performed at the relationship manager level for all commercial loans. When a loan has a calculated grade of seven or higher, a special assets officer analyzes the loan to determine whether the loan is impaired and, if impaired, the need to specifically allocate a portion of the allowance for loan losses to the loan. Specific valuation allowances are determined by analyzing the borrower’s ability to repay amounts owed, collateral deficiencies, the relative risk grade of the loan and economic conditions affecting the borrower’s industry, among other things.

Historical valuation allowances are calculated based on the historical loss experience of specific types of loans and the internal risk grade of such loans at the time they were charged-off. The Company calculates historical loss ratios for pools of similar loans with similar characteristics based on the proportion of actual charge-offs experienced to the total population of loans in the pool. The historical loss ratios are periodically updated based on actual charge-off experience. A historical valuation allowance is established for each pool of similar loans based upon the product of the historical loss ratio and the total dollar amount of the loans in the pool. The Company’s pools of similar loans include similarly risk-graded groups of commercial and industrial loans, commercial real estate loans, consumer real estate loans, and consumer and other loans.

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 5 – ALLOWANCE FOR LOAN AND LEASE LOSSES, (CONTINUED)**

The allowance for loan and lease losses is maintained at a level considered adequate to provide for the losses that can be reasonably anticipated. Management's periodic evaluation of the adequacy of the allowance is based on the Company's past loan loss experience, known and inherent risks in the portfolio, adverse situations that may affect the borrower's ability to repay, the estimated value of any underlying collateral, composition of the loan portfolio, current economic conditions and other relevant factors. This evaluation is inherently subjective as it requires material estimates that may be susceptible to change. The Company uses a rolling twenty quarters historic loss period for all segments when estimating the historical charge-off rates calculated in accordance with ASC Topic 450. Management assesses a volatility factor on certain loan pools for the purpose of capturing historical loss risk for the loan pools where the average loss rate may not capture the historical loss risk.

General valuation allowances are based on general economic conditions and other qualitative risk factors both internal and external to the Company. In general, such valuation allowances are determined by evaluating, among other things: (i) current delinquency trends; (ii) the impact of economic events on portfolio risks; (iii) the experience, ability and effectiveness of the Bank's lending management and staff; (iv) the effectiveness of the Company's loan policies, procedures and internal controls; (v) changes in asset quality; (vi) new volume loan growth trends; (vii) the composition and concentrations of credit; (viii) the impact of competition on loan structuring and pricing; (ix) the effectiveness of the internal loan review function; and (x) the impact of environmental events on portfolio risks. Management evaluates the degree of risk that each one of these components has on the quality of the loan portfolio on a quarterly basis. Each component is determined to have either a high, moderate, or low degree of risk. The results are then input into a "general allocation matrix" to determine an appropriate general valuation allowance.

Included in the general valuation allowances are allocations for groups of similar loans with risk characteristics that exceed certain concentration limits established by management. Concentration risk limits have been established, among other things, for certain industry concentrations, large balance and highly leveraged credit relationships that exceed specified risk grades, and loans originated with policy exceptions that exceed specified risk grades.

The allocations for general valuation allowances were adjusted to capture the current economic risk. The Company reviews certain local, state, and national economic data to assess risk associated with current economic conditions. The economic data that is reviewed by management includes local and state unemployment rates, the Fed's policies on interest rates, the U.S. savings rate, and the nation's Gross Domestic Product outlook.

Loans identified as losses by management and internal loan review are charged off. Furthermore, consumer loan accounts are charged off automatically based on regulatory requirements.

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 5 – ALLOWANCE FOR LOAN AND LEASE LOSSES, (CONTINUED)**

The following tables summarize the allocation in the ALLL by loan segment:

|                                         |  | <b>Beginning<br/>balance</b> | <b>Charge-offs</b> | <b>Recoveries</b> | <b>Provision<br/>(Provision<br/>credit)</b> | <b>Ending<br/>balance</b> |
|-----------------------------------------|--|------------------------------|--------------------|-------------------|---------------------------------------------|---------------------------|
| <b>December 31, 2022</b>                |  |                              |                    |                   |                                             |                           |
| <b>Commercial:</b>                      |  |                              |                    |                   |                                             |                           |
| Commercial and industrial               |  | \$ 1,917                     | \$ (4)             | \$ 28             | \$ 10                                       | \$ 1,951                  |
| Non-farm, non-residential real estate   |  | 3,351                        | -                  | -                 | (242)                                       | 3,109                     |
| Construction and development            |  | 946                          | -                  | -                 | 62                                          | 1,008                     |
| Commercial loans secured by real estate |  | 1,679                        | -                  | -                 | (112)                                       | 1,567                     |
| Other commercial                        |  | 654                          | -                  | -                 | (48)                                        | 606                       |
| Total commercial                        |  | <u>8,547</u>                 | <u>(4)</u>         | <u>28</u>         | <u>(330)</u>                                | <u>8,241</u>              |
| <b>Retail:</b>                          |  |                              |                    |                   |                                             |                           |
| Consumer loans                          |  | 201                          | (6)                | 2                 | -                                           | 197                       |
| Single family residential               |  | 124                          | -                  | 95                | (2)                                         | 217                       |
| Other retail                            |  | 733                          | (24)               | 6                 | 12                                          | 727                       |
| Total retail                            |  | <u>1,058</u>                 | <u>(30)</u>        | <u>103</u>        | <u>10</u>                                   | <u>1,141</u>              |
| <b>Totals</b>                           |  | <u>\$ 9,605</u>              | <u>\$ (34)</u>     | <u>\$ 131</u>     | <u>\$ (320)</u>                             | <u>\$ 9,382</u>           |

|                                         |  | <b>Beginning<br/>balance</b> | <b>Charge-offs</b> | <b>Recoveries</b> | <b>Provision<br/>(Provision<br/>credit)</b> | <b>Ending<br/>balance</b> |
|-----------------------------------------|--|------------------------------|--------------------|-------------------|---------------------------------------------|---------------------------|
| <b>December 31, 2021</b>                |  |                              |                    |                   |                                             |                           |
| <b>Commercial:</b>                      |  |                              |                    |                   |                                             |                           |
| Commercial and industrial               |  | \$ 1,923                     | \$ (6)             | \$ 129            | \$ (129)                                    | \$ 1,917                  |
| Non-farm, non-residential real estate   |  | 3,361                        | -                  | -                 | (10)                                        | 3,351                     |
| Construction and development            |  | 875                          | -                  | -                 | 71                                          | 946                       |
| Commercial loans secured by real estate |  | 1,677                        | -                  | -                 | 2                                           | 1,679                     |
| Other commercial                        |  | 676                          | -                  | -                 | (22)                                        | 654                       |
| Total commercial                        |  | <u>8,512</u>                 | <u>(6)</u>         | <u>129</u>        | <u>(88)</u>                                 | <u>8,547</u>              |
| <b>Retail:</b>                          |  |                              |                    |                   |                                             |                           |
| Consumer loans                          |  | 189                          | (8)                | 21                | (1)                                         | 201                       |
| Single family residential               |  | 270                          | (93)               | 4                 | (57)                                        | 124                       |
| Other retail                            |  | 744                          | (10)               | 3                 | (4)                                         | 733                       |
| Total retail                            |  | <u>1,203</u>                 | <u>(111)</u>       | <u>28</u>         | <u>(62)</u>                                 | <u>1,058</u>              |
| <b>Totals</b>                           |  | <u>\$ 9,715</u>              | <u>\$ (117)</u>    | <u>\$ 157</u>     | <u>\$ (150)</u>                             | <u>\$ 9,605</u>           |

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 5 – ALLOWANCE FOR LOAN AND LEASE LOSSES, (CONTINUED)**

The following tables detail the amount of the ALLL allocated to each portfolio segment as of December 31, 2022 and 2021, disaggregated on the basis of the Company's impairment methodology:

|                                         |    | Loans individually<br>evaluated for<br>impairment | Loans collectively<br>evaluated for<br>impairment | Ending balance  |
|-----------------------------------------|----|---------------------------------------------------|---------------------------------------------------|-----------------|
| <b>December 31, 2022</b>                |    |                                                   |                                                   |                 |
| <b>Commercial:</b>                      |    |                                                   |                                                   |                 |
| Commercial and industrial               | \$ | -                                                 | \$ 1,951                                          | \$ 1,951        |
| Non-farm, non-residential real estate   |    | -                                                 | 3,109                                             | 3,109           |
| Construction and development            |    | -                                                 | 1,008                                             | 1,008           |
| Commercial loans secured by real estate |    | -                                                 | 1,567                                             | 1,567           |
| Other commercial                        |    | -                                                 | 606                                               | 606             |
| Total commercial                        |    | -                                                 | 8,241                                             | 8,241           |
| <b>Retail:</b>                          |    |                                                   |                                                   |                 |
| Consumer loans                          |    | -                                                 | 197                                               | 197             |
| Single family residential               |    | -                                                 | 217                                               | 217             |
| Other retail                            |    | -                                                 | 727                                               | 727             |
| Total retail                            |    | -                                                 | 1,141                                             | 1,141           |
| <b>Totals</b>                           |    | <b>\$ -</b>                                       | <b>\$ 9,382</b>                                   | <b>\$ 9,382</b> |

  

|                                         |    | Loans individually<br>evaluated for<br>impairment | Loans collectively<br>evaluated for<br>impairment | Ending balance  |
|-----------------------------------------|----|---------------------------------------------------|---------------------------------------------------|-----------------|
| <b>December 31, 2021</b>                |    |                                                   |                                                   |                 |
| <b>Commercial:</b>                      |    |                                                   |                                                   |                 |
| Commercial and industrial               | \$ | -                                                 | \$ 1,917                                          | \$ 1,917        |
| Non-farm, non-residential real estate   |    | -                                                 | 3,351                                             | 3,351           |
| Construction and development            |    | -                                                 | 946                                               | 946             |
| Commercial loans secured by real estate |    | -                                                 | 1,679                                             | 1,679           |
| Other commercial                        |    | -                                                 | 654                                               | 654             |
| Total commercial                        |    | -                                                 | 8,547                                             | 8,547           |
| <b>Retail:</b>                          |    |                                                   |                                                   |                 |
| Consumer loans                          |    | -                                                 | 201                                               | 201             |
| Single family residential               |    | 1                                                 | 123                                               | 124             |
| Other retail                            |    | -                                                 | 733                                               | 733             |
| Total retail                            |    | 1                                                 | 1,057                                             | 1,058           |
| <b>Totals</b>                           |    | <b>\$ 1</b>                                       | <b>\$ 9,604</b>                                   | <b>\$ 9,605</b> |

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 5 – ALLOWANCE FOR LOAN AND LEASE LOSSES, (CONTINUED)**

The following tables show loans as of December 31, 2022 and 2021 related to each balance in the allowance for loan and lease losses by portfolio segment and disaggregated on the basis of the Company's impairment methodology:

|                                         | Loans individually<br>evaluated for<br>impairment | Loans collectively<br>evaluated for<br>impairment | Ending balance    |
|-----------------------------------------|---------------------------------------------------|---------------------------------------------------|-------------------|
| <b>December 31, 2022</b>                |                                                   |                                                   |                   |
| <b>Commercial:</b>                      |                                                   |                                                   |                   |
| Commercial and industrial               | \$ -                                              | \$ 83,717                                         | \$ 83,717         |
| Non-farm, non-residential real estate   | 73                                                | 322,933                                           | 323,006           |
| Construction and development            | -                                                 | 90,120                                            | 90,120            |
| Commercial loans secured by real estate | -                                                 | 102,645                                           | 102,645           |
| Other commercial                        | -                                                 | 54,269                                            | 54,269            |
| Total commercial                        | 73                                                | 653,684                                           | 653,757           |
| <b>Retail:</b>                          |                                                   |                                                   |                   |
| Consumer loans                          | 11                                                | 6,491                                             | 6,502             |
| Single family residential               | 910                                               | 295,928                                           | 296,838           |
| Other retail                            | 74                                                | 8,996                                             | 9,070             |
| Total retail                            | 995                                               | 311,415                                           | 312,410           |
| <b>Totals</b>                           | <b>\$ 1,068</b>                                   | <b>\$ 965,099</b>                                 | <b>\$ 966,167</b> |

|                                         | Loans individually<br>evaluated for<br>impairment | Loans collectively<br>evaluated for<br>impairment | Ending balance    |
|-----------------------------------------|---------------------------------------------------|---------------------------------------------------|-------------------|
| <b>December 31, 2021</b>                |                                                   |                                                   |                   |
| <b>Commercial:</b>                      |                                                   |                                                   |                   |
| Commercial and industrial               | \$ 18                                             | \$ 86,222                                         | \$ 86,240         |
| Non-farm, non-residential real estate   | 86                                                | 262,768                                           | 262,854           |
| Construction and development            | -                                                 | 105,580                                           | 105,580           |
| Commercial loans secured by real estate | -                                                 | 74,963                                            | 74,963            |
| Other commercial                        | -                                                 | 42,292                                            | 42,292            |
| Total commercial                        | 104                                               | 571,825                                           | 571,929           |
| <b>Retail:</b>                          |                                                   |                                                   |                   |
| Consumer loans                          | 2                                                 | 6,551                                             | 6,553             |
| Single family residential               | 1,482                                             | 294,971                                           | 296,453           |
| Other retail                            | 2                                                 | 11,954                                            | 11,956            |
| Total retail                            | 1,486                                             | 313,476                                           | 314,962           |
| <b>Totals</b>                           | <b>\$ 1,590</b>                                   | <b>\$ 885,301</b>                                 | <b>\$ 886,891</b> |

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 6 – PREMISES AND EQUIPMENT**

The following table presents the Company's fixed assets by category:

|                                  | <u>2022</u>            | <u>2021</u>      |
|----------------------------------|------------------------|------------------|
|                                  | (dollars in thousands) |                  |
| Land                             | \$ 12,869              | \$ 12,905        |
| Premises                         | 26,410                 | 26,300           |
| Furniture and equipment          | 13,316                 | 13,154           |
| Leasehold improvements           | 2,158                  | 2,156            |
| Right-of-use assets              | 4,501                  | 4,648            |
| Construction in progress         | 883                    | 256              |
| Bank premises and equipment      | 60,138                 | 59,419           |
| Less accumulated depreciation    | (27,998)               | (26,792)         |
| Bank premises and equipment, net | <u>\$ 32,140</u>       | <u>\$ 32,627</u> |

Depreciation expense was \$1.8 million, \$2.0 million, and \$2.1 million for 2022, 2021, and 2020, respectively.

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 7 – RELATED PARTY TRANSACTIONS**

Certain related parties as identified under the guidance in *ASC 850-05 Related Party Disclosures* were customers of, and had loans and other transactions with, the Bank in the ordinary course of business. An analysis of the activity with respect to such loans are shown in the table below. These totals exclude loans made in the ordinary course of business to other companies with which neither the Company nor the Bank had a relationship other than the association of one of its directors in the capacity of officer or director.

The Bank has granted loans to certain related parties including directors and their related interests. These loan transactions were made in the ordinary course of business on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable loans to persons not related to the Bank and did not involve more than the normal risk of collectability or present other unfavorable features. None of these loans to directors and their related interests are impaired at December 31, 2022 and 2021. Changes in related party loans for the years ended December 31, 2022 and 2021 are as follows:

|                                                         | <u>2022</u>            | <u>2021</u>     |
|---------------------------------------------------------|------------------------|-----------------|
|                                                         | (dollars in thousands) |                 |
| Related party extensions of credit, beginning of period | \$ 4,349               | \$ 3,785        |
| New loans                                               | 288                    | 1,851           |
| Repayments or reductions                                | <u>(1,392)</u>         | <u>(1,287)</u>  |
| Related party extension of credit, end of period        | <u>\$ 3,245</u>        | <u>\$ 4,349</u> |

The aggregate balances of related party deposits at December 31, 2022 and 2021 were \$51.7 million and \$69 million, respectively. The aggregate balances of related party insured cash sweep accounts at December 31, 2022 and 2021 were \$44.7 million and \$37.7 million, respectively.

The aggregate managed asset balances of certain related parties that receive trust and wealth management services at December 31, 2022 and 2021 were \$933 million and \$1.1 billion, respectively. The aggregate non-managed asset balances of certain related parties that receive trust and wealth management services at December 31, 2022 and 2021 were \$3.6 billion and \$4.1 billion, respectively. Trust service fees earned from trust accounts held by related parties during 2022, 2021, and 2020 were \$782,000, \$753,000 and \$612,000, respectively.

The Company and Bank utilize various services and purchased goods provided by certain related parties, in which some are governed by contractual agreements. Payments to related parties for services provided during 2022, 2021 and 2020 totaled \$243,000, \$276,000 and \$270,000, respectively.

The Company's equity securities at December 31, 2022 and 2021 reflect investment in the stock of a related party.

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 8 – LEASES**

The Bank has entered into various operating and finance leases primarily for office space and branch facilities. The Bank recognizes right-of-use assets and lease liabilities related to its operating and finance leases. Right-of-use assets represent our right to use an underlying asset for the lease term and lease liabilities represent our obligation to make lease payments arising from the lease.

Right-of-use assets and lease liabilities related to the Bank's operating and finance leases are as follows:

| <b>Balance sheet location</b> |                                          | <b>(dollars in thousands)</b> |                 |
|-------------------------------|------------------------------------------|-------------------------------|-----------------|
|                               |                                          | <b>2022</b>                   | <b>2021</b>     |
| Right-of-use assets           |                                          |                               |                 |
| Operating leases              | Other assets                             | \$ 195                        | \$ 241          |
| Finance leases                | Bank premises and equipment, net         | 2,774                         | 3,206           |
| Total right-of-use assets     |                                          | <u>\$ 2,969</u>               | <u>\$ 3,447</u> |
| Leases liabilities            |                                          |                               |                 |
| Operating leases              | Accounts payable and accrued liabilities | \$ 195                        | 241             |
| Finance leases                | Accounts payable and accrued liabilities | 3,176                         | 3,625           |
| Total lease liabilities       |                                          | <u>\$ 3,371</u>               | <u>\$ 3,866</u> |

The following table presents lease costs related to these leases:

|                                    | <b>December 31,<br/>2022</b>  | <b>December 31,<br/>2021</b> |
|------------------------------------|-------------------------------|------------------------------|
|                                    | <b>(dollars in thousands)</b> |                              |
| Operating lease cost               | \$ 46                         | \$ 43                        |
| Finance lease cost:                |                               |                              |
| Interest on lease liabilities      | 111                           | 128                          |
| Amortization of right-of-use asset | 432                           | 481                          |
| Net lease cost                     | <u>\$ 589</u>                 | <u>\$ 652</u>                |

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 8 – LEASES, (CONTINUED)**

The following table presents the weighted average remaining lease term and weighted average discount rate used to determine lease liabilities:

| Weighted average remaining lease term (years): | <b>December 31, 2022</b> | <b>December 31, 2021</b> |
|------------------------------------------------|--------------------------|--------------------------|
| Operating leases                               | 3.9                      | 4.9                      |
| Finance leases                                 | 7.6                      | 8.4                      |
| Weighted average discount rate:                |                          |                          |
| Operating leases                               | 3.09%                    | 3.09%                    |
| Finance leases                                 | 3.36%                    | 3.34%                    |

The following table presents a maturity analysis of undiscounted cash flows due under operating leases and finance leases and a reconciliation to total operating lease liabilities and finance lease liabilities:

|                         | <b>December 31, 2022</b> |                       |
|-------------------------|--------------------------|-----------------------|
|                         | <b>Operating leases</b>  | <b>Finance leases</b> |
|                         | (dollars in thousands)   |                       |
| 2023                    | \$ 53                    | \$ 552                |
| 2024                    | 53                       | 553                   |
| 2025                    | 53                       | 557                   |
| 2026                    | 48                       | 537                   |
| 2027                    | -                        | 339                   |
| Thereafter              | -                        | 1,079                 |
| Total                   | 207                      | 3,617                 |
| Less: Imputed interest  | (12)                     | (440)                 |
| Total lease liabilities | \$ 195                   | \$ 3,177              |

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 9 – FEDERAL AND STATE INCOME TAXES**

The following table presents components of income tax expense (benefit) attributable to continuing operations:

|                                  | <u>2022</u>            | <u>2021</u>     | <u>2020</u>     |
|----------------------------------|------------------------|-----------------|-----------------|
|                                  | (dollars in thousands) |                 |                 |
| Current                          | \$ 4,244               | \$ 3,770        | \$ 3,739        |
| Deferred                         | <u>(27)</u>            | <u>(282)</u>    | <u>(954)</u>    |
| Total provision for income taxes | <u>\$ 4,217</u>        | <u>\$ 3,448</u> | <u>\$ 2,785</u> |

A reconciliation between reported income tax expense and the amounts computed by applying the U.S. federal statutory income tax rate of 21% to income before income taxes is presented in the following table:

|                                               | <u>2022</u>            | <u>2021</u>     | <u>2020</u>     |
|-----------------------------------------------|------------------------|-----------------|-----------------|
|                                               | (dollars in thousands) |                 |                 |
| Tax expense at statutory rate                 | \$ 4,676               | \$ 4,012        | \$ 3,566        |
| Increase (decrease) in taxes resulting from:  |                        |                 |                 |
| Tax-exempt interest                           | (520)                  | (558)           | (605)           |
| Nondeductible interest expense                | 23                     | 16              | 12              |
| Employee benefits                             | (106)                  | (113)           | (283)           |
| Other nondeductible expenses                  |                        |                 |                 |
| (nontaxable income) - net                     | 7                      | 8               | 11              |
| State income taxes net of federal tax benefit | 134                    | 127             | 77              |
| Other                                         | <u>3</u>               | <u>(4)</u>      | <u>7</u>        |
| Total provision for income taxes              | <u>\$ 4,217</u>        | <u>\$ 3,488</u> | <u>\$ 2,785</u> |
| Effective tax rate                            | <u>18.9%</u>           | <u>18.3%</u>    | <u>16.4%</u>    |

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 9 – FEDERAL AND STATE INCOME TAXES, (CONTINUED)**

Year-end net deferred taxes included on the Company's balance sheets are presented in the table below.

|                                                            | (dollars in thousands) |                 |
|------------------------------------------------------------|------------------------|-----------------|
|                                                            | <b>2022</b>            | <b>2021</b>     |
| Deferred tax effects of principal temporary differences    |                        |                 |
| Allowance for loan and lease losses                        | \$ 2,450               | \$ 2,510        |
| Deferred compensation                                      | 2,917                  | 2,919           |
| Amortization of intangibles                                | (2,100)                | (2,100)         |
| Recognition of nonaccrual loan income                      | 70                     | 67              |
| Unrealized (gains)/losses on available-for-sale securities | 28,278                 | 1,792           |
| Post-retirement benefit obligation                         | 395                    | 480             |
| Accelerated depreciation                                   | (830)                  | (872)           |
| Prepaid expenses                                           | (37)                   | (39)            |
| REIT dividends                                             | (359)                  | (299)           |
| Loan fees                                                  | 342                    | 332             |
| FHLB stock dividends                                       | (344)                  | (428)           |
| Right-of-use asset                                         | (725)                  | (901)           |
| Lease liability                                            | 881                    | 1,010           |
| Other                                                      | 18                     | (10)            |
| Net deferred tax asset                                     | <u>\$ 30,956</u>       | <u>\$ 4,461</u> |

No valuation allowance for deferred tax assets was recorded at December 31, 2022 and 2021 as management believes it is more likely than not that all of the deferred tax assets will be realized against deferred tax liabilities and projected future taxable income. There were no unrecognized tax benefits during any of the reported periods.

The Company and its subsidiaries file income tax returns with the Internal Revenue Service, State of Tennessee and State of Alabama. The Company is not subject to U.S. federal, state and local, or non-U.S. income tax examinations by tax authorities for years prior to 2019.

**NOTE 10 – BORROWED FUNDS**

The Bank is a party to the Blanket Agreement for Advances and Security Agreement (the "Blanket Agreement") with the Federal Home Loan Bank of Cincinnati (the "FHLB"). Advances made to the Bank under the Blanket Agreement are collateralized by the FHLB stock and qualifying residential mortgage loans totaling 150% of the outstanding amount borrowed. These collateralization matters are outlined in the Blanket Agreement dated June 20, 2006 between the Bank and the FHLB. As of December 31, 2022 and 2021, the FHLB advances totaled \$25 million and \$0, respectively. Pursuant to collateral agreements with the FHLB, advances are secured by all the stock invested in the FHLB and certain qualifying mortgage loans. The advances were collateralized by \$254.4 million and \$223.1 million of first mortgage and Home Equity Line of Credit ("HELOC") loans under a blanket lien arrangement at December 31, 2022 and 2021, respectively. Based on this collateral and the Company's holdings of FHLB stock, the Bank was eligible to borrow up to a total of \$188.4 million in additional advances at December 31, 2022.

Stock held in the FHLB totaling \$5.2 million and \$3.3 million at December 31, 2022 and 2021, respectively, is carried at cost. The stock is restricted, can only be sold back to the FHLB at par, and is included in other assets on the consolidated balance sheet.

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 11 – SIGNIFICANT ESTIMATES, COMMITMENTS, AND CONTINGENCIES**

GAAP requires disclosure of certain significant estimates and current vulnerabilities due to certain concentrations. Estimates related to the ALLL are reflected in the Note 5 – Allowance for Loan and Lease Losses. Other significant estimates and concentrations not discussed in those footnotes include:

**General Litigation**

The Company is subject to claims and lawsuits that arise primarily in the ordinary course of business. It is the opinion of management that the disposition or ultimate resolution of such claims and lawsuits will not have a material adverse effect on the consolidated financial position, results of operations, cash flows and disclosures of the Company.

**Pension and Other Post-Retirement Benefit Obligations**

The Company has a noncontributory defined benefit post-retirement health care plan whereby it agrees to provide certain post-retirement benefits to eligible employees. The benefit obligation is the actuarial present value of all benefits attributed to service rendered prior to the valuation date based on the projected unit credit cost method. It is reasonably possible that events could occur that would change the estimated amount of this liability materially in the near term.

**Self-Insurance Reserves**

The Company is self-insured for its employees' health benefit programs, which include medical, dental, and prescription drug benefits. The costs of the Company's employee health insurance benefits, including paid claims, an estimate of incurred but not reported ("IBNR") claims, stop loss premiums and administrative fees are included in salaries and employee benefits on the consolidated statements of income.

The accrual for stop loss premiums and employee health insurance benefits is based on analysis performed internally by management. There was no receivable for stop loss premiums at December 31, 2022 and 2021. The liability for employee health insurance benefits at December 31, 2022 and 2021 was \$356,000 and \$400,000, respectively. The Company analyzes the liability on a regular basis for the IBNR claims and believes the reserves are adequate. However, judgement is involved in assessing these reserves, such as assessing historical claims paid, average lag times between claims incurred dates, reported dates and paid dates, and the frequency and severity of claims. There may be differences between actual settlement amounts and recorded reserves and any resulting adjustment is included in expense once a probable amount is known. Any significant increase in the number of employee health insurance claims or costs of those claims above our recorded reserve could have a material impact to our financial results. The Company mitigates the risk of potential claims for both individual participants and in the aggregate by carrying stop loss insurance coverage.

**Current Economic Conditions**

The accompanying financial statements have been prepared using values and information currently available to the Company. Given the potential for volatility of economic conditions, the values of assets and liabilities recorded in the financial statements could change rapidly, resulting in material future adjustments in asset values, the ALLL and capital that could negatively impact the Company's ability to meet regulatory capital requirements and maintain sufficient liquidity. Furthermore, the Company's regulators could require material adjustments to asset values or the allowance for loan and lease losses for regulatory capital purposes that could affect the Company's measurement of regulatory capital and compliance with the capital adequacy guidelines under the regulatory framework for prompt corrective action.

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 11 – SIGNIFICANT ESTIMATES, COMMITMENTS, AND CONTINGENCIES, (CONTINUED)**

**Commitments and Credit Risk**

The Company grants commercial, consumer, and residential loans to customers primarily throughout the States of Tennessee and Alabama. The Bank is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit and standby letters of credit. Those instruments involve, to varying degrees, elements of credit risk in excess of the amount recognized in the balance sheet. The contract or notional amounts of those instruments reflect the extent of involvement the Bank has in those particular financial instruments.

**Commitments to Originate Loans**

Commitments to originate loans are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since a portion of the commitments may expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. Each customer's creditworthiness is evaluated on a case-by-case basis. The amount of collateral obtained, if deemed necessary, is based on management's credit evaluation of the counterparty. Collateral held varies, but may include accounts receivable, inventory, property, plant and equipment, commercial real estate, and residential real estate.

Mortgage loans in the process of origination represent amounts that the Company plans to fund within a normal period of 30 to 90 days, and which are intended for sale to investors in the secondary market. Total mortgage loans in process of origination were \$376,000 and \$2.6 million at December 31, 2022 and 2021, respectively. Total mortgage loans held-for-sale amounted to \$0 and \$2.2 million, at December 31, 2022 and 2021, respectively.

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 11 – SIGNIFICANT ESTIMATES, COMMITMENTS, AND CONTINGENCIES, (CONTINUED)**

**Standby Letters of Credit**

Standby letters of credit are irrevocable conditional commitments issued by the Company to guarantee the performance of a customer to a third party. Financial standby letters of credit are primarily issued to support public and private borrowing arrangements, including commercial paper, bond financing and similar transactions. Performance standby letters of credit are issued to guarantee performance of certain customers under nonfinancial contractual obligations. The credit risk involved in issuing standby letters of credit is essentially the same as that involved in extending loans to customers. Should the Company be obligated to perform under the standby letters of credit, the Company may seek recourse from the customer for reimbursement of amounts paid. The Company had total outstanding standby letters of credit amounting to \$12.9 million and \$46 million, at December 31, 2022 and 2021, respectively, with terms ranging from seven days to 24 months.

**Lines of Credit**

Lines of credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Lines of credit generally have fixed expiration dates. Since a portion of the line may expire without being drawn upon, the total unused lines do not necessarily represent future cash requirements. Each customer's creditworthiness is evaluated on a case-by-case basis. The amount of collateral obtained, if deemed necessary, is based on management's credit evaluation of the counterparty. Collateral held varies but may include accounts receivable, inventory, property, plant and equipment, commercial real estate, and residential real estate. Management uses the same credit policies in granting lines of credit as it does for on-balance-sheet instruments.

At December 31, 2022, the Company had granted unused lines of credit to borrowers for commercial lines and open-end consumer lines aggregating \$183.0 million and \$95.5 million, respectively. At December 31, 2021, unused lines of credit to borrowers for commercial lines and open-end consumer lines aggregated \$176.1 million and \$82.1 million, respectively.

**NOTE 12 – FAIR VALUE MEASUREMENT**

The fair value of an asset or liability is the exchange price that would be received for an asset or paid to transfer a liability or exit price in an orderly transaction between market participants on the measurement date. Fair value measurement must maximize the use of observable inputs and minimize the use of unobservable inputs. In estimating fair value, the Company utilizes valuation techniques that are consistent with the market approach, the income approach and/or the cost approach. Such valuation techniques are consistently applied. Inputs to valuation techniques include the assumptions that market participants would use in pricing an asset or liability. The three levels of inputs that may be used to measure fair values are as follows:

- *Level 1 Inputs* - Unadjusted quoted prices in active markets for identical assets or liabilities.
- *Level 2 Inputs* - Inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. These might include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability (such as interest rates, volatilities, market consensus, prepayment speeds, credit risks, etc.) or inputs that are derived principally from or corroborated by market data by correlation or other means.
- *Level 3 Inputs* - Unobservable inputs for determining the fair values of assets or liabilities that reflect an entity's own assumptions that market participants would use in pricing the assets or liabilities.

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 12 – FAIR VALUE MEASUREMENT, (CONTINUED)**

Transfers between levels of the fair value hierarchy are recognized on the actual date of the event or circumstances that caused the transfer, which generally coincides with the Company's monthly and/or quarterly valuation process. There were no transfers between levels during 2022 or 2021.

**Recurring Measurements**

The following table summarizes financial assets measured at fair value on a recurring basis by the level within the fair value hierarchy utilized to measure fair value:

|                                                                | Recurring fair value measurements at<br>December 31, 2022 |         |            |          |
|----------------------------------------------------------------|-----------------------------------------------------------|---------|------------|----------|
|                                                                | Total carrying<br>value                                   | Level 1 | Level 2    | Level 3  |
|                                                                | (dollars in thousands)                                    |         |            |          |
| <b>Assets</b>                                                  |                                                           |         |            |          |
| Available-for-sale investment securities:                      |                                                           |         |            |          |
| U.S. treasuries securities                                     | \$ 69,685                                                 | \$ -    | \$ 69,685  | \$ -     |
| U.S. government sponsored agencies                             | 229,021                                                   | -       | 229,021    | -        |
| U.S. government sponsored agency<br>mortgage-backed securities | 383,060                                                   | -       | 383,060    | -        |
| State and political subdivision                                | 113,199                                                   | -       | 113,199    | -        |
| Corporate bonds                                                | 15,626                                                    | -       | 15,626     | -        |
| Equity securities                                              | 2,505                                                     | -       | -          | 2,505    |
| Total assets at fair value                                     | \$ 813,096                                                | \$ -    | \$ 810,591 | \$ 2,505 |

|                                                                | Recurring fair value measurements at<br>December 31, 2021 |         |            |          |
|----------------------------------------------------------------|-----------------------------------------------------------|---------|------------|----------|
|                                                                | Total carrying<br>value                                   | Level 1 | Level 2    | Level 3  |
|                                                                | (dollars in thousands)                                    |         |            |          |
| <b>Assets</b>                                                  |                                                           |         |            |          |
| Available-for-sale investment securities:                      |                                                           |         |            |          |
| U.S. treasuries securities                                     | \$ 17,853                                                 | \$ -    | \$ 17,853  | \$ -     |
| U.S. government sponsored agencies                             | 261,402                                                   |         | 261,402    |          |
| U.S. government sponsored agency<br>mortgage-backed securities | 446,720                                                   | -       | 446,720    | -        |
| State and political subdivision                                | 134,048                                                   | -       | 134,048    | -        |
| Corporate bonds                                                | 16,964                                                    | -       | 16,964     | -        |
| Equity securities                                              | 2,481                                                     | -       | -          | 2,481    |
| Total assets at fair value                                     | \$ 879,468                                                | \$ -    | \$ 876,987 | \$ 2,481 |

The following is a description of the valuation methodologies and inputs used for assets measured at fair value on a recurring basis and recognized in the accompanying balance sheets, as well as the general classification of such assets pursuant to the valuation hierarchy. There have been no significant changes in the valuation techniques during the year ended December 31, 2022.

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 12 – FAIR VALUE MEASUREMENT, (CONTINUED)**

**Available-for-Sale Securities**

Where quoted market prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. If quoted market prices are not available, the Company obtains fair value measurements from an independent pricing service, such as ICE Data Pricing & Reference Data, LLC, which utilizes pricing models to determine fair value measurement. The Company reviews the pricing quarterly to verify the reasonableness of the pricing. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information and the bond's terms and conditions, among other factors. U.S. government agencies, state and political subdivisions, U.S. government sponsored agency mortgage-backed securities and corporate bonds are classified as Level 2 inputs.

**Equity Securities**

Equity securities held by the Company are common shares in a private company. The common shares held are not freely tradeable on any market exchange. The investment is held at fair value on the consolidated balance sheets. An annual appraisal is conducted as of each calendar year and communicated to shareholders. Upon receipt of the annual appraisal, the investment is adjusted to fair value with changes in fair value recognized in income.

**Nonrecurring Measurements**

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

| <b>December 31, 2022</b>              | <b>Level 1</b>         | <b>Level 2</b> | <b>Level 3</b> | <b>Total</b> |
|---------------------------------------|------------------------|----------------|----------------|--------------|
|                                       | (dollars in thousands) |                |                |              |
| Impaired loans (collateral-dependent) | \$ -                   | \$ -           | \$ 135         | \$ 135       |
| <b>December 31, 2021</b>              | <b>Level 1</b>         | <b>Level 2</b> | <b>Level 3</b> | <b>Total</b> |
|                                       | (dollars in thousands) |                |                |              |
| Impaired loans (collateral-dependent) | \$ -                   | \$ -           | \$ 325         | \$ 325       |

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 12 – FAIR VALUE MEASUREMENT, (CONTINUED)**

**Impaired Loans (Collateral-Dependent)**

The estimated fair value of collateral-dependent impaired loans is based on the appraised fair value of the collateral, less estimated cost to sell. Collateral-dependent impaired loans are classified within Level 3 of the fair value hierarchy.

The Company considers the appraisal or evaluation as the starting point for determining fair value and then considers other factors and events in the environment that may affect the fair value. Appraisals of the collateral underlying collateral-dependent loans are obtained when the loan is determined to be collateral-dependent and subsequently as deemed necessary by management. Appraisals are reviewed for accuracy and consistency by management. Appraisers are selected from the list of approved appraisers maintained by management. The appraised values are reduced by discounts to consider estimated cost to sell if repayment or satisfaction of the loan is dependent on the sale of the collateral. These discounts and estimates are developed by management by comparison to historical results. There were fair value adjustments of \$65,000 and \$104,000 at December 31, 2022 and 2021, respectively.

Loans considered impaired under ASC 310-35, “Impairment of a Loan,” are loans for which, based on current information and events, it is probable that the creditor will be unable to collect all amounts due according to the contractual terms of the loan agreement. Impaired loans are subject to nonrecurring fair value adjustments to reflect (1) subsequent partial write-downs that are based on the observable market price or current appraised value of the collateral or (2) the full charge-off of the loan carrying value.

**Unobservable (Level 3) Inputs**

The following table presents quantitative information about unobservable inputs used in nonrecurring Level 3 fair value measurements:

| Quantitative information about Level 3 fair value measurements |            |                              |                        |                          |
|----------------------------------------------------------------|------------|------------------------------|------------------------|--------------------------|
|                                                                | Fair value | Valuation technique(s)       | Unobservable input     | Range (weighted average) |
| December 31, 2022                                              |            | (dollars in thousands)       |                        |                          |
| Impaired loans (collateral-dependent)                          | \$ 135     | Market comparable properties | Marketability discount | 10.0% (10.0%)            |
| Quantitative Information about Level 3 fair value measurements |            |                              |                        |                          |
|                                                                | Fair value | Valuation technique(s)       | Unobservable input     | Range (weighted average) |
| December 31, 2021                                              |            | (dollars in thousands)       |                        |                          |
| Impaired loans (collateral-dependent)                          | \$ 325     | Market comparable properties | Marketability discount | 10.0% (10.0%)            |

ASC Topic 825, “Financial Instruments,” requires disclosure of the fair value of financial assets and liabilities, including those financial assets and liabilities that are not measured and reported at fair value on a recurring basis or non-recurring basis.

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 12 – FAIR VALUE MEASUREMENT, (CONTINUED)**

The following tables present the assets and liabilities that are measured at fair value on a non-recurring basis by level within the fair value hierarchy as reported on the consolidated statements of financial position:

**Fair value measurements at December 31, 2022**

|                                                          | Carrying<br>amount     | Quoted prices<br>in active<br>markets for<br>identical assets<br>(Level 1) | Significant<br>other<br>observable<br>inputs<br>(Level 2) | Significant<br>unobservable<br>inputs (Level 3) |
|----------------------------------------------------------|------------------------|----------------------------------------------------------------------------|-----------------------------------------------------------|-------------------------------------------------|
|                                                          | (dollars in thousands) |                                                                            |                                                           |                                                 |
| Financial assets                                         |                        |                                                                            |                                                           |                                                 |
| Cash and due from banks                                  | \$ 27,193              | \$ 27,193                                                                  | \$ -                                                      | -                                               |
| Interest-bearing deposits in other banks                 | 1,754                  | 1,754                                                                      | -                                                         | -                                               |
| Federal funds sold                                       | 57                     | 57                                                                         | -                                                         | -                                               |
| Securities available-for-sale                            | 810,591                | -                                                                          | 810,591                                                   | -                                               |
| Securities held-to-maturity                              | 15,087                 | -                                                                          | 14,162                                                    | -                                               |
| Equity securities                                        | 2,505                  | -                                                                          | -                                                         | 2,505                                           |
| Loans, net                                               | 966,167                | -                                                                          | -                                                         | 900,167                                         |
| Federal Home Loan Bank and Federal Reserve Bank<br>stock | 6,092                  | -                                                                          | 6,092                                                     | -                                               |
| Accrued interest receivable                              | 5,943                  | -                                                                          | 5,943                                                     | -                                               |
| Financial liabilities                                    |                        |                                                                            |                                                           |                                                 |
| Non-interest bearing deposits                            | 534,474                | 534,474                                                                    | -                                                         | -                                               |
| Interest-bearing deposits                                | 1,264,154              | -                                                                          | 1,120,882                                                 | -                                               |
| Accrued interest payable                                 | 407                    | -                                                                          | 407                                                       | -                                               |
| Off-balance sheet credit related instruments:            |                        |                                                                            |                                                           |                                                 |
| Commitments to extend credit and letters of credit       | -                      | -                                                                          | -                                                         | -                                               |

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 12 – FAIR VALUE MEASUREMENT, (CONTINUED)**

**Fair value measurements at December 31, 2021**

|                                                          | <b>Carrying<br/>amount</b> | <b>Quoted prices<br/>in active<br/>markets for<br/>identical assets<br/>(Level 1)</b> | <b>Significant<br/>other<br/>observable<br/>inputs<br/>(Level 2)</b> | <b>Significant<br/>unobservable<br/>inputs (Level 3)</b> |
|----------------------------------------------------------|----------------------------|---------------------------------------------------------------------------------------|----------------------------------------------------------------------|----------------------------------------------------------|
|                                                          | (dollars in thousands)     |                                                                                       |                                                                      |                                                          |
| Financial assets                                         |                            |                                                                                       |                                                                      |                                                          |
| Cash and due from banks                                  | \$ 19,791                  | \$ 19,791                                                                             | \$ -                                                                 | -                                                        |
| Interest-bearing deposits in other banks                 | 75,065                     | 75,065                                                                                | -                                                                    | -                                                        |
| Federal funds sold                                       | 8,374                      | 8,374                                                                                 | -                                                                    | -                                                        |
| Securities available-for-sale                            | 876,987                    | -                                                                                     | 876,987                                                              | -                                                        |
| Securities held-to-maturity                              | 15,128                     | -                                                                                     | 15,932                                                               | -                                                        |
| Equity securities                                        | 2,481                      | -                                                                                     | -                                                                    | 2,481                                                    |
| Loans held-for-sale                                      | 2,197                      | -                                                                                     | 2,197                                                                | -                                                        |
| Loans, net                                               | 886,891                    | -                                                                                     | -                                                                    | 882,508                                                  |
| Federal Home Loan Bank and Federal Reserve Bank<br>stock | 4,149                      | -                                                                                     | 4,149                                                                | -                                                        |
| Accrued interest receivable                              | 5,228                      | -                                                                                     | 5,228                                                                | -                                                        |
| Financial liabilities                                    |                            |                                                                                       |                                                                      |                                                          |
| Non-interest bearing deposits                            | 522,725                    | 522,725                                                                               | -                                                                    | -                                                        |
| Interest-bearing deposits                                | 1,268,481                  | -                                                                                     | 985,505                                                              | -                                                        |
| Accrued interest payable                                 | 528                        | -                                                                                     | 528                                                                  | -                                                        |
| Off-balance sheet credit related instruments:            |                            |                                                                                       |                                                                      |                                                          |
| Commitments to extend credit and letters of credit       | -                          | -                                                                                     | -                                                                    | -                                                        |

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 13 – QUARTERLY RESULTS OF OPERATIONS (Unaudited)**

The following tables present unaudited quarterly interim financial information for the Company for the periods presented:

|                                                                                    | <b>March 31,<br/>2022</b> | <b>June 30,<br/>2022</b> | <b>September 30,<br/>2022</b> | <b>December 31,<br/>2022</b> | <b>Total</b> |
|------------------------------------------------------------------------------------|---------------------------|--------------------------|-------------------------------|------------------------------|--------------|
|                                                                                    |                           |                          | (dollars in thousands)        |                              |              |
| Interest income                                                                    | \$ 11,490                 | \$ 12,198                | 13,279                        | \$ 14,256                    | \$ 51,223    |
| Interest expense                                                                   | 372                       | 505                      | 810                           | 1,552                        | 3,239        |
| Net interest income                                                                | 11,118                    | 11,693                   | 12,469                        | 12,704                       | 47,984       |
| Provision credit for loan and lease losses                                         | (320)                     | -                        | -                             | -                            | (320)        |
| Non-interest income                                                                | 3,466                     | 3,660                    | 3,526                         | 3,495                        | 14,147       |
| Non-interest expenses and non-controlling interest – preferred stock of subsidiary | 10,425                    | 9,763                    | 10,076                        | 9,920                        | 40,184       |
| Income before provision for income taxes                                           | 4,479                     | 5,590                    | 5,919                         | 6,279                        | 22,267       |
| Provision for income taxes                                                         | 797                       | 1,052                    | 1,116                         | 1,252                        | 4,217        |
| Net income available to common shareholders                                        | \$ 3,682                  | 4,538                    | \$ 4,803                      | 5,027                        | 18,050       |
| Basic earnings per share                                                           | \$ 0.85                   | \$ 1.05                  | \$ 1.12                       | \$ 1.17                      | \$ 4.19      |
| Weighted average shares outstanding                                                | 4,317,169                 | 4,313,455                | 4,301,056                     | 4,290,886                    | 4,305,557    |

|                                                                                    | <b>March 31,<br/>2021</b> | <b>June 30,<br/>2021</b> | <b>September 30,<br/>2021</b> | <b>December 31,<br/>2021</b> | <b>Total</b> |
|------------------------------------------------------------------------------------|---------------------------|--------------------------|-------------------------------|------------------------------|--------------|
|                                                                                    |                           |                          | (dollars in thousands)        |                              |              |
| Interest income                                                                    | \$ 11,371                 | \$ 11,872                | \$ 12,143                     | \$ 12,151                    | \$ 47,537    |
| Interest expense                                                                   | 778                       | 686                      | 517                           | 400                          | 2,381        |
| Net interest income                                                                | 10,593                    | 11,186                   | 11,626                        | 11,751                       | 45,156       |
| Provision credit for loan and lease losses                                         | (150)                     | -                        | -                             | -                            | (150)        |
| Non-interest income                                                                | 3,550                     | 5,658                    | 3,712                         | 3,863                        | 16,783       |
| Non-interest expenses and non-controlling interest – preferred stock of subsidiary | 10,690                    | 9,933                    | 10,398                        | 11,961                       | 42,982       |
| Income before provision for income taxes                                           | 3,603                     | 6,911                    | 4,940                         | 3,653                        | 19,107       |
| Provision for income taxes                                                         | 600                       | 1,435                    | 871                           | 582                          | 3,488        |
| Net income available to common shareholders                                        | \$ 3,003                  | \$ 5,476                 | \$ 4,069                      | \$ 3,071                     | \$ 15,619    |
| Basic earnings per share                                                           | \$ 0.69                   | \$ 1.26                  | \$ 0.94                       | \$ 0.71                      | \$ 3.59      |
| Weighted average shares outstanding                                                | 4,359,405                 | 4,357,546                | 4,340,048                     | 4,326,090                    | 4,345,665    |

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 14 – DEPOSITS**

The Bank does not have any foreign offices and all deposits are serviced in its 22 domestic offices. Maturities of time deposits more than \$250,000 at December 31, 2022 and 2021 are as follows:

|                | <u>2022</u>            | <u>2021</u>      |
|----------------|------------------------|------------------|
|                | (dollars in thousands) |                  |
| Under 3 months | \$ 3,900               | \$ 7,998         |
| 3 to 12 months | 9,680                  | 11,212           |
| Over 12 months | <u>4,521</u>           | <u>7,132</u>     |
| Total          | <u>\$ 18,101</u>       | <u>\$ 26,342</u> |

At December 31, 2022 and 2021, the Bank had \$318,000 and \$323,000, respectively, of deposit accounts in overdraft status and thus have been reclassified to loans in the accompanying consolidated balance sheets.

The following table presents maturities of interest-bearing time deposits as of December 31, 2022:

|  |                        |                   |
|--|------------------------|-------------------|
|  | (dollars in thousands) |                   |
|  | 2023                   | \$ 105,654        |
|  | 2024                   | 16,958            |
|  | 2025                   | 5,901             |
|  | 2026                   | 4,315             |
|  | 2027 and thereafter    | <u>6,046</u>      |
|  | Total                  | <u>\$ 138,874</u> |

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 15 – CONDENSED FINANCIAL INFORMATION OF THE PARENT COMPANY**

The following tables present the condensed balance sheet, statements of income, and cash flows of the Parent Company:

**CONDENSED BALANCE SHEET**

|                                                                                                                                                     | <b>As of December 31,</b> |                   |
|-----------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------|-------------------|
|                                                                                                                                                     | <b>2022</b>               | <b>2021</b>       |
|                                                                                                                                                     | (dollars in thousands)    |                   |
| Cash                                                                                                                                                | \$ 3                      | \$ 85             |
| Investment in bank subsidiary                                                                                                                       | 96,604                    | 158,441           |
| Investment in credit life insurance company                                                                                                         | 54                        | 54                |
| Dividends receivable from bank subsidiary                                                                                                           | 983                       | 907               |
| Equity securities                                                                                                                                   | 2,505                     | 2,481             |
| Other assets                                                                                                                                        | -                         | 7                 |
| Total assets                                                                                                                                        | <u>\$ 100,149</u>         | <u>\$ 161,975</u> |
| Liabilities                                                                                                                                         |                           |                   |
| Accrued liabilities                                                                                                                                 | \$ 2,596                  | \$ 2,532          |
| Due to bank subsidiary                                                                                                                              | -                         | -                 |
| Dividends payable                                                                                                                                   | 983                       | 907               |
| Total liabilities                                                                                                                                   | <u>3,579</u>              | <u>3,439</u>      |
| Shareholders' equity                                                                                                                                |                           |                   |
| Common stock - \$10 par value, 8,000,000 shares authorized;<br>4,275,328 and 4,317,306 shares issued and outstanding as of<br>the periods presented | 42,753                    | 43,173            |
| Retained earnings                                                                                                                                   | 132,905                   | 119,507           |
| Accumulated other comprehensive loss                                                                                                                | <u>(79,088)</u>           | <u>(4,144)</u>    |
| Total shareholders' equity                                                                                                                          | <u>96,570</u>             | <u>158,536</u>    |
| Total liabilities and shareholders' equity                                                                                                          | <u>\$ 100,149</u>         | <u>\$ 161,975</u> |

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 15 – CONDENSED FINANCIAL INFORMATION OF THE PARENT COMPANY, (CONTINUED)**

**CONDENSED STATEMENTS OF INCOME**

|                                                                          | <b>Years ended December 31,</b> |                        |             |
|--------------------------------------------------------------------------|---------------------------------|------------------------|-------------|
|                                                                          | <b>2022</b>                     | <b>2021</b>            | <b>2020</b> |
| Operating income                                                         |                                 | (dollars in thousands) |             |
| Dividends from bank subsidiary                                           | \$ 5,340                        | \$ 5,647               | \$ 4,582    |
| Other                                                                    | 25                              | 239                    | 242         |
| Operating expenses                                                       | (418)                           | (464)                  | (463)       |
| Income before equity in undistributed net<br>income of bank subsidiary   | 4,947                           | 5,422                  | 4,361       |
| Equity in undistributed net income of bank subsidiary                    | 13,119                          | 10,213                 | 9,849       |
| Net income                                                               | \$ 18,066                       | \$ 15,635              | \$ 14,210   |
| Non-controlling interest – dividends on preferred stock<br>of subsidiary | (16)                            | (16)                   | (16)        |
| Net income available to common shareholders                              | \$ 18,050                       | \$ 15,619              | \$ 14,194   |

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 15 – CONDENSED FINANCIAL INFORMATION OF THE PARENT COMPANY, (CONTINUED)**

**CONDENSED STATEMENTS OF CASH FLOWS**

|                                                                                  | Years ended December 31, |              |               |
|----------------------------------------------------------------------------------|--------------------------|--------------|---------------|
|                                                                                  | 2022                     | 2021         | 2020          |
|                                                                                  | (dollars in thousands)   |              |               |
| Operating activities                                                             |                          |              |               |
| Net income                                                                       | \$ 18,066                | \$ 15,635    | \$ 14,210     |
| Adjustments to reconcile net income to net cash provided by operating activities |                          |              |               |
| Equity in undistributed net income of bank subsidiary                            | (13,119)                 | (10,213)     | (9,849)       |
| Gain on equity securities                                                        | (25)                     | (239)        | (242)         |
| (Increase) decrease in other assets                                              | (56)                     | 9            | 4             |
| Increase (decrease) in payables                                                  | 64                       | (89)         | 227           |
| Total adjustments                                                                | (13,136)                 | (10,532)     | (9,860)       |
| Net cash provided by operating activities                                        | 4,930                    | 5,103        | 4,350         |
| Investing activities                                                             |                          |              |               |
| Purchase of equity securities                                                    | -                        | -            | -             |
| Net cash used in investing activities                                            | -                        | -            | -             |
| Financing activities                                                             |                          |              |               |
| Payment to repurchase common stock                                               | (1,290)                  | (1,653)      | (918)         |
| Common stock dividends paid                                                      | (3,706)                  | (3,653)      | (3,666)       |
| Preferred stock of subsidiary dividends paid                                     | (16)                     | (16)         | (16)          |
| Net cash used in financing activities                                            | (5,012)                  | (5,322)      | (4,600)       |
| Decrease in cash                                                                 | (82)                     | (219)        | (250)         |
| Cash at beginning of year                                                        | 85                       | 304          | 554           |
| Cash at end of year                                                              | <u>\$ 3</u>              | <u>\$ 85</u> | <u>\$ 304</u> |

**NOTE 16 – EMPLOYEE BENEFIT PLANS**

The Bank contributes to a qualified profit-sharing plan covering employees who meet participation requirements. To be eligible to participate, employees must complete 1,000 hours of service within the twelve-month time period following their date of hire. Employees must be age 20 or older. The amount of the contribution is at the discretion of the Bank's Board of Directors, up to the maximum deduction allowed for federal income tax purposes. Contributions to the plan, which amounted to \$1.3 million, \$1.4 million, and \$1.1 million in 2022, 2021 and 2020, respectively, are included in salaries and employee benefits expense.

The Bank has SERP agreements for certain key officers, and the principal cost of these agreements is accrued over the anticipated remaining period of active employment, based on the present value of the expected retirement benefit. At December 31, 2022 and 2021, the related liability totaled \$3.4 million and was included in other liabilities. The prior year liability includes a one-time adjustment of \$1.5 million for a SERP agreement formalized on December 10, 2021 which enhanced the previous agreement executed on November 15, 2016 for one key officer.

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 16 – EMPLOYEE BENEFIT PLANS, (CONTINUED)**

The Company and the Bank have deferred compensation plans that permit directors to defer their director's fees and earn interest on the deferred amount at the wall street journal prime rate plus three percent. The agreements provide for a lump sum payment or 120 monthly payments of deferred fees plus accrued interest after retirement, separation from service, or death. At December 31, 2022 and 2021, the liability accrued for this plan totaled \$7.5 million. The charge to expense for the agreements was \$1.0 million for the years ended December 31, 2022, 2021 and 2020.

**NOTE 17 – POST-RETIREMENT BENEFIT PLAN**

Effective July 1, 2013, the Company revised its retiree medical benefit plan for employees who were hired before March 20, 2007. Newly retiring employees will no longer be offered medical, dental or life insurance coverage. Instead, qualified retirees will receive a post-retirement bonus. The Company will pay a post-retirement bonus equal to \$20,000 to employees who: (i) were hired prior to March 20, 2007; (ii) retire on or after July 1, 2013; (iii) are at least age 59 ½ at the time of retirement; and (iv) have at least 25 years of service to the Company as of retirement. The bonus will be paid in a lump sum cash payment (subject to applicable tax withholding requirements) within 60 days after the employee's retirement, provided such retirement constitutes a "separation from service" under section 409A of the Internal Revenue Code. The Company still sponsors a defined benefit post-retirement health care plan for retirees who retired prior to July 1, 2007. Under this plan, premiums paid by retirees and spouses depend on date of retirement, age and coverage election.

The Company funding policy is to make the minimal annual contribution that is required by applicable regulations, plus such amounts as the Company may determine to be appropriate from time to time. The Company expects to contribute \$188,000 to the plan in 2023.

The following table provides further information about the plan:

|                                                                    | <b>Post-retirement benefits</b> |                   |
|--------------------------------------------------------------------|---------------------------------|-------------------|
|                                                                    | <b>2022</b>                     | <b>2021</b>       |
|                                                                    | (dollars in thousands)          |                   |
| <b>Change in benefit obligation</b>                                |                                 |                   |
| Benefit obligation at beginning of year                            | \$ 1,835                        | \$ 2,020          |
| Service cost                                                       | 23                              | 26                |
| Interest cost                                                      | 50                              | 52                |
| Expected benefits paid                                             | (174)                           | (172)             |
| Actuarial gain                                                     | (224)                           | (91)              |
| Benefit obligation at end of year                                  | <u>\$ 1,510</u>                 | <u>\$ 1,835</u>   |
| <b>Change in fair value of assets</b>                              |                                 |                   |
| Fair value of plans assets at beginning of year                    | \$ -                            | \$ -              |
| Employer contribution                                              | 174                             | 173               |
| Benefits paid                                                      | (174)                           | (173)             |
| Fair value of plan assets at end of year                           | <u>\$ -</u>                     | <u>\$ -</u>       |
| <b>Reconciliation of funded status to benefit costs recognized</b> |                                 |                   |
| Projected benefit obligation, end of year                          | \$ (1,510)                      | \$ (1,835)        |
| Fair value of assets, end of year                                  | -                               | -                 |
| Funded status, end of year                                         | <u>\$ (1,510)</u>               | <u>\$ (1,835)</u> |

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 17 – POST-RETIREMENT BENEFIT PLAN, (CONTINUED)**

Amounts recognized in accumulated other comprehensive income not yet recognized as components of net periodic benefit cost consist of:

|                                 | <u>2022</u>            | <u>2021</u>       |
|---------------------------------|------------------------|-------------------|
|                                 | (dollars in thousands) |                   |
| Unrecognized net actuarial gain | \$ (1,320)             | \$ (1,248)        |
| Unrecognized prior service cost | (5)                    | (10)              |
|                                 | <u>\$ (1,325)</u>      | <u>\$ (1,258)</u> |

Amounts recognized in statement of financial position are as follows:

|                                          | <u>2022</u>            | <u>2021</u> |
|------------------------------------------|------------------------|-------------|
|                                          | (dollars in thousands) |             |
| Accounts payable and accrued liabilities | \$ 1,510               | \$ 1,835    |

A reconciliation of other comprehensive loss is as follows:

|                                                        | <u>2022</u>            | <u>2021</u>       |
|--------------------------------------------------------|------------------------|-------------------|
|                                                        | (dollars in thousands) |                   |
| Accumulated other comprehensive loss beginning of year | \$ (1,258)             | \$ (1,308)        |
| Amortization of net actuarial gain                     | 152                    | 136               |
| Gain incurred in current year                          | (224)                  | (91)              |
| Prior service cost established in current year         | 5                      | 5                 |
| Other comprehensive income                             | (67)                   | 50                |
| Ending balance (before tax effects)                    | <u>\$ (1,325)</u>      | <u>\$ (1,258)</u> |

|                                         | <u>2022</u>            | <u>2021</u>    |
|-----------------------------------------|------------------------|----------------|
|                                         | (dollars in thousands) |                |
| Components of net periodic benefit cost |                        |                |
| Service cost                            | \$ 23                  | \$ 26          |
| Interest cost                           | 50                     | 52             |
| Amortization of prior service cost      | (5)                    | (5)            |
| Recognized net actuarial gain           | (152)                  | (136)          |
| Net periodic benefit cost               | <u>\$ (84)</u>         | <u>\$ (63)</u> |

The components of net periodic benefit cost other than the service cost component are included in other non-interest expense in the consolidated income statement. The estimated net gain for the defined benefits post-retirement plan that will be amortized from accumulated other comprehensive income into net periodic benefit cost over the next fiscal year is \$167,000.

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 17 – POST-RETIREMENT BENEFIT PLAN, (CONTINUED)**

|                                                                   | <b>Post-retirement benefits</b> |             |
|-------------------------------------------------------------------|---------------------------------|-------------|
|                                                                   | <b>2022</b>                     | <b>2021</b> |
| Weighted-average assumption used to determine benefit obligation: |                                 |             |
| Discount rate                                                     | 5.15%                           | 2.85%       |
| Rate of compensation increase                                     | NA                              | NA          |
|                                                                   | <b>Post-retirement benefits</b> |             |
|                                                                   | <b>2022</b>                     | <b>2021</b> |
| Weighted-average assumptions used to determine benefit costs:     |                                 |             |
| Discount rate                                                     | 5.15%                           | 2.85%       |

The following table gives the health care cost trend, which is applied to gross charges, net claims and retiree paid premiums to reflect the Company's past practice and stated ongoing intention to maintain relatively constant cost sharing between the Company and retirees:

|                            | <b>2022</b> | <b>2021</b> |
|----------------------------|-------------|-------------|
| Health care trend rate     |             |             |
| Initial                    |             |             |
| Pre-65                     | 7.50%       | 8.00%       |
| Post-65                    | 6.50%       | 8.00%       |
| Ultimate (pre and post-65) | 4.50%       | 4.50%       |
| Years to ultimate          |             |             |
| Pre-65                     | 6           | 7           |
| Post-65                    | 7           | 7           |

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid, net of participant contributions:

| <b>FYE</b> | <b>Company benefits</b> |
|------------|-------------------------|
|            | (dollars in thousands)  |
| 2023       | \$ 188                  |
| 2024       | 179                     |
| 2025       | 162                     |
| 2026       | 182                     |
| 2027       | 170                     |
| 2028-2032  | <u>657</u>              |
|            | <u><u>\$ 1,538</u></u>  |

**NOTE 18 – REGULATORY CAPITAL**

The Company and Bank are subject to various regulatory capital requirements administered by federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory, and possibly additional discretionary actions, by regulators that, if undertaken, could have a direct material effect on the financial statements.

In May of 2018, the Economic Growth, Regulatory Relief, and Consumer Protection Act was signed into law. The new law makes a variety of changes aimed to simplify regulatory reporting requirements on community banks and scale down requirements previously required by Dodd-Frank Act. The new law contains a Small Bank Holding Company Policy statement which provides a capital requirement exemption for holding companies with total consolidated assets under \$3 billion. The Company, which was previously subject to similar regulatory capital requirements as the Bank, is now subject to the Federal Reserve's "Small Bank Holding Company and Savings and Loan Policy Statement." As such, the Company is no longer subject to certain capital adequacy guidelines and regulatory reporting.

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 18 – REGULATORY CAPITAL, (CONTINUED)**

To be considered well capitalized under applicable banking regulations, the Bank must maintain the following minimum capital ratios and not be subject to a written agreement, order or directive to maintain a higher capital level:

- (1) a common equity Tier 1 capital ratio of 6.5%;
- (2) a Tier 1 risk based capital ratio of 8%;
- (3) a Total risk based capital ratio of 10%; and
- (4) a Tier 1 leverage ratio of 5%.

Under capital level requirements, common equity Tier 1 capital generally consists of common stock (plus related surplus) and retained earnings plus limited amounts of minority interest in the form of common stock, less goodwill and other specified intangible assets and other regulatory deductions. Tier 1 capital generally consists of common stock (plus related surplus) and retained earnings, limited amounts of minority interest in the form of additional Tier 1 capital instruments, and non-cumulative preferred stock and related surplus, subject to certain eligibility standards, less goodwill and other specified intangible assets and other regulatory deductions. Tier 2 capital generally consists of subordinated debt (including that portion of subordinated debentures associated with trust preferred securities in excess of the amount that is treated as Tier 1 capital), types of preferred stock that don't qualify as Tier 1 capital and a limited amount of loan loss reserves, subject to certain eligibility criteria.

The current capital level requirements allow banks and their holding companies with less than \$250 billion in assets a one-time opportunity to opt out of a requirement to include unrealized gains and losses in accumulated other comprehensive income in their capital calculation. The Bank has opted out of this requirement.

Actual capital amounts and ratios are presented in the table below. Management believes, as of December 31, 2022, that the Bank met the guidelines to which they were subject.

| (Dollars in thousands)<br>As of December 31, 2022 | Actual     |       | Minimum<br>capital requirement |       | Minimum to be<br>well capitalized |       |
|---------------------------------------------------|------------|-------|--------------------------------|-------|-----------------------------------|-------|
|                                                   | Amount     | Ratio | Amount                         | Ratio | Amount                            | Ratio |
| Common equity Tier 1 (to risk weighted assets)    | \$ 166,675 | 14.6% | \$ 51,335                      | 4.5%  | \$ 74,151                         | 6.5%  |
| Total capital (to risk weighted assets)           | 176,057    | 15.4% | 91,263                         | 8.0%  | 114,079                           | 10.0% |
| Tier 1 capital (to risk weighted assets)          | 166,675    | 14.6% | 68,447                         | 6.0%  | 91,263                            | 8.0%  |
| Tier 1 capital (to average assets)                | 166,675    | 8.1%  | 82,103                         | 4.0%  | 102,629                           | 5.0%  |

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 18 – REGULATORY CAPITAL, (CONTINUED)**

| (Dollars in thousands)<br>As of December 31, 2021 | Actual     |       | Minimum<br>capital requirement |       | Minimum to be<br>well capitalized |       |
|---------------------------------------------------|------------|-------|--------------------------------|-------|-----------------------------------|-------|
|                                                   | Amount     | Ratio | Amount                         | Ratio | Amount                            | Ratio |
| Common equity Tier 1 (to risk weighted assets)    | \$ 153,568 | 14.3% | \$ 48,198                      | 4.5%  | \$ 69,619                         | 6.5%  |
| Total capital (to risk weighted assets)           | 163,173    | 15.2% | 85,685                         | 8.0%  | 107,107                           | 10.0% |
| Tier 1 capital (to risk weighted assets)          | 153,568    | 14.3% | 64,264                         | 6.0%  | 85,685                            | 8.0%  |
| Tier 1 capital (to average assets)                | 153,568    | 8.0%  | 76,815                         | 4.0%  | 96,019                            | 5.0%  |

The Bank is subject to certain restrictions on the amount of dividends that it may declare without prior regulatory approval. At December 31, 2022, approximately \$13.0 million of retained earnings were available for dividend declaration without prior approval.

**NOTE 19 – REVENUE FROM CONTRACTS WITH CUSTOMERS**

All of the Company's revenue from contracts with customers in the scope of ASC 606 is recognized within non-interest income. The following table presents the Company's sources of non-interest income for the periods presented. Items outside the scope of ASC Topic 606 are noted as such.

|                                                                | Years ended December 31, |                  |                  |
|----------------------------------------------------------------|--------------------------|------------------|------------------|
|                                                                | 2022                     | 2021             | 2020             |
|                                                                | (dollars in thousands)   |                  |                  |
| Mortgage banking activities <sup>(1)</sup>                     | \$ 614                   | \$ 1,442         | \$ 1,362         |
| Trust service fees income                                      | 4,160                    | 4,045            | 3,643            |
| Service fees on deposit accounts:                              |                          |                  |                  |
| Overdraft fees                                                 | 1,838                    | 1,508            | 1,585            |
| Interchange income                                             | 3,315                    | 3,268            | 2,669            |
| Maintenance fees and charges                                   | 1,759                    | 1,535            | 1,645            |
| Other                                                          | 743                      | 782              | 718              |
| Investment service fees income                                 | 406                      | 341              | 371              |
| Earnings on bank-owned life insurance <sup>(1)</sup>           | 475                      | 554              | 551              |
| (Loss) gain on sales of investments <sup>(1)</sup>             | (5)                      | 621              | 129              |
| Gain on redemption of bank-owned life insurance <sup>(1)</sup> | -                        | -                | 820              |
| Gain on equity securities                                      | 25                       | 239              | 242              |
| Gain on sale of Visa class B stock <sup>(1)</sup>              | -                        | 1,811            | -                |
| Other non-interest income                                      | 817                      | 637              | 712              |
| Total non-interest income                                      | <u>\$ 14,147</u>         | <u>\$ 16,783</u> | <u>\$ 14,447</u> |

<sup>(1)</sup> Not within the scope of ASC Topic 606.

**FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 19 – REVENUE FROM CONTRACTS WITH CUSTOMERS, (CONTINUED)**

A description of the Company's revenue streams accounted for under ASC Topic 606 follows:

**Trust service fees** - The Company earns wealth management fees from its contracts with trust customers to manage assets for investment, and/or to transact on their accounts. These fees are primarily earned over time as the Company provides the contracted monthly services and are generally assessed based on a tiered scale of the market value of assets under management at month-end. The fees are recognized monthly when the Company satisfies the performance obligation. Other services provided include third party benefit plan administration and estate management. Fees for third party benefit plan administration are billed quarterly or annually and accrued for over the period the performance obligation of administering the third party plan is being performed. Executor fees earned for estate management are a source of nonrecurring revenue and are recorded upon the satisfaction of the performance obligation, which is determined to be when the estate is closed and/or in some instances when the court has approved the executor's billing to the estate.

**Service fees on deposit accounts** - The Company earns fees on its deposit customers for transaction-based, account maintenance, and overdraft services. Transaction-based fees, which include services such as ATM usage fees, stop payment charges, statement rendering, and ACH fees are recognized at the time the transaction is executed and the Company fulfills the customer's request. Account maintenance fees, which relate primarily to monthly maintenance, are earned over the course of a month, representing the period over which the Company satisfies the performance obligation. Account maintenance fees are recognized in the same month the Company earns and satisfies the performance obligation. Overdraft fees are recognized at the point in time that the overdraft occurs. Service charges on deposits are withdrawn from the customer's account balance.

The Company earns interchange fees from debit cardholder transactions conducted through the Visa payment network. Interchange fees from cardholder transactions represent a percentage of the underlying transaction value and is concurrent with the transaction processing services provided to the cardholder. Revenue activity associated with cardholder transactions is recognized on the business day the Company satisfies the performance obligation. Additionally, the Company is acting as an agent in providing cardholder services to customers, thus costs associated with cardholder transactions is netted against the fee income from such transactions.

**Investment service fees income** - The Company earns fees from investment brokerage services provided to its customers by a third-party service provider. The Company receives commissions from the third-party service provider on a bi-monthly basis based upon customer activity for the month. The fees are recognized monthly when the Company satisfies the performance obligation. Because the Company (1) acts as an agent in arranging the relationship between the customer and third-party service provider and (2) does not control the services rendered to the customer, investment brokerage fees are presented net of related servicing and administration costs.

**NOTE 20 – SUBSEQUENT EVENTS**

The Company evaluated all events or transactions that occurred after December 31, 2022, through March 1, 2023. There were no material recognizable subsequent events that occurred after December 31, 2022 through the date of the independent auditor's report that require recognition or disclosure in the December 31, 2022 consolidated financial statements.