STAR

Bank | Insurance | Private Advisory

2023 ANNUAL REPORT

EST. 1943

80 YEARS

STAR

Chairman's Letter

I am pleased to present STAR Financial Group's Annual Report, highlighting our strong results and journey as one of Indiana's leading community-focused banks in 2023. Our talented workforce was the driving force behind our strong performance, and it is a privilege to witness their unwavering commitment to service, security and stability in all we do.

80 years in business is a milestone worth celebrating, and that is exactly what we did. We reflected on our strong legacy of service, celebrated longstanding relationships with the many organizations, families and individuals we cherish and proudly showcased a special 80th Anniversary emblem throughout 2023, designed especially for this momentous year in business.

Service and philanthropic support remain at the heart of what we care so deeply about, and that is the communities we serve. Further, our investments in optimizing the experience of every interaction you have with us continued, as we again upgraded and expanded new technologies across each line of business. We remain passionate about giving you the personalized service and reliability you expect, while also offering the convenience and flexibility you deserve. Rest assured, there is a never-ending pursuit to continuously improve how, where and when we serve you.

In closing, I would be remiss if I did not share the exciting news we received as wrapped up 2023 and said hello to 2024. STAR Financial Bank was named one of America's Top 250 Regional Banks and Credit Unions by Newsweek. In partnership with market data research firm Plant-A Insights Group, Newsweek identified the best financial institutions in the country who not only stand out for their customer-centric services, but also are using their powerful community-centered approach to redefine the banking experience. It is undoubtedly a tremendous honor and a testament to the type of company our employees have built and continue to grow.

Thank you for your continued trust and partnership.

Sincerely,

THOMAS M. MARCUCCILLI
Chairman, STAR Financial Group, Inc.

Economic Review

At the start of the year, many worried about a recession, wondering if it would be mild like we experienced in July 1990 through March 1991, or more severe like the most recent one we experienced from 2007-2009. Businesses struggled to find and keep employees. The Federal Reserve raised interest rates a total of 3.75%, which further fueled concerns. However, strong consumer spending and low unemployment rates staved off a full-blown recession.

Despite worries, the stock market, especially big tech companies like Apple and Google, had a good year, while some sectors like utilities and consumer staples didn't do as well.

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Line of Business Celebrations

The Private Advisory team met many milestones in 2023, including:

- Hit a high-water mark mid-year in assets under management in the wealth management department and finished the year strong with $465M.
- Had another record year in total revenue generated by advisors in the investment services channel (GDC).
- Hired the first Chief Investment Officer to the wealth management team when Scott Freeman joined the STAR team in January 2024.

The Private Banking team hit record earnings for the 4th consecutive year:

- Balances grew by 18% from EOY 2023 to EOY 2024 in a highly competitive deposit market.
- Realized the benefits of multiple internal talent development strategies that included a successful Associate Private Banker transition from Retail, Healthcare Banker growth from Retail and successful growth of externally placed Private Banking.

The Commercial Banking team had many accomplishments in 2023, including:

- Commercial loan outstandings reached its highest water mark in average outstandings (excluding PPP dollars from 2020) of nearly $1.16B.
- Another year of new money loan production of nearly $500M.
- The continuation of very strong credit metrics, ending the year with 95.4% of loan outstandings being pass grade.

The Small Business team beat their Net Income budget by 85% this year. Other accomplishments include:

- A seamless transition in sales management of the business segment.
- Financial reporting exceptions reduction due to focused cleanup effort.

The Retail branch network had a very promising 2023 with success in several key areas:

- Consumer lenders were responsible for $46M in loan production in 2023, which resulted in over 5% portfolio growth.
- The STAR branch network ushered in a fleet of new enhanced self-service machines to its lobbies at 5 locations in 2023. This will allow customers an alternative experience to working with a live banker, while maintaining the same level of customer satisfaction they have grown to love at STAR.

Community Focus on the Future

STAR continues its commitment to the community it serves throughout its footprint, as evidenced in the investment toward the youth through scholarships and opportunities.

STAR once again offered five college scholarships directed to those whose career path includes agriculture, doubling its initial investment from the inaugural year, increasing each award from $500 to $1,000.

STAR's 2023 Agriculture Scholarship Award Winners

Winners of STAR's annual Kickoff to May Coloring Contest

STAR was proud to partner with The 500 Festival through its "Kickoff to May" event. Hundreds gathered outside of the STAR Bank location on Monument Circle on a beautiful sunny early May afternoon. And there's more... STAR was able to provide a pair of young Hoosiers with a $500 scholarship as a part of our annual coloring contest!

STAR was blessed to be able to grow our stable of interns to 11 in 2023, an increase from eight the previous year, positively impacting our team and providing us with a fresh perspective on banking for a younger generation. Trine University, Indiana Tech, Indiana University, Purdue University, University of Saint Francis, Butler University and Ivy Tech were represented by this impressive group.

STAR Bank 2023 Interns

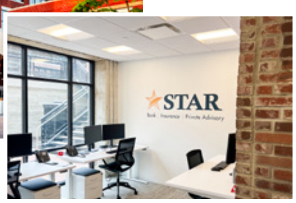
Highlights and Key Initiatives of 2023

The Debut of Orbi

To make banking easier and more convenient for our customers, STAR continued to think outside the bank through upgrades to our enhanced self-service technology and was excited to introduce Orbi. This upgraded technology allows customers to perform a myriad of additional banking services than were previously available including making loan payments, access to more accounts, and more! This gives our customers choices, which allows them to bank their way and be on their way.

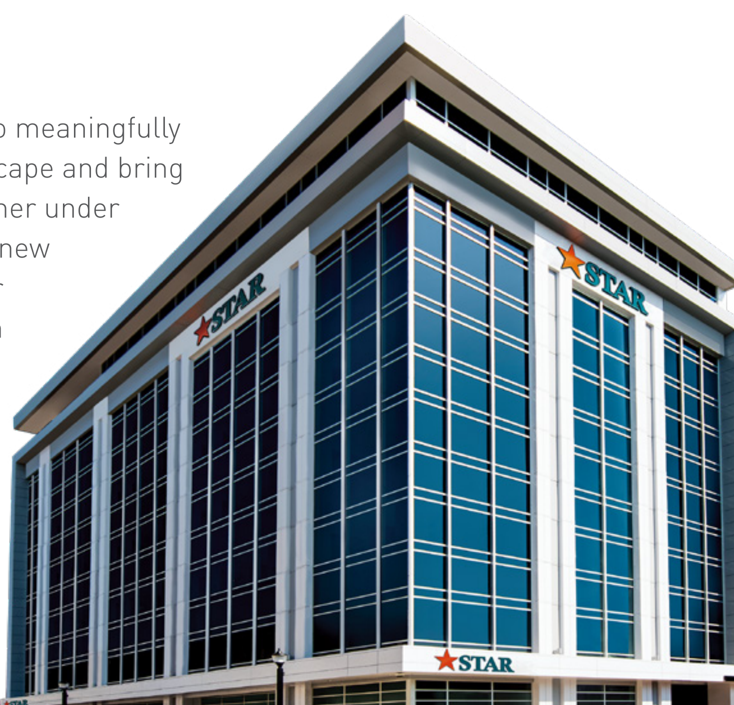
A New Presence at Electric Works

The Electric Works project, a thrilling new multi-purpose endeavor located in Fort Wayne on the former General Electric campus, has flourished in both scope and popularity since its opening in 2022. As proud participants in this venture, STAR secured an office in the co-working space to work alongside the many startups in that space. We also placed two state-of-the-art Orbi machines on the bustling campus. This investment gives us an exceptional platform to showcase our talented team, technology, share exciting updates from our newly-opened HQ less than five minutes away, as well as spotlight our best products and services.



The big move into a new HQ

It was over three years in the making, but our pursuit to meaningfully contribute to the booming downtown Fort Wayne landscape and bring more than 220 of our Fort Wayne team members together under one roof came to fruition. We moved in to the beautiful new space at the end of the year, and this $43-million dollar plus project includes a 7-story 50,000 square feet north tower, a 3-story 20,000 foot south tower and a nearly 400-space adjoining parking garage.



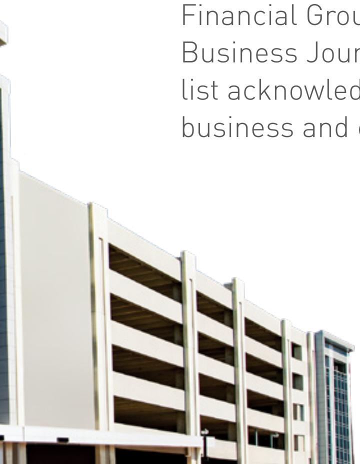
Happy 80th Birthday, STAR!

STAR began a journey in 1943 to become one of Indiana's trusted community banks, celebrating the friends, family and the business that call this Hoosier Heartland home. 2023 marked 80 years in business, and we celebrated it! From a stunning commercial that aired during the Super Bowl, to staff celebrations, print ads, articles and more, STAR was front of mind and center stage for a vast audience.

Celebrating Our STARs

When you have a great business, it usually means it's made up of a great group of people. STAR is no exception as its team members, both past and present, shined in 2023 through notable recognitions from multiple organizations throughout our footprint. So many to list, here are some of the more notable honors:

- Former STAR Bank Anderson President Carl Erskine was honored with the prestigious John Jordan "Buck" O'Neil Lifetime Achievement Award in July during the Hall of Fame Weekend in Cooperstown, New York. As a heartfelt tribute to this esteemed member of the STAR Bank team, we proudly featured an advertisement in the commemorative edition of the Indianapolis Business Journal, released on August 3. Running the same day, we showcased a captivating full-page ad in the Anderson Herald Bulletin, with a portion of the proceeds generously donated to support the Special Olympics.
- STAR board member Melissa Proffitt Schmidt and Partner-in-Charge of Client Relations at the law firm of Ice Miller LLP., was honored by the Indiana Historical Society as a "Living Legend" for 2023. Each year, IHS recognizes extraordinary Hoosiers for their local, statewide and national accomplishments in a variety of areas and disciplines.
- STAR Bank was voted "Grant County's Greatest Bank" this year! We are extremely proud of the group we have in that town with all the banking options our customers have in this legacy market.
- Kudos to Jim Marcuccilli, Chairman & CEO, and Kristin Marcuccilli, President, STAR Financial Group, for their well-deserved recognition on the prestigious Indianapolis Business Journal's Indiana 250 list for the second year in a row! This impressive list acknowledges the top leaders who have made a significant impact on both the business and community landscape in Indiana.



STAR Financial Group, Inc.

Independent Auditor's Report and
Consolidated Financial Statements

December 31, 2023 and 2022

STAR Financial Group, Inc.
Financial Highlights
Years Ended December 31, 2023, 2022, and 2021
(In Thousands Except Share Data)

	2023	2022	2021
For the Year			
Net income	$ 23,863	$ 23,129	$ 33,245
Dividends declared	3,658	3,667	4,021
Weighted average shares	2,792,246	2,968,111	3,346,906
Per Basic Common Share			
Net income	$ 8.55	$ 7.79	$ 9.93
Dividends declared	1.31	1.24	1.20
Book value at December 31	67.08	54.02	81.81
At December 31			
Total assets	$ 2,998,676	$ 3,011,251	$ 3,107,138
Earning assets	2,737,004	2,754,128	2,917,649
Loans and leases	1,639,546	1,598,869	1,500,906
Deposits	2,546,014	2,523,807	2,754,738
Total parent company stockholders' equity	187,308	150,835	247,281
Capital Ratios (Bank only)			
Risk-based capital ratios			
Tier I	12.32%	13.00%	13.61%
Total (Tier I plus Tier II)	13.18	13.89	14.63
Leverage ratio	9.73	9.03	8.30
Common Equity Tier I	12.32	13.00	13.61

FORV/S

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Independent Auditor's Report

Audit Committee
STAR Financial Group, Inc.
Fort Wayne, Indiana

Opinion

We have audited the consolidated financial statements of STAR Financial Group, Inc. (Company) and subsidiaries, which comprise the consolidated balance sheets as December 31, 2023 and 2022, and the related statements of income, comprehensive income (loss), changes in stockholders' equity, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of STAR Financial Group, Inc. and subsidiaries as of December 31, 2023 and 2022, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

We also have audited, in accordance with auditing standards generally accepted in the United States of America, STAR Financial Group, Inc.'s internal control over financial reporting as of December 31, 2023, based on criteria established in *Internal Control – Integrated Framework* (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) and our report dated March 27, 2024, expressed an unmodified opinion on the effectiveness of the Company's internal control over financial reporting.

Basis for Opinion

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

Emphasis of Matter

As discussed in Note 1 to the consolidated financial statements, in 2023, the entity changed its method of accounting for credit losses on financial instruments due to the adoption of Accounting Standards Codification Topic 326: *Financial Instruments – Credit Losses*. Our opinion is not modified with respect to this matter.

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 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 STAR Financial Group, Inc.'s ability to continue as a going concern within one year after the date that these consolidated financial statements are 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.

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 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 STAR Financial Group, Inc.'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 Included in the Annual Report

Management is responsible for the other information included in the annual report. The other information comprises the information included in the annual report 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 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.

FORVIS, LLP

Fort Wayne, Indiana
March 27, 2024

STAR Financial Group, Inc.

Consolidated Balance Sheets
Years Ended December 31, 2023 and 2022
(In Thousands Except Share Data)

	2023	2022
Assets		
Cash and cash equivalents		
Cash and due from banks	$ 62,511	$ 67,721
Interest-bearing demand deposits	51,204	37,384
Total cash and cash equivalents	113,715	105,105
Investment securities available-for-sale	1,065,207	1,136,572
Loans held for sale	249	422
Loans and leases	1,639,546	1,598,869
Less: Allowance for credit losses	(19,202)	(19,119)
Net loans and leases	1,620,344	1,579,750
Bank owned life insurance	46,838	46,449
Premises and equipment, net	80,184	66,041
Interest receivable	11,328	11,249
Goodwill	2,636	2,636
Other assets, net	58,175	63,027
Total assets	$ 2,998,676	$ 3,011,251
Liabilities and Equity		
Liabilities		
Deposits		
Demand, noninterest bearing	$ 908,898	$ 982,696
Interest bearing		
Demand	1,358,934	1,427,816
Time deposits	278,182	113,295
Total deposits	2,546,014	2,523,807
Long-term borrowings	175,000	245,013
Junior subordinated debt	10,310	10,310
Subordinated debt	50,000	50,000
Other liabilities, net	27,438	28,677
Total liabilities	2,808,762	2,857,807
Equity		
Common Stock		
No par value, 5,000,000 shares authorized, 4,854,380 shares issued	7,359	7,359
Capital surplus	7,454	7,318
Retained earnings	367,296	349,183
Accumulated other comprehensive loss	(81,968)	(100,285)
Treasury stock at cost, 2,063,382 and 2,062,007 shares		
as of December 31, 2023 and 2022, respectively	(112,833)	(112,740)
Total Parent Company Stockholders' Equity	187,308	150,835
Noncontrolling Interest	2,606	2,609
Total equity	189,914	153,444
Total liabilities and equity	$ 2,998,676	$ 3,011,251

STAR Financial Group, Inc.

Consolidated Statements of Income
Years Ended December 31, 2023 and 2022
(In Thousands Except Share Data)

	2023	2022
Interest Income		
Interest on loans	$ 88,778	$ 66,628
Interest on investment securities		
Taxable	39,588	19,219
Tax exempt	1,365	3,495
Total interest income	129,731	89,342
Interest Expense		
Interest on deposits	32,265	4,087
Interest on borrowings	11,390	3,272
Total interest expense	43,655	7,359
Net Interest Income	86,076	81,983
Credit Loss Expense	2,950	725
Net Interest Income After Credit Loss Expense	83,126	81,258
Noninterest Income		
Service charges and fees	7,338	7,764
Bank card processing	9,115	9,621
Mortgage sales and servicing fees	1,263	1,693
Trust and brokerage fee income	4,338	3,993
Loss on sale of fixed assets	(80)	(155)
Other fees and commissions	1,035	837
Loss on sales of securities	(658)	(1,693)
Other	2,860	2,810
Total noninterest income	25,211	24,870
Noninterest Expense		
Salaries and employee benefits	45,025	42,936
Occupancy expense	5,386	5,259
Equipment expense	11,572	11,596
Bank card processing fees	3,566	3,024
Loan and collection expense	1,126	1,549
Deposit insurance premiums	1,520	1,363
Advertising and promotional	1,742	1,458
Professional services	2,218	2,693
Other	7,849	8,541
Total noninterest expense	80,004	78,419
Income Before Income Taxes	28,333	27,709
Provision for Income Taxes	4,470	4,580
Net Income	$ 23,863	$ 23,129
Income Per Share		
Basic	$ 8.55	$ 7.79
Diluted	$ 8.50	$ 7.77
Weighted Average Shares Outstanding		
Basic	2,792,246	2,968,111
Diluted	2,806,099	2,975,058

See Notes to Consolidated Financial Statements

STAR Financial Group, Inc.

Consolidated Statements of Comprehensive Income (Loss)
Years Ended December 31, 2023 and 2022
(In Thousands)

	2023	2022
Net Income	$ 23,863	$ 23,129
Other Comprehensive Income (Loss)		
Unrealized appreciation (depreciation) on available-for-sale securities, net of taxes of $4,731 and ($26,425), for 2023 and 2022, respectively	17,797	(99,409)
Reclassification adjustment for realized losses included in net income, net of taxes of $138 and $356, for 2023 and 2022, respectively	520	1,337
	18,317	(98,072)
Comprehensive Income (Loss)	$ 42,180	$ (74,943)

See Notes to Consolidated Financial Statements

STAR Financial Group, Inc.

Consolidated Statements of Changes in Equity
Years Ended December 31, 2023 and 2022
(In Thousands Except Share Data)

	Common Stock	Capital Surplus	Retained Earnings	Accumulated Other Comprehensive Loss	Treasury Stock	Total Parent Company Stockholders' Equity	Non Controlling Interest	Total Equity
Balance, January 1, 2022	$ 7,359	$ 6,712	$ 329,721	$ (2,213)	$ (94,298)	$ 247,281	$ 934	$ 248,215
Net income	-	-	23,129	-	-	23,129	-	23,129
Other comprehensive loss	-	-	-	(98,072)	-	(98,072)	-	(98,072)
Cash dividends ($1.24 per share)	-	-	(3,667)	-	-	(3,667)	-	(3,667)
Purchase of treasury stock (231,686 shares)	-	-	-	-	(18,547)	(18,547)	-	(18,547)
Share based compensation expense	-	711	-	-	-	711	-	711
Issuance of treasury stock for restricted stock awards (1,451 shares)	-	(105)	-	-	105	-	-	-
Contributions from noncontrolling interests	-	-	-	-	-	-	2,152	2,152
Distributions to noncontrolling interests	-	-	-	-	-	-	(477)	(477)
Balance, December 31, 2022	7,359	7,318	349,183	(100,285)	(112,740)	150,835	2,609	153,444
Cumulative change in accounting principle (Note 1)	-	-	(2,092)	-	-	(2,092)	-	(2,092)
Balance at January 1, 2023 (as adjusted for change in accounting principle)	7,359	7,318	347,091	(100,285)	(112,740)	148,743	2,609	151,352
Net income	-	-	23,863	-	-	23,863	-	23,863
Other comprehensive income	-	-	-	18,317	-	18,317	-	18,317
Cash dividends ($1.31 per share)	-	-	(3,658)	-	-	(3,658)	-	(3,658)
Purchase of treasury stock (4,218 shares)	-	-	-	-	(317)	(317)	-	(317)
Share based compensation expense	-	360	-	-	-	360	-	360
Issuance of treasury stock for restricted stock awards (2,843 shares)	-	(224)	-	-	224	-	-	-
Distributions to noncontrolling interests	-	-	-	-	-	-	(3)	(3)
Balance, December 31, 2023	$ 7,359	$ 7,454	$ 367,296	$ (81,968)	$ (112,833)	$ 187,308	$ 2,606	$ 189,914

See Notes to Consolidated Financial Statements

STAR Financial Group, Inc.

Consolidated Statements of Cash Flows
Years Ended December 31, 2023 and 2022
(In Thousands)

	2023	2022
Operating Activities		
Net income	$ 23,863	$ 23,129
Items not requiring (providing) cash		
Provision for credit losses	2,950	725
Net gain from sale of loans	(426)	(874)
Origination of loans for sale	(11,064)	(26,375)
Proceeds from sale of loans	11,663	30,088
Increase in value of bank-owned life insurance	(1,123)	(1,062)
Depreciation and amortization on premises and equipment	5,203	5,479
Net amortization of securities	4,220	9,951
Provision for deferred taxes	(420)	506
Loss on sale of securities	658	1,693
Loss on sale of premises and equipment	80	155
Repayment of operating lease liabilities	1,197	1,773
Share based compensation expense	360	711
Change in interest receivable	(79)	(2,874)
Change in other assets	(272)	(8,683)
Change in other liabilities	(3,060)	(7,289)
Net cash provided by operating activities	33,750	27,053
Investing Activities		
Proceeds from sales of investment securities available-for-sale	82,177	33,498
Proceeds from maturities and calls of investment securities available-for-sale	68,813	110,192
Proceeds from disposal of premises and equipment	-	58
Proceeds from bank-owned life insurance policy	734	1,179
Purchases of premises and equipment	(19,426)	(23,502)
Purchases of investment securities available-for-sale	(61,283)	(365,519)
Net change in loans	(44,371)	(98,583)
Net cash provided (used) in investing activities	26,644	(342,677)
Financing Activities		
Net change in deposits	22,207	(230,931)
Proceeds from long-term borrowings	210,000	370,000
Repayment of long-term borrowings	(280,013)	(135,013)
Cash dividends	(3,658)	(3,667)
Purchase of treasury stock	(317)	(18,547)
Contributions from noncontrolling interests	-	2,152
Distributions to noncontrolling interests	(3)	(477)
Net cash used by financing activities	(51,784)	(16,483)
Net Change in Cash and Cash Equivalents	8,610	(332,107)
Cash and Cash Equivalents, Beginning of Year	105,105	437,212
Cash and Cash Equivalents, End of Year	$ 113,715	$ 105,105

See Notes to Consolidated Financial Statements

STAR Financial Group, Inc.

Consolidated Statements of Cash Flows
Years Ended December 31, 2023 and 2022
(In Thousands)

	2023	2022
Supplemental Cash Flows Information		
Interest paid	$ 43,093	$ 6,962
Income taxes paid	5,381	4,580
Lease liabilities arising from obtaining right-of use assets	-	2,117

See Notes to Consolidated Financial Statements

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

Nature of Operations

STAR Financial Group, Inc. (STAR or the Company) is a bank holding company whose principal activity is the ownership and management of its wholly owned subsidiaries, STAR Financial Bank (Bank), Finance and Insurance, Inc. (Insurance), and STAR Captive Insurance (Captive). In 2013, the Company formed STAR Captive Insurance as a wholly owned subsidiary to insure members of the consolidated group for potential losses in excess of existing insurance policies. Effective December 31, 2023, Captive was legally liquidated and dissolved. The Bank has one wholly owned subsidiary, Titan, Inc. (Titan). In the first quarter of 2021, the Company completed an asset sale of STAR Insurance Agency (SIA) and changed the name of the business entity to Finance and Insurance, Inc. Effective December 31, 2022, Finance and Insurance, Inc. was legally dissolved. In 2020, the Company owned 100% of the newly formed entity, 215 W Main, LLC, which was established to acquire and hold real estate. 215 W Main is the majority owner in the new construction project, incorporated as Berry Maiden Main, LLC, that began in 2021 for STAR's new headquarters. The Bank is primarily engaged in providing a full range of banking and financial services to individual and corporate customers throughout Central and Northeastern Indiana. The Bank is subject to the regulation of certain federal and state agencies and undergoes periodic examinations by those regulatory authorities. The Bank also provides trust and investment advisory services through a separate division titled STAR Wealth Management (Wealth). Titan is primarily engaged in managing the Bank's investment securities.

Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

Material estimates that are particularly susceptible to significant change relate to the determination of the allowance for credit losses.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation.

Cash and Cash Equivalents

All highly liquid investments with original maturities of three months or less are considered to be cash equivalents. Cash and cash equivalents are defined to include the Company's cash on hand and demand deposits with other institutions (including money market mutual funds).

At December 31, 2023, the Company's cash accounts exceeded federally insured limits by approximately $22,244,000.

Investment Securities

Available-for-sale securities, which include any debt security for which the Company has no immediate plan to sell but which may be sold in the future, are carried at fair value. Unrealized gains and losses for those with no allowance for credit losses are recorded, net of related income tax effects, in other comprehensive income (loss). Changes in the fair value of equity securities is recorded in non-interest income. Amortization of premiums and accretion of discounts are recorded as interest income from securities. Realized gains and losses are recorded as net security gains (losses). Gains and losses on sales of securities are determined on the specific-identification method.

For debt securities with fair value below amortized cost when the Company does not intend to sell a debt security, and it is more likely than not, the Company will not have to sell the security before recovery of its cost basis, it recognizes the credit component in earnings as an allowance for credit losses and the remaining portion is recognized in other comprehensive income (loss). The credit loss component recognized in earnings is identified as the amount of principal cash flows not expected to be received over the remaining term of the security as projected based on cash flow projections.

Allowance for Credit Losses – Available-For-Sale Securities

For available-for-sale securities in an unrealized loss position, the Company first assesses whether the security meets certain criteria. The criteria is whether the Company intends to sell the security, or it is more likely than not than it will be required to sell the security before recovery of its amortized cost basis. If either of the criteria regarding intent or requirements to sell is met, the security's amortized cost basis is written down to fair value through income.

For debt securities available-for-sale that do not meet the above criteria, the Company evaluates whether the decline in fair value has resulted from credit losses or other factors. In making this assessment, management considers the extent to which fair value is less than amortized cost, any changes to the rating of the security by a rating agency, and adverse conditions specifically related to the security, among other factors. If this assessment indicates that a credit loss exists, the present value of cash flows expected to be collected from the security are compared to the amortized cost basis of the security. If the present value of cash flows expected to be collected is less than the amortized cost basis, a credit loss exists and an allowance for credit losses is recorded for the credit loss, limited by the amount that the fair value is less than the amortized cost basis. Any impairment that has not been recorded through an allowance for credit losses is recognized in other comprehensive income.

Changes in the allowance for credit losses are recorded as credit loss expense (or reversal). Losses are charged against the allowance when management believes the uncollectibility of an available-for-sale security is confirmed or when either of the criteria regarding intent to requirement to sell is met.

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 in the aggregate. Net unrealized losses, if any, are recognized through a valuation allowance by charges to noninterest income. Gains and losses on loan sales are recorded in noninterest income, and direct loan origination costs and fees are deferred at origination of the loan and are recognized in noninterest income upon sale of the loan.

Loans

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are reported at their outstanding principal balances adjusted for unearned income, charge-offs, the allowance for credit 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 as a level yield adjustment over the respective term of the loan.

For all loan classes, the accrual of interest 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. For all loan classes, the entire balance of the loan is considered past due if the minimum payment contractually required to be paid is not received by the contractual due date. For all loan classes, loans are placed on nonaccrual or charged off at an earlier date if collection of principal or interest is considered doubtful.

Management's general practice is to proactively charge down loans individually evaluated to the fair value of the underlying collateral. Consistent with regulatory guidance, charge-offs on all loan segments are taken when specific loans, or portions thereof, are considered uncollectible. The Company's policy is to promptly charge these loans off in the period the uncollectible loss is reasonably determined.

For all loan portfolio segments except residential and consumer loans, the Company promptly charges-off loans, or portions thereof, when available information confirms that specific loans are uncollectible based on information that includes, but is not limited to, (1) the deteriorating financial condition of the borrower, (2) declining collateral values, and/or (3) legal action, including bankruptcy, that impairs the borrower's ability to adequately meet its obligations. For loans that are considered to be solely collateral dependent, a partial charge-off is recorded when a loss has been confirmed by an updated appraisal or other appropriate valuation of the collateral.

The Company charges-off residential and consumer loans, or portions thereof, when the Company reasonably determines the amount of the loss. The Company adheres to timeframes established by applicable regulatory guidance which provides for the charge-down of 1-4 family first mortgages, junior lien mortgages and other secured consumer loans at 90 days past due. Unsecured retail loans are wholly charged off when the loan is 90 days past due.

For all loan classes, 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 and future payments are reasonably assured. Nonaccrual loans are returned to accrual status when, in the opinion of management, the financial position of the borrower indicates there is no longer any reasonable doubt as to the timely collection of interest or principal. The Company requires a period of satisfactory performance of not less than six months before returning a nonaccrual loan to accrual status.

When cash payments are received on individually evaluated loans in each loan class, the Company records the payment as interest income unless collection of the remaining recorded principal amount is doubtful, at which time payments are used to reduce the principal balance of the loan. Troubled debt modification loans recognize interest income on an accrual basis at the renegotiated rate if the loan is in compliance with the modified terms, no principal reduction has been granted and the loan has demonstrated the ability to perform in accordance with the renegotiated terms for a period of at least six months.

Allowance for Credit Losses - Loans

The allowance for credit losses is established as losses are estimated to have occurred through a provision for credit losses charged to income. Credit losses are charged against the allowance when management believes the uncollectability of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

The allowance for credit losses is evaluated on a regular basis by management and is based upon management’s periodic review of the collectability of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower’s ability to repay, estimated value of any underlying collateral and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

The allowance for credit losses contains general and allocated components. The general component covers loans with similar risk characteristics. The allocated component covers loans that do not share risk characteristics and are evaluated on an individual basis. Loans evaluated individually are not also included in the collective evaluation. For those loans that are individually evaluated, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the loan is lower than the carrying value of that loan.

The methodology for calculating the general component of the allowance for credit loss contains four elements: the average charge-off method, qualitative elements, a forward look consideration, and a prepayment analysis. The average charge-off method calculates an estimate of losses primarily based on past experience by segment. The historical loss experience is determined by portfolio segment and is based on the actual loss history on a weighted average basis experienced by the Company. Management believes the weighted average historical loss experience methodology is appropriate in the current economic environment. The qualitative elements utilized in the allowance for credit loss calculation utilizes both objective and subjective indicators. The qualitative elements include nine categories: ability of staff, changes in collateral values, changes in loan concentration levels, economic conditions, external factors such as regulatory, level and trends in non-accrual or adversely classified loans, loan review results, nature and volume of the portfolio and loan terms, and changes in lending policies and procedures. Items within these categories are ranked as baseline, low, medium, or high levels of risk, and the related risk level per categories dictates the level of qualitative factor that is used depending on the standard deviation level from historical loss. The forward look consideration consists of leveraging a regression analysis based on forward looking economic forecasts. Forecast data for GDP and unemployment from the Federal Reserve are used in conjunction with third-party providers to complete a forward look consideration in the allowance for credit loss calculation. The prepayment analysis relates to anticipated prepayment speeds which will adjust anticipated loan losses. The prepayment calculation considers the interest rate environment and whether any economic incentives exist that would affect the average life of the loan portfolio.

A loan is considered collateral dependent when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in identifying a collateral dependent loan include payment status, collateral value and the probability of collecting scheduled principal and interest payments when due based on the loan's current payment status and the borrower's financial condition including available sources of cash flows. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as collateral dependent. 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. Collateral dependency is measured on a loan-by-loan basis for non-homogenous type loans such as commercial, non-owner residential and construction 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. For collateral dependent loans where the Company utilizes the discounted cash flows method, the Company includes the entire change in the present value of cash flows as provision for credit losses.

The fair values of collateral dependent loans are based on independent appraisals of the collateral. In general, the Company acquires an updated appraisal upon identification of individual evaluation and annually thereafter for commercial, commercial real estate and multi-family loans. It is the Company's practice to obtain annual appraisals on collateral dependent loans. The Company applies a discount rate to the appraisal based upon the collateral type. In the case of commercial real estate, the discount rate is 25%. After determining the collateral value as described, the fair value is calculated based on the determined collateral value less selling expenses. The potential for outdated appraisal values is considered in the Company's determination of the allowance for credit losses through the analysis of various trends and conditions including the local economy, trends in charge-offs and delinquencies, etc. and the related qualitative adjustments assigned by the Company.

Segments of loans with similar risk characteristics are collectively evaluated based on the segment's historical loss experience adjusted for changes in trends, conditions and other relevant factors that affect repayment of the loans. Accordingly, the Company does not separately identify individual consumer and residential loans for the allocated component of the allowance for credit loss calculation, unless such loans are the subject of a restructuring agreement due to financial difficulties of the borrower.

In the course of working with borrowers, the Company may choose to restructure the contractual terms of certain loans. In this scenario, the Company attempts to work-out an alternative payment schedule with the borrower in order to optimize collectability of the loan. Any loans that are modified are reviewed by the Company to identify if a troubled debt modification (TDM) has occurred, which is when, for economic or legal reasons related to a borrower's financial difficulties, the Company grants a concession to the borrower that it would not otherwise consider. Terms may be modified to fit the ability of the borrower to repay in line with its current financial status and the restructuring of the loan may include the transfer of assets from the borrower to satisfy the debt, a modification of loan terms, or a combination of the two. If such efforts by the Company do not result in a satisfactory arrangement, the loan is referred to legal counsel, at which time foreclosure proceedings are initiated. At any time prior to a sale of the property at foreclosure, the Company may terminate foreclosure proceedings if the borrower is able to work-out a satisfactory payment plan.

It is the Company's policy to have any restructured loans which are on nonaccrual status prior to being restructured remain on nonaccrual status until six months of satisfactory borrower performance at which time management would consider its return to accrual status. If a loan was accruing at the time of restructuring, the Company reviews the loan to determine if it is appropriate to continue the accrual of interest on the restructured loan.

Allowance for Credit Losses – Off-Balance Sheet Exposure

The Company estimates expected credit losses over the contractual period in which the Company is exposed to credit risk via a contractual obligation to extend credit, unless that obligation is unconditionally cancellable by the Company. The allowance for credit losses on off-balance sheet exposures is adjusted through credit loss expense. The estimate includes consideration of the likelihood that funding will occur and an estimate of expected credit losses on commitments expected to be funded over its estimated life.

Bank Owned Life Insurance

Bank owned life insurance consists of investments in life insurance policies on certain key executives and other members of the Bank's management. The policies are carried at their net cash surrender value. Changes in the policy value are recorded as an adjustment to the carrying value with the corresponding amount recognized as non-interest income or expense. Earnings on these policies are based on the net earnings on the cash surrender value of the policies.

Premises and Equipment

Premises and equipment are recorded at cost less accumulated depreciation. The provision for depreciation is computed on the straight-line method over the estimated useful lives of the assets generally ranging from three to 25 years. Leasehold improvements are capitalized and depreciated using the straight-line method over the terms of the respective leases or the estimated useful lives of the improvements, whichever is shorter. Maintenance and repairs are expensed as incurred, while major additions and improvements are capitalized. Gains and losses on disposition are included in the consolidated statements of income.

FHLB Stock

Federal Home Loan Bank (FHLB) stock is a required investment for institutions that are members of the Federal Home Loan Bank system. The required investment in the common stock is based on a predetermined formula, carried at cost and evaluated for impairment. Included in other assets on the consolidated balance sheets is FHLB stock totaling $11,070,600 at December 31, 2023 and 2022.

Goodwill

Goodwill is evaluated annually for impairment – or more frequently if impairment indicators are present. 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 recorded in the consolidated financial statements. There was no impairment as of December 31, 2023.

Intangible Assets

Intangible assets with finite lives are being amortized on the straight-line basis over periods ranging from five to seven years. Such assets are periodically evaluated as to the recoverability of their carrying values.

Other Real Estate Owned

Other real estate owned represents properties acquired through foreclosures or deeds in lieu of foreclosure or former branches held for sale. The properties 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. Any excess of the loan amount over the net realizable value of such property when acquired is charged to the allowance for loan and lease losses, 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. In the case of former branches, any excess of net book value over the net realizable value of such property is charged to impairment of premises and equipment. Subsequent write-downs and gains or losses on sales are recorded in the income statement. Costs of maintaining the properties are recorded in the consolidated income statement as incurred. Included in other assets on the consolidated balance sheets is other real estate owned totaling $301,343 and $521,343 at December 31, 2023 and 2022, respectively.

Mortgage Servicing Rights

Mortgage servicing assets are recognized when rights are acquired through the sale of financial assets. Under the servicing assets and liabilities accounting guidance (ASC 860-50), servicing rights resulting from the sale of loans originated by the Company are initially measured at fair value at the date of transfer. The Company subsequently measures each class of servicing asset using the amortization method. Under the amortization method, servicing rights are amortized in proportion to and over the period of estimated net servicing income. The amortized assets are assessed for impairment based on fair value at each reporting date.

Fair value is based on market prices for comparable mortgage servicing contracts, when available, or alternatively, is based on a valuation model that calculates the present value of estimated future net servicing income. The valuation model incorporates assumptions that market participants would use in estimating future net servicing income, such as the cost to service, the discount rate, the custodial earnings rate, an inflation rate, ancillary income, prepayment speeds and default rates and losses. These variables change from quarter to quarter as market conditions and projected interest rates change, and may have an adverse impact on the value of the mortgage servicing right and may result in a reduction to noninterest income.

Each class of separately recognized servicing assets subsequently measured using the amortization method are evaluated and measured for impairment. Impairment is determined by stratifying rights into tranches based on predominant characteristics, such as interest rate, loan type and investor type. Impairment is recognized through a valuation allowance for an individual tranche, to the extent that fair value is less than the carrying amount of the servicing assets for that tranche. The valuation allowance is adjusted to reflect changes in the measurement of impairment after the initial measurement of impairment. Changes in valuation allowances are reported with mortgage sales and servicing fees on the income statement. Fair value in excess of the carrying amount of servicing assets for that stratum is not recognized.

Servicing fee income is recorded for fees earned for servicing loans. The fees are based on a contractual percentage of the outstanding principal or a fixed amount per loan and are recorded as income when earned. The amortization of mortgage servicing rights is netted against loan servicing fee income.

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.

Lease Commitments

The Company leases certain banking center locations, office space, land and billboards. In determining whether a contract contains a lease, the Company examines the contract to ensure an asset was specifically identified and that the Company has control of use over the asset. To determine whether a lease is classified as operating or finance, the Company performs an economic life test on all building leases with greater than a twenty years term. Further, the Company performs a fair value test to identify any leases that have a present value of future lease payments over the lease term that is greater than 90% of the fair value of the building.

At lease inception, the Company determines the lease term by adding together the minimum lease term and all optional renewal periods that it is reasonably certain to renew. The Company determines this on each lease by considering all relevant contract based, asset-based, market-based, and entity-based economic factors. Generally, the exercise of lease renewal options is at the Company's sole discretion. The lease term is used to determine whether a lease is operating or finance and is used to calculate straight-line rent expense. Additionally, the depreciable life of leasehold improvements is limited by the expected lease term.

Operating lease rentals are expensed on a straight-line basis over the life of the lease beginning on the date the Company takes possession of the property. Rent expense and variable lease costs are included in occupancy expense on the Company's consolidated statements of income. Included in variable lease costs are leases with rent escalations based on recent financial indices, such as the Consumer Price Index, where the Company estimates future rent increases and records the actual difference to variable costs. Certain leases require the Company to pay common area maintenance, real estate taxes, insurance and other operating expenses associated with the leases premises. These expenses are classified in occupancy expense, consistent with similar costs for owned locations. There are no residual value guarantees, restrictions or covenants imposed by leases.

The Company accounts for lease and non-lease components together as a single lease component by class of underlying asset. Operating lease obligations with an initial term longer than 12 months are recorded with a right of use asset and a lease liability in the consolidated balance sheet.

The discount rate used in determining the lease liability and related right of use asset is based upon what would be obtained by the Company for similar loans as an incremental rate as of the date of origination or renewal.

Treasury Stock

Common stock shares repurchased are recorded at cost. Cost of shares retired or reissued is determined using the first-in, first-out method.

Earnings Per Share

Basic earnings per share are based on the weighted average number of common shares outstanding. Dilutive earnings per share includes the dilutive effect of additional potential common shares issuable under restricted stock awards.

Income Taxes

The Company accounts for income taxes in accordance with income tax accounting guidance (ASC 740, *Income Taxes*). The income tax accounting guidance results in two components of income tax expense: 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 revenue. The Company determines deferred income taxes using the liability 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. Uncertain 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.

The Company files consolidated income tax returns with its subsidiaries. The Company recognizes interest and penalties, if any, as income tax expense.

Reclassifications

Some items in the prior year financial statements were reclassified to conform to the current presentation. Reclassifications had no effect on prior year net income or shareholders’ equity.

Adoption of New Accounting Standards

On January 1, 2023, the Company adopted ASU 2016-13 *Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments,* as amended, which replaces the incurred loss methodology with an expected loss methodology that is referred to as the current expected credit loss (CECL) methodology. The measurement of expected credit losses under the CECL methodology is applicable to financial assets measured at amortized cost, including loan receivables and held-to-maturity debit securities. It also applies to off-balance sheet credit exposures not accounted for as insurance (loan commitments, standby letters of credit, financial guarantees, and other similar instruments) and net investments in leases recognized by a lessor in accordance with Topic 842 on leases. In addition, ASC 326 made changes to the accounting for available-for-sale debt securities. One such change is to require credit losses to be presented as an allowance rather than as a write-down on available-for-sale debt securities management does not intend to sell or believes that it is more likely than not they will be required to sell.

The Company adopted ASC 326 using the modified retrospective method for all financial assets measured at amortized cost and off-balance sheet (OBS) credit exposures. Results for reporting periods beginning after January 1, 2023 are presented under ASC 326 while prior period amounts continue to be reported in accordance with previously applicable GAAP. The Company recorded a net decrease of $2,092,000 to retained earnings as of January 1, 2023 for the cumulative effect of adopting ASC 326. The transition adjustment is net of taxes of $555,000.

(Table Dollars in Thousands Except Share Data)

The following table illustrates the impact of ASC 326.

	January 1, 2023		
	As Reported Under ASC 326	Pre-ASC 326 Adoption	Impact of ASC 326 Adoption
Assets:			
Allowance for credit losses on loans	$ 19,946	$ 19,119	$ 827
Liabilities			
Allowance for credit losses on OBS credit exposures	1,820	-	1,820
	$ 21,766	$ 19,119	$ 2,647

The Company adopted ASC 326 using the prospective approach for debt securities for which other-than-temporary impairment had been recognized prior to January 1, 2023. As a result, the amortized cost basis remains the same before and after the effective date of ASC 326. The effective interest rate on these debt securities was not changed. Amounts previously recognized in accumulated other comprehensive loss as of January 1, 2023 relating to improvements in cash flows expected to be collected will be accreted into income over the remaining life of the asset. Recoveries of amounts previously written off relating to improvements in cash flows after January 1, 2023 will be recorded in earnings when received.

Subsequent Events

Subsequent events have been evaluated through March 27, 2024, which is the date the consolidated financial statements were available to be issued.

Note 2: Investment Securities

The amortized cost and approximate fair values, together with gross unrealized gains and losses, of securities are as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
December 31, 2023				
U.S. Treasury and agency securities	$ 106,120	$ -	$ 7,363	$ 98,757
Obligations of states and political subdivisions	159,591	7	28,399	131,199
Mortgage-backed Government Sponsored Enterprise (GSE) residential	879,159	477	67,441	812,195
Pooled trust preferred securities	24,015	139	1,098	23,056
	$ 1,168,885	$ 623	$ 104,301	$ 1,065,207

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
December 31, 2022				
U.S. Treasury and agency securities	$ 109,500	$ -	$ 9,977	$ 99,523
Obligations of states and political subdivisions	243,587	45	37,744	205,888
Mortgage-backed Government Sponsored Enterprise (GSE) residential	896,093	301	78,249	818,145
Pooled trust preferred securities	14,335	-	1,319	13,016
	$ 1,263,515	$ 346	$ 127,289	$ 1,136,572

Securities with a carrying value of approximately $212,157,000 and $133,373,000 at December 31, 2023 and 2022, respectively, were pledged to secure public and trust deposits, securities sold under agreements to repurchase and for other purposes as required by law.

(Table Dollars in Thousands Except Share Data)

The amortized cost and fair value of securities at December 31, 2023, by contractual maturity are shown below. Expected maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Available for Sale	
	Amortized Cost	Fair Value
Due within one year	$ 950	$ 947
Due after one year through five years	84,876	79,641
Due after five years through ten years	29,584	25,902
Due after ten years	174,316	146,522
Total investment securities with a contractual maturity	289,726	253,012
Mortgage-backed GSE residential	879,159	812,195
Total investment securities	$ 1,168,885	$ 1,065,207

There were no gross gains on available-for-sale securities during 2023 and 2022. Gross losses of $658,000 and $1,693,000 resulting from sales of AFS securities were realized in 2023 and 2022.

Certain investments in debt and equity securities are reported in the consolidated financial statements at an amount less than their historical cost. Total fair value of these investments at December 31, 2023 and 2022, was $1,016,859,000 and $1,102,788,000 respectively, which is approximately 95% and 97%, respectively, of the available-for-sale investment portfolio. These declines primarily resulted from changes in market interest rates since the securities were purchased and current depressed market conditions.

The Company has not recorded an allowance for credit losses for available-for-sale securities at December 31, 2023. This is based on evaluation of available evidence, including recent changes in market interest rates, discounted cash flow analysis, and credit rating information, except as discussed below.

The following table shows the Company's investments' gross unrealized losses and fair value, aggregated by investment class and length of time that individual securities have been in a continuous unrealized loss position at December 31, 2023 and 2022.

	December 31, 2023					
	Less than 12 Months		12 Months or More		Total	
Description of Securities	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. Treasury and agency securities	$ 947	$ 3	$ 97,482	$ 7,360	$ 98,429	$ 7,363
Obligations of states and political subdivisions	-	-	130,867	28,399	130,867	28,399
Mortgage-backed GSE residential	31,581	386	743,206	67,055	774,787	67,441
Pooled trust preferred securities	-	-	12,776	1,098	12,776	1,098
	$ 32,528	$ 389	$ 984,331	$ 103,912	$ 1,016,859	$ 104,301

	December 31, 2022					
	Less than 12 Months		12 Months or More		Total	
Description of Securities	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. Treasury and agency securities	$ 23,229	$ 1,452	$ 76,294	$ 8,525	$ 99,523	$ 9,977
Obligations of states and political subdivisions	106,218	7,091	86,155	30,653	192,373	37,744
Mortgage-backed GSE residential	292,491	18,642	505,385	59,607	797,876	78,249
Pooled trust preferred securities	-	-	13,016	1,319	13,016	1,319
	$ 421,938	$ 27,185	$ 680,850	$ 100,104	$ 1,102,788	$ 127,289

(Table Dollars in Thousands Except Share Data)

U.S. Treasury and Agency Securities

The unrealized losses on the Company's investments in securities of U.S. Treasury and Agency Securities were caused by interest rate changes. The contractual terms of those investments do not permit the issuer to settle the securities at a price less than the amortized cost basis of the investments. Because the Company does not intend to sell the investments and it is not more likely than not the Company will be required to sell the investments before recovery of their amortized cost basis, which may be maturity, the Company has not recorded an allowance for credit losses at December 31, 2023.

Obligations of State and Political Subdivisions

The unrealized losses on the Company's investments in securities of state and political subdivisions were caused by interest rate changes. The contractual terms of those investments do not permit the issuer to settle the securities at a price less than the amortized cost basis of the investments. Because the Company does not intend to sell the investments and it is not more likely than not the Company will be required to sell the investments before recovery of their amortized cost basis, which may be maturity, the Company has not recorded an allowance for credit losses at December 31, 2023.

Mortgage-backed GSE Residential

The unrealized losses on the Company's investment in mortgage-backed GSE residential securities were caused by interest rate changes. The Company expects to recover the amortized cost basis over the term of the securities. Because the decline in market value is attributable to changes in interest rates and not credit quality, and because the Company does not intend to sell the investments and it is not more likely than not the Company will be required to sell the investments before recovery of their amortized cost basis, which may be maturity, the Company has not recorded an allowance for credit losses at December 31, 2023.

Pooled Trust Preferred Securities

Pooled trust preferred securities within the available-for-sale portfolio include six securities which are collateralized by trust preferred securities principally issued by banks. As of December 31, 2023, there were six pools and one pool was determined to be fully evaluated if a credit loss exists by monitoring to ensure it has adequate credit support. Management believes there is no need for an allowance for credit losses. The remaining five securities rated below investment grade were evaluated for impairment as discussed below and not deemed to be other-than-temporarily impaired. The Company's unrealized losses on pooled trust preferred securities were primarily caused by deterioration in the financial status of the institutions within the respective pools and sector downgrades by analysts and rating agencies.

Note 3: Loans and Allowance for Loan and Lease Losses

STAR's business activity is primarily with customers located in north central and northeast Indiana. The loan portfolio is diversified by type and industry. Collateral requirements for each loan are based upon the credit evaluation of each transaction.

Classes of loans at December 31, include:

	2023	2022
Commercial and industrial	$ 584,054	$ 587,937
Commercial real estate	632,247	620,929
Consumer:		
Consumer, home equity lines of credit	84,083	76,955
Consumer, auto	11,998	13,279
Consumer, other	12,772	14,312
Residential	310,182	278,836
Finance leases	4,210	6,621
Gross loans	1,639,546	1,598,869
Allowance for credit losses	(19,202)	(19,119)
Net loans	$ 1,620,344	$ 1,579,750

(Table Dollars in Thousands Except Share Data)

The components of the Company's direct financing leases as of December 31 are summarized below:

	2023	2022
Future minimum lease payments	$ 4,393	$ 6,826
Residual interests	218	408
Initial direct costs	1	6
Unearned income	(402)	(619)
	$ 4,210	$ 6,621

Future minimum lease payments are as follows:

2024	$ 1,223
2025	829
2026	627
2027	462
2028	275
Thereafter	977
	$ 4,393

The risk characteristics of each loan portfolio segment are as follows:

Commercial and Industrial and Commercial Real Estate

Commercial and industrial loans are primarily 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 loans are secured by the assets being financed or other business assets, such as accounts receivable or inventory, and may include a personal guarantee. 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 on the ability of the borrower to collect amounts due from its customers.

Commercial real estate loans are viewed primarily as cash flow loans and secondarily as loans secured by real estate. Commercial real estate lending typically involves higher loan principal amounts and the repayment of these loans is generally 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. The characteristics of properties securing the Company's commercial real estate portfolio are diverse, but with geographic location almost entirely in the Company's market area. Management monitors and evaluates commercial real estate loans based on collateral, geography and risk grade criteria. In general, the Company avoids financing single purpose projects unless other underwriting factors are present to help mitigate risk. In addition, management tracks the level of owner-occupied commercial real estate versus nonowner-occupied loans.

Real Estate, Consumer, Leases and Other

Real estate, consumer, leases and other loans consist of four segments - residential mortgage loans, personal loans, direct financing leases and other loans. For residential mortgage loans that are secured by 1-4 family residences and are generally owner-occupied, the Company generally establishes a maximum loan-to-value ratio and requires private mortgage insurance if that ratio is exceeded. Home equity loans are typically secured by a subordinate interest in 1-4 family residences. Consumer personal, leases and other loans are secured by consumer personal assets, such as automobiles or recreational vehicles. Some consumer personal loans are unsecured, such as small installment loans and certain lines of credit. Repayment of these loans is primarily dependent on the personal income of the borrowers, which can be impacted by economic conditions in their market areas, such as unemployment levels. Repayment can also be impacted by changes in property values on residential properties. Risk is mitigated by the fact that the loans are of smaller individual amounts and spread over a large number of borrowers.

(Table Dollars in Thousands Except Share Data)

The following tables present the activity in the allowance for credit losses and the recorded investment in loans based on portfolio segment as of December 31, 2023 and 2022:

	2023					
	Commercial and Industrial	Commercial Real Estate	Consumer	Residential	Finance Leases	Total
Allowance for Credit Loss						
Balance, beginning of year, prior to adoption of ASC 326	$ 7,714	$ 7,932	$ 981	$ 2,256	$ 236	$ 19,119
Impact of adopting ASC 326	334	343	42	98	10	827
Credit loss expense	2,158	-	366	-	-	2,524
Losses charged off	(2,998)	-	(507)	-	-	(3,505)
Recoveries	190	10	35	2	-	237
Balance, end of year	$ 7,398	$ 8,285	$ 917	$ 2,356	$ 246	$ 19,202

	2022					
	Commercial and Industrial	Commercial Real Estate	Consumer	Residential	Finance Leases	Total
Allowance for Loan Loss						
Balance, beginning of year	$ 7,674	$ 7,892	$ 975	$ 2,238	$ 235	$ 19,014
Provision charged to expense	129	136	123	329	8	725
Losses charged off	(189)	(201)	(145)	(386)	(9)	(930)
Recoveries	100	105	28	75	2	310
Balance, end of year	$ 7,714	$ 7,932	$ 981	$ 2,256	$ 236	$ 19,119
Ending Balance, individually evaluated for impairment	$ 1,050	$ -	$ -	$ -	$ -	$ 1,050
Ending Balance, collectively evaluated for impairment	$ 6,664	$ 7,932	$ 981	$ 2,256	$ 236	$ 18,069
Loans						
Ending Balance	$ 587,937	$ 620,929	$ 104,546	$ 278,836	$ 6,621	$ 1,598,869
Ending Balance, individually evaluated for impairment	$ 5,130	$ 596	$ -	$ -	$ -	$ 5,726
Ending Balance, collectively evaluated for impairment	$ 582,807	$ 620,333	$ 104,546	$ 278,836	$ 6,621	$ 1,593,143

Internal Risk Categories

Loan grades are numbered 1 through 10. Grades 1 through 6 are considered satisfactory grades. The grade of 7, or Watch, represents loans of lower quality and is considered criticized. The grades of 8, or Substandard, and 9, or Special Mention, and 10, or Loss, refer to assets that are classified. The use and application of these grades by the Bank conform to the Bank's policy.

Prime (1) loans have exceptional credit fundamentals, including stable and predictable income and balance sheet performance; highly regarded with excellent management and management depth.

Good (2) loans have very good credit fundamentals but less predictable income and balance sheet performance than a prime graded credit. Loans have regional exposure in stable industry with seasoned management.

(Table Dollars in Thousands Except Share Data)

Satisfactory (3) loans are medium size or a local company in a good industry with predictable income and balance sheet performance over time.

Pass (4) all loans with acceptable credit risk but of a moderate to small size for local markets. Credit compares equally or favorably to peers and competitors with a solid balance sheet and profitability with some volatility.

Pass Minus (5) loans are credits where overall risk associated with creditworthiness criteria is considered higher than normal and warrant attention. Startup or less seasoned company within cyclical industry with moderate levels of volatility and deterioration of credit fundamentals.

Risk rated with caution (6) loans are credits where overall risk associated with creditworthiness criteria are less desirable but with potential. High or increasing risk dependence upon collateral or guarantor for protection with weaker or deteriorating financial trends.

Watch (7) all credits where overall credit fundamentals need continued review. Considered higher risk with unfavorable characteristics present. Risk, however, remains reasonable. Borrowings would usually be on a fully secured basis.

Substandard (8) credits have well-defined weaknesses where payment default is possible but not yet probable. Deficiencies are not corrected quickly and financing alternatives are limited. Reliance on collateral and guarantors is increased.

Doubtful (9) loans are credits where the possibility of loss is high, repayment is erratic or nonexistent, and loan is collateral dependent or firm in bankruptcy.

Loss (10) loans are no longer considered bankable assets.

Nonperforming mortgage, home equity and consumer loans on non-accrual or greater than 90 days past due and are internally monitored monthly by management.

Performing all other mortgage, home equity and consumer loans.

The following table presents the credit risk profile of the Company's commercial, commercial real estate, and finance leases loan portfolios based on internal rating category as of December 31, 2023 and 2022:

	Commercial and Industrial		Commercial Real Estate		Finance Leases	
	2023	2022	2023	2022	2023	2022
Grade						
Pass (1-6)	$ 549,963	$ 555,300	$ 585,239	$ 590,997	$ 4,210	$ 6,621
Watch (7)	28,218	26,867	29,814	27,954	-	-
Substandard (8)	5,285	4,716	17,194	1,382	-	-
Doubtful (9)	588	1,054	-	596	-	-
Loss (10)	-	-	-	-	-	-
Total	$ 584,054	$ 587,937	$ 632,247	$ 620,929	$ 4,210	$ 6,621

The following table presents the credit risk profile of the Company's residential real estate, home equity lines of credit, and consumer loan portfolios based on internal rating category as of December 31, 2023 and 2022:

	Consumer - Home Equity Lines of Credit		Consumer - Auto		Consumer - Other		Residential	
	2023	2022	2023	2022	2023	2022	2023	2022
Performing	$ 83,974	$ 76,884	$ 11,994	$ 13,279	$ 12,772	$ 14,312	$ 310,055	$ 278,641
Nonperforming	109	71	4	-	-	-	127	195
	$ 84,083	$ 76,955	$ 11,998	$ 13,279	$ 12,772	$ 14,312	$ 310,182	$ 278,836

(Table Dollars in Thousands Except Share Data)

The following tables present the Company's loan portfolio aging analysis of the recorded investment in loans as of December 31, 2023 and 2022:

2023

	30-59 Days Past Due	60-89 Days Past Due	Greater than 90 Days	Total Past Due	Current	Total Loans
Commercial and industrial	$ 712	$ 163	$ 2,448	$ 3,323	$ 580,731	$ 584,054
Commercial real estate	-	-	-	-	632,247	632,247
Consumer						
Consumer, home equity lines of credit	-	54	70	124	83,959	84,083
Consumer, auto	10	-	4	14	11,984	11,998
Consumer, other	4	-	-	4	12,768	12,772
Residential	256	-	13	269	309,913	310,182
Finance leases	-	-	-	-	4,210	4,210
Total	$ 982	$ 217	$ 2,535	$ 3,734	$ 1,635,812	$ 1,639,546

2022

	30-59 Days Past Due	60-89 Days Past Due	Greater than 90 Days	Total Past Due	Current	Total Loans	Total Loans > 90 Days and Accruing
Commercial and industrial	$ 324	$ -	$ 1,103	$ 1,427	$ 586,510	$ 587,937	$ 78
Commercial real estate	596	-	-	596	620,333	620,929	-
Consumer							
Consumer, home equity lines of credit	144	78	22	244	76,711	76,955	22
Consumer, auto	-	-	-	-	13,279	13,279	-
Consumer, other	25	-	-	25	14,287	14,312	-
Residential	104	116	22	242	278,594	278,836	-
Finance leases	-	-	-	-	6,621	6,621	-
Total	$ 1,193	$ 194	$ 1,147	$ 2,534	$ 1,596,335	$ 1,598,869	$ 100

Prior to adoption of ASC 326, a loan was considered impaired, in accordance with the impairment accounting guidance (ASC 310-10-35-16), 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 nonperforming commercial loans but also include loans modified in accordance with ASC 310-20-35.

(Table Dollars in Thousands Except Share Data)

The following table presents impaired loans for the year ended December 31, 2022:

	2022					
	Recorded Balance	Unpaid Principal Balance	Specific Allowance	Average Investment in Impaired Loans	Interest Income Recognized	Interest Income Recognized on Cash Basis
Loans without a specific valuation allowance:						
Commercial and industrial	$ 3,482	$ 3,487	$ -	$ 4,514	$ 183	$ 180
Commercial real estate	596	667	-	936	24	21
Loans with a specific valuation allowance:						
Commercial and industrial	1,648	1,736	1,050	1,727	81	41
Total impaired loans	$ 5,726	$ 5,890	$ 1,050	$ 7,177	$ 288	$ 242

The following table presents the Company's nonaccrual loans at December 31, 2023:

	2023		
	Nonaccrual with No ACL	Nonaccrual	Loan Past Due Over 89 Days and Still Accruing
Commercial and industrial	$ -	$ 3,793	$ -
Commercial real estate	-	-	-
Consumer			-
Consumer, home equity lines of credit	-	109	-
Consumer, auto	-	-	4
Consumer, other	-	-	-
Residential	-	127	-
Finance leases	-	-	-
	$ -	$ 4,029	$ 4

The following table presents the Company's nonaccrual loans at December 31, 2022. This table excludes performing troubled debt modifications.

	2022
Commercial and industrial	$ 1,706
Commercial real estate	596
Consumer	
Consumer, home equity lines of credit	48
Consumer, auto	-
Consumer, other	-
Residential	195
Finance leases	-
Total	$ 2,545

(Table Dollars in Thousands Except Share Data)

The following table presents the amortized cost basis of collateral-dependent loans by class of loans as of December 31, 2023:

	Real Estate	General Business Assets	Other	Total
Commercial and industrial	$ 1,552	$ 2,498	$ 26	$ 4,076
Consumer				-
Consumer, home equity				-
lines of credit	63	-	-	63
Consumer, other	5	-	26	31
Residential	896	-	-	896
	$ 2,516	$ 2,498	$ 52	$ 5,066

The Company closely monitors the performance of loans that are modified to borrowers experiencing financial difficulty to understand the effectiveness of its modification efforts. The following table presents the performance of loans that have been modified in the last 12 months:

	2023		
	Current	30-89 Days Past Due	> 90 Days Past Due
Commercial and industrial	$ 26	$ -	$ -
Commercial real estate	-	-	-
Consumer			
Consumer, residential	-	-	-
	$ 26	$ -	$ -

There was not a material financial effect of the loan modifications presented above to borrowers experiencing financial difficulty for the year ended December 31, 2023.

The following table presents information regarding troubled debt modifications by class for the year ended December 31, 2022.

	Number of Loans	Pre-Modification Recorded Balance	Post-Modification Recorded Balance
December 31, 2022			
Commercial and industrial	$ 1	$ 391	$ 363
Consumer			
Consumer, residential	1	6	4
	$ 2	$ 397	$ 367

The troubled debt modifications described above did not materially increase the allowance for loan losses for the year ended December 31, 2022. The troubled debt modifications described above did not result in any charge offs during the year ended December 31, 2022.

(Table Dollars in Thousands Except Share Data)

Newly restructured loans by type of modification for the 12 months ended December 31, 2022:

	2022			
	Interest Only	Term	Combination	Total Modification
Commercial and industrial	$ -	$ -	$ 363	$ 363
Consumer				
Consumer, residential	-	-	-	4
	$ -	$ -	$ 363	$ 367

There were no loans that had a payment default during the year ended December 31, 2023 and were modified in the twelve months prior to that default to borrowers experiencing financial difficulties.

The Company had no foreclosed residential real estate property obtained by physical possession as of December 31, 2023 and 2022. The Company had no consumer mortgage loans secured by residential real estate properties for which foreclosure proceedings are in process according to local jurisdictions as of December 31, 2023 and 2022.

Note 4: Premises and Equipment

Premises and equipment as of December 31 are summarized as follows:

	2023	2022
Land	$ 18,986	$ 18,756
Buildings and improvements	37,479	37,480
Furniture and equipment	45,921	37,223
Construction in progress	34,819	26,864
	137,205	120,323
Less accumulated depreciation	(57,021)	(54,282)
Net premises and equipment	$ 80,184	$ 66,041

Note 5: Mortgage Servicing

Mortgage loans serviced for others are not included in the accompanying consolidated balance sheets. The unpaid principal balances of mortgage loans serviced for others were approximately $279,131,000 and $299,663,000 at December 31, 2023 and 2022, respectively.

Custodial escrow balances maintained in connection with the foregoing loan servicing, and included in other liabilities, were approximately $1,410,000 and $1,383,000 at December 31, 2023 and 2022, respectively.

Mortgage servicing rights are included in other assets in the accompanying consolidated balance sheets. Comparable market values and a valuation model that calculates the present value of future cash flows were used to estimate fair value.

(Table Dollars in Thousands Except Share Data)

Activity in the balance of servicing assets was as follows:

	2023	2022
Carrying amount, beginning of year	$ 1,505	$ 1,534
Servicing obligations that result from transfers of financial assets	120	317
Amortization	(271)	(354)
Change in valuation allowance	8	8
Carrying amount, end of year	$ 1,362	$ 1,505
Valuation allowance, beginning of year	(22)	(30)
Additions	15	11
Reductions	(7)	(3)
Valuation allowance, end of year	$ (14)	$ (22)
Fair value, beginning of year	$ 3,999	$ 2,573
Fair value, end of year	$ 3,916	$ 3,999

Note 6: Time Deposits

At December 31, the scheduled maturities of time deposits, including brokered deposits, are as follows:

2024	$ 204,135
2025	20,650
2026	2,858
2027	1,305
2028	48,885
Thereafter	349
	$ 278,182

Time deposits with balances of $250,000 or greater were approximately $45,373,000 and $11,885,000 at December 31, 2023 and 2022, respectively.

Included in time deposits at December 31, 2023 and 2022 were $18,461,000 and $16,288,000 respectively, of deposits which were obtained through the IntraFi Network. This service allows deposit customers to maintain fully insured balances in excess of the $250,000 FDIC insurance limit without the inconvenience of having multi-banking relationships. Under the reciprocal program that the Company is currently participating in, customers agree to allow the Company to place their deposits with other participating banks in the IntraFi Network program in insurable amounts under $250,000. In exchange, other banks in the program agree to place their deposits with the Company also in insurable amounts under $250,000.

Note 7: Long-Term Borrowings

As of December 31, 2023 and 2022, STAR had Federal Home Loan Bank of Indianapolis advances (advances) outstanding totaling $175,000,000 and $245,013,000, respectively. The advances bear interest at rates ranging from 4.35% to 5.69% and mature at various dates through November 1, 2027.

Interest is paid monthly and the weighted average interest rate on the advances was 5.12% and 4.53% as of December 31, 2023 and 2022, respectively. The advances at December 31, 2023, are secured by first-mortgage loans totaling $407,424,000 and are subject to restrictions or penalties in the event of prepayment.

Maturities of long-term debt are as follows: 2024 - $100,000,000; 2025 - $25,000,000; 2026 - $25,000,000; and 2027 - $25,000,000.

The Company has established borrowing capacity of $999,913,200 and $1,003,076,400 as of December 31, 2023 and 2022, respectively, with the Federal Home Loan Bank and other financial institutions, of which $175,000,000 and $245,013,000 was outstanding at December 31, 2023 and 2022, respectively. In addition to the other borrowings, the Company also had $1,000,000 and $1,000,000 letters of credit available as of December 31, 2023 and 2022, respectively.

Note 8: Junior Subordinated Debt and Subordinated Debt

In 2021, the Company privately placed $50 million in aggregate principal amount of fixed-to-floating rate subordinated notes due 2031 to certain qualified institutional buyers. The Notes will initially bear interest at 3.25% per year, payable semi-annually in arrears. Beginning October 1, 2026 through the maturity date or earlier redemption, the interest rate will reset quarterly based on the then current Three-Month Term SOFR plus 257 basis points, payable quarterly in arrears. Also beginning on October 1, 2026 through maturity, the Notes may be redeemed in whole or in part, at the Company's option. The Notes will mature on October 1, 2031.

In March 2006, the Company formed STAR Capital Trust I (Trust I) and STAR Capital Trust II (Trust II) which are both statutory business trusts. Trust I issued $5,155,000 of trust preferred capital securities as a participant in a pooled trust preferred securities offering. The Company issued subordinated debentures aggregating $5,155,000 to Trust I. The subordinated debentures are the sole assets of Trust I. The subordinated debentures and the trust preferred securities pay interest and dividends, respectively, on a quarterly basis. The subordinated debentures and trust preferred capital securities bear interest at a rate of three-month CME Term SOFR (5.65%) plus 1.40% (7.05%) and mature on June 30, 2036, and are non-callable for five years after issuance. The securities may be called at any quarterly interest date at par.

Trust II issued $5,155,000 of trust preferred capital securities as a participant in a pooled trust preferred securities offering. The Company issued subordinated debentures aggregating $5,155,000 to Trust II. The subordinated debentures are the sole assets of Trust II. The subordinated debentures and the trust preferred securities pay interest and dividends, respectively, on a quarterly basis. The subordinated debentures and trust preferred capital securities bear interest at a rate of three-month CME Term SOFR (5.65%) plus 1.40% (7.05%) and mature on June 30, 2036. The securities may be called at any quarterly interest date at par.

The trust preferred capital securities, subject to certain limitations, are included in Tier I Capital for regulatory purposes. Trust I and Trust II are not consolidated into the Company and as a result, the Company accounts for the investment in Trust I and Trust II as assets, the subordinated debentures as debt, and the interest paid/received thereon as interest expense/income.

Note 9: Stock Based Compensation

The Company's long-term incentive model was approved in 2020 and agreements with employees were entered into in January 2021. Issuance of stock vests over a period of three years. Restricted stock units (RSU) are either time vested or based on performance metrics achieved by the Company. The total compensation expense recognized for the long-term incentive plan was $360,000 and $711,000 for the years ended December 31, 2023 and 2022, respectively.

(Table Dollars in Thousands Except Share Data)

A summary of the status of the Company's nonvested restricted stock units as of December 31, 2023, and 2022, and changes during the periods then ended is presented below:

	Shares	Weighted Average Grant Date Fair Value
Nonvested at January 1, 2022	7,850	$ 72.00
Granted	8,159	85.00
Vested	(1,451)	72.00
Forfeited	-	-
Nonvested at December 31, 2022	14,558	$ 74.10
Granted	9,638	84.00
Vested	(2,843)	78.68
Forfeited	-	-
Nonvested at December 31, 2023	21,353	$ 81.49

The total unrecognized compensation was $777,000 and $350,000 for the years ended December 31, 2023 and 2022, respectively.

Note 10: Income Tax Expense

The Company files income tax returns in the U.S. federal jurisdiction and various states and local jurisdictions. With a few exceptions, the Company is no longer subject to U.S. federal, state and local or income tax examinations by tax authorities for years before 2020.

Income tax provision is summarized as follows:

	2023	2022
Current		
Federal	$ 4,861	$ 4,134
State	29	(60)
Deferred		
Federal	15	142
State	(435)	364
Total tax expense	$ 4,470	$ 4,580

(Table Dollars in Thousands Except Share Data)

A net deferred tax asset is included in other assets and is comprised of the following temporary differences at December 31:

	2023	2022
Deferred tax assets		
Allowance for credit losses	$ 5,413	$ 4,925
Other nondeductible accruals	1,511	1,493
Unrealized losses on available-for-sale securities	21,789	26,652
State net operating loss	398	-
Other-than-temporary impairment	309	309
Partnership investments	266	150
Deferred income	288	379
Other	329	223
	$ 30,303	$ 34,131
Deferred tax liabilities		
Mortgage servicing rights	$ (339)	$ (382)
Premises and equipment, including equipment leased to others	(1,513)	(2,159)
Prepaid expenses	(793)	(1,110)
Accretion	(1,357)	(627)
Deferred loan fees	(398)	(623)
Other	(155)	(72)
	$ (4,555)	$ (4,973)
Total net deferred taxes	$ 25,748	$ 29,158

A reconciliation of income tax expense at the statutory rate to the Company's actual income tax expense is as follows:

	2023	2022
Income taxes at statutory rate	$ 5,932	$ 5,809
State income taxes, net of federal benefit	(317)	353
Tax-exempt interest	(636)	(1,036)
Bank owned life insurance	(204)	(172)
Captive insurance income	(357)	(393)
Tax credits	(39)	(36)
Other, net	91	55
Net income tax expense	$ 4,470	$ 4,580

At December 31, 2023, the Company had a state net operating loss of $8,132, which carries forward for twenty years.

Note 11: Accumulated Other Comprehensive Loss

The components of accumulated other comprehensive loss, included in stockholders' equity, are as follows:

	2023	2022
Net unrealized loss on available-for-sale securities	$ (103,678)	$ (126,943)
Tax effect	21,710	26,658
Net-of-tax amount	$ (81,968)	$ (100,285)

(Table Dollars in Thousands Except Share Data)

Note 12: Employee Retirement and Savings Plans

STAR has a Section 401(k) savings plan for substantially all employees. The savings plan provides that STAR may contribute up to 50% of the amount of compensation deferred by the employee, up to 5%. STAR contributed $1,138,000 and $983,000 to the plans in 2023 and 2022, respectively.

Note 13: Related Party Transactions

The Bank has loan, deposit and other transactions with its directors and officers, and with organizations and individuals with which they are associated. In management's opinion, such loans and other extensions of credit were made in the ordinary course of business and were made on substantially the same terms (including interest rates and collateral) as those prevailing at the time for comparable transactions with other persons. Further, in management's opinion, these loans did not involve more than normal risk of collectability or present other unfavorable features. The aggregate dollar amount of loans to directors and executive officers who held office at the end of the year, and organizations and individuals with which they are associated, amounted to approximately $38,380,000 and $15,854,000 at December 31, 2023 and 2022, respectively. The aggregate dollar amount of deposits of directors and executive officers who held office at the end of the year, and organizations and individuals with which they are associated, amounted to approximately $8,456,000 and $11,209,000 at December 31, 2023 and 2022, respectively.

Note 14: Commitments and Contingencies

The Bank, in the normal course of business, is a party to various financial instruments with off-balance sheet risk to meet the financing needs of customers. These instruments involve elements of credit risk in excess of amounts recognized in the financial statements. The contract amounts of those instruments reflect the extent of involvement STAR has in financial instruments.

Financial instruments whose contract amounts represent credit risk at December 31:

	2023	2022
Commitments to extend credit	$ 810,729	$ 726,583
Standby letters of credit	9,986	10,680
Forward sale commitments	805	920

STAR's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and standby letters of credit is represented by the contractual amount of those instruments. STAR follows the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments.

Commitments to extend credit are agreements to loan funds to customers providing there is compliance with terms of the commitment. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Bank evaluates each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained if deemed necessary by the Bank upon extension of credit is based on management's credit evaluation of the customer. Collateral held varies but may include accounts receivable, inventory, plant and equipment and real estate.

Letters of credit are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. The Bank holds collateral supporting those commitments when deemed necessary.

Forward sale commitments are commitments to sell groups of residential mortgage loans that the Bank originates or purchases as part of its mortgage banking activities. The Bank commits to sell the loans at specified prices in a future period, typically within 90 days. These commitments are acquired to reduce market risk on mortgage loans in the process of origination and mortgage loans held for sale since the Bank is exposed to interest rate risk during the period between issuing a loan commitment and the sale of the loan into the secondary market.

Management does not expect any material losses to result from these financial instruments.

The Company and Bank are also subject to claims and lawsuits which 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 of the Company.

(Table Dollars in Thousands Except Share Data)

The Company is obligated under operating leases for certain office premises and equipment. The following table shows operating lease right of use assets and operating lease liabilities as of December 31, 2023 and 2022.

	2023	2022
Operating lease right of use assets	$ 4,434	$ 5,462
Operating lease liabilities	4,806	5,807

The following table shows the components of operating leases expenses for the years ended December 31, 2023 and 2022.

	2023	2022
Operating lease cost	$ 1,567	$ 1,960

The following table shows future minimum rental commitments for all non-cancellable operating leases with an initial term longer than 12 months for the next five years and thereafter.

2024	$ 1,176
2025	1,007
2026	557
2027	535
2028	518
Thereafter	2,011
Total lease payments	5,804
Less: imputed interest	(998)
Present value of operating lease liabilities	$ 4,806

The following table shows the weighted average remaining operating lease term, the weighted average discount rate and supplemental consolidated statement of cash flows information for operating leases at December 31, 2023 and 2022.

	2023	2022
Weighted average remaining lease term (years)	12.53	11.69
Weighted average discount rate	3.30%	3.18%

In early 2021, STAR announced plans to begin construction on their new headquarters which will be located in downtown Fort Wayne. Construction began in 2021 and is scheduled to be complete in the third quarter of 2024. The Company has entered into construction-related contracts in the amount of $37.7 million. The amount outstanding on the contract is $4,762,000 and $8,762,000 as of December 31, 2023 and 2022 respectively.

Note 15: Regulatory Matters

The Company and Bank are subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Company's and Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company and Bank must meet specific capital guidelines that involve quantitative measures of the Company's and Bank's assets, liabilities and certain off-balance sheet items as calculated under U.S. GAAP, regulatory reporting requirements and regulatory capital standards. The Company's and Bank's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings and other factors.

(Table Dollars in Thousands Except Share Data)

Quantitative measures established by regulatory capital standards to ensure capital adequacy require the Company and Bank to maintain minimum amounts and ratios (set forth in the following table) of Total and Tier 1 capital (as defined) to risk-weighted assets (as defined), common equity Tier I capital (as defined) to total risk-weighted assets (as defined) and of Tier 1 capital (as defined) to average assets (as defined).

As of December 31, 2023, the most recent notification received from federal banking agencies categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, the Bank must maintain minimum total risk-based capital, Tier I risk-based capital, common equity Tier I risk-based capital and Tier I leverage ratios as set forth in the following table. There are no conditions or events since that notification that management believes have changed the Bank's category.

STAR Bank's capital amounts and ratios are presented in the following table:

	Actual		Minimum Capital Requirement		Minimum to be Well Capitalized Under Prompt Corrective Actions Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2023						
Total capital (to risk weighted assets)						
STAR Financial Bank	$ 326,123	13.18%	$ 197,903	8.00%	$ 247,379	10.00%
Tier I capital (to risk weighted assets)						
STAR Financial Bank	304,674	12.32	148,427	6.00	197,903	8.00
Tier 1 capital (to average assets)						
STAR Financial Bank	304,674	9.73	125,308	4.00	156,635	5.00
Common equity Tier I capital						
STAR Financial Bank	304,674	12.32	111,320	4.50	160,796	6.50

	Actual		Minimum Capital Requirement		Minimum to be Well Capitalized Under Prompt Corrective Actions Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2022						
Total capital (to risk weighted assets)						
STAR Financial Bank	$ 297,490	13.89%	$ 171,325	8.00%	$ 214,156	10.00%
Tier I capital (to risk weighted assets)						
STAR Financial Bank	278,371	13.00	128,494	6.00	171,325	8.00
Tier 1 capital (to average assets)						
STAR Financial Bank	278,371	9.03	123,317	4.00	154,147	5.00
Common equity Tier I capital						
STAR Financial Bank	278,371	13.00	96,370	4.50	139,202	6.50

(Table Dollars in Thousands Except Share Data)

Banking regulations limit the amount that the Bank may pay the Company without prior approval of bank regulatory authorities. At December 31, 2023, retained earnings available for dividends to the Company without such approval totaled approximately $67,565,000.

Note 16: Disclosures About Fair Value of Assets and Liabilities

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value measurements must maximize the use of observable inputs and minimize the use of unobservable inputs. There is a hierarchy of three levels of inputs that may be used to measure fair value:

Level 1 Quoted prices in active markets for identical assets or liabilities

Level 2 Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities

Level 3 Unobservable inputs supported by little or no market activity and are significant to the fair value of the assets or liabilities

Recurring Measurements

The following tables present the fair value measurements of assets and liabilities recognized in the accompanying balance sheets measured at fair value on a recurring basis and the level within the fair value hierarchy in which the fair value measurements fall at December 31, 2023 and 2022:

	2023			
		Fair Value Measurements Using		
	Fair Value	Quoted Prices in Active Markets for Identical Assets Level 1	Significant Other Observable Inputs Level 2	Significant Unobservable Inputs Level 3
Cash Equivalents				
Money market mutual funds	$ 114	$ 114	$ -	$ -
Available-for-Sale Securities				
U.S. Treasury and agency securities	98,757	-	98,757	-
Obligations of states and political subdivisions	131,199	-	131,199	-
Mortgage-backed GSE residential	812,195	-	812,195	-
Pooled trust preferred securities	23,056	-	23,056	-

(Table Dollars in Thousands Except Share Data)

	2022			
		Fair Value Measurements Using		
	Fair Value	Quoted Prices in Active Markets for Identical Assets Level 1	Significant Other Observable Inputs Level 2	Significant Unobservable Inputs Level 3
Cash Equivalents				
Money market mutual funds	$ 14,775	$ 14,775	$ -	$ -
Available-for-Sale Securities				
U.S. Treasury and agency securities	99,523	-	99,523	-
Obligations of states and political subdivisions	205,888	-	205,888	-
Mortgage-backed GSE residential	818,145	-	818,145	-
Pooled trust preferred securities	13,016	-	13,016	-

Following is a description of the valuation methodologies used for assets and liabilities measured at fair value on a recurring basis and recognized in the accompanying consolidated balance sheets, as well as the general classification of such assets and liabilities pursuant to the valuation hierarchy. There have been no significant changes in the valuation techniques during the year ended December 31, 2023. For assets and liabilities classified within Level 3 of the fair value hierarchy, the process used to develop the reported fair value is described below.

Cash Equivalents

Where quoted market prices are available in an active market, cash equivalents are classified within Level 1 of the valuation hierarchy and include only money market mutual funds. The Company had no cash equivalents classified as Level 2 or Level 3.

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, then fair values are estimated by a third-party pricing service using pricing models, quoted market prices of securities with similar characteristics or discounted cash flows. The inputs used by the pricing service to determine fair value may include one, or a combination of, observable inputs such as benchmark yields, reported trades, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers and reference data market research publications and are classified within Level 2 of the valuation hierarchy. These level 2 securities include U.S. Treasury and agency securities, obligations of state and political subdivisions, pooled trust preferred securities, and mortgage-backed GSE residential securities. In certain cases where Level 1 or Level 2 inputs are not available, securities are classified within Level 3 of the hierarchy.

Fair value determinations for Level 3 measurements of securities are the responsibility of the Finance department. The Finance department contracts with a pricing specialist to generate fair value estimates on a monthly or quarterly basis. The Finance department challenges the reasonableness of the assumptions used and reviews the methodology to ensure the estimated fair value complies with accounting standards generally accepted in the United States.

Nonrecurring Measurements

The following table presents the fair value measurement of assets measured at fair value on a nonrecurring basis and the level within the fair value hierarchy in which the fair value measurements fall at December 31, 2023 and 2022.

	2023			
		Fair Value Measurements Using		
	Fair Value	Quoted Prices in Active Markets for Identical Assets Level 1	Significant Other Observable Inputs Level 2	Significant Unobservable Inputs Level 3
Collateral Dependent Loans	$ 5,066	$ -	$ -	$ 5,066

	2022			
		Fair Value Measurements Using		
	Fair Value	Quoted Prices in Active Markets for Identical Assets Level 1	Significant Other Observable Inputs Level 2	Significant Unobservable Inputs Level 3
Collateral Dependent Loans	$ 597	$ -	$ -	$ 597

Following is a description of the valuation methodologies used for assets measured at fair value on a nonrecurring basis and recognized in the accompanying consolidated balance sheets, as well as the general classification of such assets pursuant to the valuation hierarchy. The Company has no liabilities measured at fair value on a nonrecurring basis.

Collateral Dependent Loans

Loans for which it is probable that the Company will not collect all principal and interest due according to contractual terms are individually evaluated. An allowable method for determining the amount of expected credit loss includes estimating fair value using the fair value of the collateral for collateral dependent loans. If the individually evaluated loan is identified as collateral dependent, then the fair value method of measuring the amount of expected credit loss is utilized. This method requires obtaining a current independent appraisal of the collateral and applying a discount factor to the value. Loans that are collateral dependent are classified within Level 3 of the fair value hierarchy when the estimated expected credit loss is determined using the fair value method.

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 the Managed Assets department and Asset Quality Committee. Appraisals are reviewed for accuracy and consistency by the Loan Review department. Appraisers are selected from the list of approved appraisers maintained by management. The appraised values are reduced by discounts to consider lack of marketability and 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 the Loan Review department by comparison to historical results.

(Table Dollars in Thousands Except Share Data)

Unobservable (Level 3) Inputs

The following tables present quantitative information about unobservable inputs used in recurring and nonrecurring Level 3 fair value measurements as of December 31, 2023 and 2022.

	Fair Value at December 31, 2023	Valuation Technique	Unobservable Inputs	Range (Weighted Average)
Collateral Dependent Loans	$ 5,066	Market comparable properties	Marketability discount	65.43% - 100% (12.08%)

	Fair Value at December 31, 2022	Valuation Technique	Unobservable Inputs	Range (Weighted Average)
Collateral Dependent Loans	$ 597	Market comparable properties	Marketability discount	31.93% - 91.73% (63.74%)

Sensitivity of Significant Unobservable Inputs

The following is a discussion of the sensitivity of significant unobservable inputs, the interrelationship between those inputs and other unobservable inputs used in recurring fair value measurement and of how those inputs might magnify or mitigate the effect of changes in the unobservable inputs on the fair value measurement.

(Table Dollars in Thousands Except Share Data)

Fair Value of Financial Instruments

The following table presents estimated fair values of the Company's financial instruments at December 31, 2023 and 2022.

	Carrying Amount	Fair Value	Level 1	Level 2	Level 3
December 31, 2023					
Financial assets					
Cash and cash equivalents	$ 113,715	$ 113,715	$ 113,715	$ -	$ -
Loans held for sale	249	257	-	257	-
Loans and leases, net	1,620,344	1,557,345	-	-	1,557,345
Interest receivable	11,328	11,328	-	11,328	-
Federal Home Loan Bank stock	11,071	11,071	-	11,071	-
Financial liabilities					
Demand deposits	2,267,832	2,267,832	2,267,832	-	-
Time deposits	278,182	260,753	-	260,753	-
Long-term borrowings	175,000	176,479	-	176,479	-
Subordinated debt	60,310	43,720	-	43,720	-
Interest payable	1,449	1,449	-	1,449	-
December 31, 2022					
Financial assets					
Cash and cash equivalents	$ 105,105	$ 105,105	$ 105,105	$ -	$ -
Loans held for sale	422	426	-	426	-
Loans and leases, net	1,579,750	1,489,023	-	-	1,489,023
Interest receivable	11,249	11,249	-	11,249	-
Federal Home Loan Bank stock	11,071	11,071	-	11,071	-
Financial liabilities					
Demand deposits	2,410,512	2,410,512	2,410,512	-	-
Time deposits	113,295	91,692	-	91,692	-
Long-term borrowings	245,013	245,679	-	245,679	-
Subordinated debt	60,310	45,615	-	45,615	-
Interest payable	887	887	-	887	-

The following methods were used to estimate the fair value of all other financial instruments recognized in the accompanying consolidated balance sheets at amounts other than fair value.

Cash and Cash Equivalents, Federal Home Loan Bank Stock, Interest Receivable and Interest Payable

The carrying amounts approximate fair value.

Loans Held for Sale

For homogeneous categories of loans, such as mortgage loans held for sale, fair value is estimated using the quoted market prices for securities backed by similar loans, adjusted for differences in loan characteristics.

(Table Dollars in Thousands Except Share Data)

Loans and Leases, net

Fair value is estimated by discounting the future cash flows using market rates for similar loans to similar borrowers. The market rates reflect a market participant assumption about risks associated with nonperformance, illiquidity, and the structure and term of the loans along with local economic and market conditions.

Deposit Liabilities

The fair values disclosed for demand deposits (*e.g.*, interest and noninterest checking, savings and money market accounts) are, by definition, equal to the amount payable on demand at the reporting date (*i.e.*, their carrying amounts). The carrying amounts for variable-rate, fixed-term time deposits approximate their fair values at the reporting date. Fair values for fixed-rate certificates of deposit are estimated using a discounted cash flow calculation that applies interest rates currently being offered on certificates to a schedule of aggregated expected monthly maturities on time deposits.

Long-Term Borrowings

Fair values for Federal Home Loan Bank and other borrowings are estimated using a discounted cash flow calculation that applies interest rates currently being offered for similar maturities.

Subordinated Debt

The fair value for subordinated debt is estimated using a discounted cash flow calculation that applies interest rates currently being offered for similar maturities.

Commitments to Originate Loans, Forward Sale Commitments, Letters of Credit and Lines of Credit

The fair value of commitments to originate loans is estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present creditworthiness of the counterparties. For fixed-rate loan commitments, fair value also considers the difference between current levels of interest rates and the committed rates. The fair value of forward sale commitments is estimated based on current market prices for loans of similar terms and credit quality. The fair values of letters of credit and lines of credit are based on fees currently charged for similar agreements or on the estimated cost to terminate or otherwise settle the obligations with the counterparties at the reporting date. The fair value of these items is not material.

Note 17: Earnings Per Share

The factors used in the Company's earnings per share computation are as follows:

	2023	2022
Net income	$ 23,863	$ 23,129
Weighted average shares outstanding	2,792,246	2,968,111
Add: Dilutive effects of restricted stock units	13,853	6,947
Average shares and dilutive potential shares	2,806,099	2,975,058
Basic earnings per share	$ 8.55	$ 7.79
Diluted earnings per share	$ 8.50	$ 7.77

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STAR Financial Group

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C. Robin Wright
Kevin A. Wright
Thomas W. Wright

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Kristin M. Marcuccilli, *President*
Thomas M. Marcuccilli, *Chairman*
Brian M. Miller, *Chief Financial Officer, Treasurer*
Thomas W. Wright, *Vice Chairman*

2024 Annual Meeting

The 2024 Annual Meeting of the Shareholders of STAR Financial Group occurs on May 22, 2024, at 10:00 a.m. at STAR Financial Group's Corporate Office: 215 W. Main Street, 6th Floor, Fort Wayne, Indiana.

STAR Financial Bank

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