

United Financial Bancorp, Inc.  
Form 10-Q  
August 08, 2012  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
**WASHINGTON, D.C. 20549**

**FORM 10-Q**

(Mark One)

**Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**  
**For the quarterly period ended June 30, 2012**

**OR**

**Transition report pursuant to section 13 or 15(d) of the Securities Exchange Act of 1934**  
**For the transition period from            to**

**Commission File Number 000-52947**

**United Financial Bancorp, Inc.**

**(Exact name of registrant as specified in its charter)**

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**Maryland**  
(State or other jurisdiction of  
incorporation or organization)

**74-3242562**  
(I.R.S. Employer

Identification Number)

**95 Elm Street, West Springfield, Massachusetts**  
(Address of principal executive offices)

**01089**  
Zip Code

Registrant's telephone number, including area code: **(413) 787-1700**

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No .

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

Large accelerated filer  Accelerated filer

Non-accelerated filer  (Do not check if a smaller reporting company) Smaller reporting company

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

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

**Common stock, \$0.01 par value**

**15,517,924 shares outstanding as of August 1, 2012**

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**Table of Contents****PART I. FINANCIAL INFORMATION****ITEM 1. Financial Statements****UNITED FINANCIAL BANCORP, INC. AND SUBSIDIARY****CONSOLIDATED STATEMENTS OF CONDITION (unaudited)**

(Dollars in thousands, except per share amounts)

	<b>June 30, 2012</b>	<b>December 31, 2011</b>
<b>ASSETS</b>		
Cash and due from banks	\$ 21,652	\$ 20,112
Interest-bearing deposits	20,755	41,406
Total cash and cash equivalents	42,407	61,518
Securities available for sale, at fair value	243,897	221,813
Securities held to maturity, at amortized cost (fair value of \$102,290 at June 30, 2012 and \$118,311 at December 31, 2011)	99,421	115,897
Loans held for sale	835	53
Loans, net of allowance for loan losses of \$11,751 at June 30, 2012 and \$11,132 at December 31, 2011	1,152,889	1,112,941
Other real estate owned	2,397	2,054
Accrued interest receivable	4,603	4,846
Deferred tax asset, net	14,221	14,006
Stock in the Federal Home Loan Bank of Boston	14,454	15,365
Banking premises and equipment, net	17,638	16,438
Bank-owned life insurance	41,469	40,688
Goodwill	8,192	8,192
Other assets	11,203	9,941
<b>TOTAL ASSETS</b>	<b>\$ 1,653,626</b>	<b>\$ 1,623,752</b>

**LIABILITIES AND STOCKHOLDERS EQUITY**

## Liabilities:

## Deposits:

Interest-bearing	\$ 1,032,118	\$ 1,024,073
Non-interest-bearing	228,495	205,902
Total deposits	1,260,613	1,229,975
Short-term borrowings	17,772	17,260
Long-term debt	125,025	126,857
Subordinated debentures	5,585	5,539
Escrow funds held for borrowers	1,804	2,103
Capitalized lease obligations	4,794	4,874
Accrued expenses and other liabilities	9,904	9,783

Total liabilities	1,425,497	1,396,391
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## Stockholders equity:

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Preferred stock, par value \$0.01 per share, authorized 50,000,000 shares; none issued		
Common stock, par value \$0.01 per share, authorized 100,000,000 shares; 18,706,933 shares issued and outstanding at June 30, 2012 and December 31, 2011	187	187
Paid-in capital	183,077	182,433
Retained earnings	91,836	89,019
Unearned compensation	(9,695)	(10,047)
Treasury stock, at cost (3,186,409 shares at June 30, 2012 and 2,994,036 shares at December 31, 2011)	(44,051)	(40,983)
Accumulated other comprehensive income, net of taxes	6,775	6,752
<b>Total stockholders' equity</b>	<b>228,129</b>	<b>227,361</b>
<b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>	<b>\$ 1,653,626</b>	<b>\$ 1,623,752</b>

See notes to unaudited consolidated financial statements

**Table of Contents****UNITED FINANCIAL BANCORP, INC. AND SUBSIDIARY****CONSOLIDATED STATEMENTS OF EARNINGS (unaudited)**

(Dollars in thousands, except per share amounts)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
<b>Interest and dividend income:</b>				
Loans	\$ 14,181	\$ 14,703	\$ 28,256	\$ 29,190
Investments	2,767	3,387	5,622	6,578
Other interest-earning assets	51	38	92	78
<b>Total interest and dividend income</b>	<b>16,999</b>	<b>18,128</b>	<b>33,970</b>	<b>35,846</b>
<b>Interest expense:</b>				
Deposits	2,598	3,194	5,351	6,491
Short-term borrowings	13	30	33	67
Long-term debt	1,094	1,522	2,192	3,115
<b>Total interest expense</b>	<b>3,705</b>	<b>4,746</b>	<b>7,576</b>	<b>9,673</b>
<b>Net interest income before provision for loan losses</b>	<b>13,294</b>	<b>13,382</b>	<b>26,394</b>	<b>26,173</b>
Provision for loan losses	750	673	1,400	1,481
<b>Net interest income after provision for loan losses</b>	<b>12,544</b>	<b>12,709</b>	<b>24,994</b>	<b>24,692</b>
<b>Non-interest income:</b>				
Fee income on depositors' accounts	1,529	1,373	2,937	2,665
Wealth management income	289	214	516	454
Income from bank-owned life insurance	436	393	876	724
Net gain on sale of loans	162	50	270	73
Net gain on sale of securities				1
Impairment charges on securities		(59)		(59)
Other income	154	240	544	502
<b>Total non-interest income</b>	<b>2,570</b>	<b>2,211</b>	<b>5,143</b>	<b>4,360</b>
<b>Non-interest expense:</b>				
Salaries and benefits	6,286	6,414	12,728	12,683
Occupancy expenses	870	805	1,744	1,649
Marketing expenses	501	635	941	1,082
Data processing expenses	1,011	984	2,031	1,972
Professional fees	404	407	910	1,068
Acquisition related expenses	592		592	
FDIC insurance assessments	267	244	536	574
Low income housing tax credit fund		197	243	395
Other expenses	1,537	1,717	3,018	2,920

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Total non-interest expense	11,468	11,403	22,743	22,343
Income before income taxes	3,646	3,517	7,394	6,709
Income tax expense	1,064	827	1,963	1,590
Net income	\$ 2,582	\$ 2,690	\$ 5,431	\$ 5,119
Earnings per share:				
Basic	\$ 0.18	\$ 0.18	\$ 0.37	\$ 0.34
Diluted	\$ 0.17	\$ 0.18	\$ 0.36	\$ 0.33
Weighted average shares outstanding:				
Basic	14,542,642	15,028,468	14,606,624	15,022,249
Diluted	14,787,690	15,309,156	14,887,361	15,285,246
Dividends paid per share	\$ 0.09	\$ 0.08	\$ 0.18	\$ 0.16

See notes to unaudited consolidated financial statements.

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## CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (unaudited)

(In thousands)

The components of comprehensive income and related tax effects are as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Net Income	\$ 2,582	\$ 2,690	\$ 5,431	\$ 5,119
Other comprehensive income:				
Unrealized gains on securities:				
Unrealized holding gains on available-for-sale securities	374	2,181	39	1,628
Reclassification adjustment for gains realized in income				(1)
Net change in unrealized gains	374	2,181	39	1,627
Tax effect	(148)	(854)	(16)	(646)
Net of tax amount	226	1,327	23	981
Comprehensive income	\$ 2,808	\$ 4,017	\$ 5,454	\$ 6,100

See notes to unaudited consolidated financial statements.



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## CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY (unaudited)

FOR THE SIX MONTHS ENDED JUNE 30, 2012 and 2011

(Dollars in thousands, except per share amounts)

	Common Shares Outstanding	Common Stock	Paid-In Capital	Retained Earnings	Unearned Compensation	Treasury Stock	Accumulated Other Comprehensive Income	Total
Balances at December 31, 2010	16,109,106	\$ 187	\$ 180,322	\$ 82,899	\$ (10,750)	\$ (34,940)	\$ 4,858	\$ 222,576
Net income				5,119				5,119
Other comprehensive income							981	981
Cash dividends paid (\$0.16 per share)				(2,400)				(2,400)
Treasury stock purchases	(13,896)					(195)		(195)
Shares repurchased in connection with restricted stock forfeited for tax purposes	(11,336)					(170)		(170)
Restricted shares forfeited	(10,910)		181			(181)		
Excess tax benefit on stock compensation plans			50					50
Cancellation of shares for tax withholdings on options exercised			(22)					(22)
Reissuance of treasury shares in connection with stock options exercised	16,514					200		200
Reissuance of treasury shares in connection with restricted stock grants	9,997		(158)			158		
Stock-based compensation			1,069					1,069
ESOP shares committed to be released			212		345			557
Balances at June 30, 2011	16,099,475	\$ 187	\$ 181,654	\$ 85,618	\$ (10,405)	\$ (35,128)	\$ 5,839	\$ 227,765
Balances at December 31, 2011	15,712,897	\$ 187	\$ 182,433	\$ 89,019	\$ (10,047)	\$ (40,983)	\$ 6,752	\$ 227,361
Net income				5,431				5,431
Other comprehensive income							23	23
Cash dividends paid (\$0.18 per share)				(2,628)				(2,628)
Treasury stock purchases	(199,400)					(3,166)		(3,166)
Shares repurchased in connection with restricted stock forfeited for tax purposes	(10,834)					(148)		(148)
Restricted shares forfeited	(10,000)		137			(137)		
Excess tax benefit on stock compensation plans			29					29
			(88)					(88)

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Cancellation of shares for tax withholdings on options exercised									
Reissuance of treasury shares in connection with stock options exercised	15,361		(156)	(10)		211			45
Reissuance of treasury shares in connection with restricted stock grants	12,500		(196)	24		172			
Stock-based compensation			712						712
ESOP shares committed to be released			206		352				558
Balances at June 30, 2012	15,520,524	\$ 187	\$ 183,077	\$ 91,836	\$ (9,695)	\$ (44,051)	\$ 6,775		\$ 228,129

See notes to unaudited consolidated financial statements.

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## CONSOLIDATED STATEMENTS OF CASH FLOWS (unaudited)

FOR THE SIX MONTHS ENDED JUNE 30, 2012 and 2011

(Dollars in thousands)

	2012	2011
<b>Cash flows from operating activities:</b>		
Net income	\$ 5,431	\$ 5,119
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	1,400	1,481
ESOP expense	558	557
Stock-based compensation	712	1,069
Excess tax benefits on stock compensation plan	(29)	(50)
Amortization of premiums and discounts	935	697
Depreciation and amortization	808	494
Amortization of intangible assets	46	50
Net loss on sale and write down of other real estate owned	69	21
Impairment charges on securities		59
Net gain on sale/call of available for sale securities		(1)
Loans originated for sale	(10,396)	(4,516)
Proceeds from sales of loans held for sale	9,884	4,247
Net gain on sale of loans	(270)	(73)
Deferred tax benefit	(215)	(646)
Net increase in cash surrender value of bank-owned life insurance	(781)	(724)
Decrease (increase) in accrued interest receivable	243	(129)
Increase in other assets	(1,324)	(3,421)
Increase (decrease) in accrued expenses and other liabilities	867	(312)
Net cash provided by operating activities	7,938	3,922
<b>Cash flows from investing activities:</b>		
Purchases of securities available for sale	(51,636)	(69,491)
Proceeds from maturities, calls and principal repayments of securities available for sale	29,292	32,897
Purchases of securities held to maturity	(125)	
Proceeds from maturities, calls and principal repayments of securities held to maturity	15,965	11,100
Redemption of Federal Home Loan Bank of Boston stock	911	
Proceeds from sales of other real estate owned	1,096	732
Net loan originations, purchases and principal repayments	(42,856)	(32,077)
Purchases of property and equipment	(2,001)	(1,180)
Cash paid for merger related expenses	(592)	
Purchases of bank-owned life insurance		(9,928)
Net cash used in investing activities	(49,946)	(67,947)

(Continued)



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## CONSOLIDATED STATEMENTS OF CASH FLOWS (unaudited)

FOR THE SIX MONTHS ENDED JUNE 30, 2012 and 2011 (Concluded)

(Dollars in thousands)

	2012	2011
<b>Cash flows from financing activities:</b>		
Net increase in deposits	\$ 30,638	\$ 45,969
Net change in short-term borrowings	512	(4,327)
Net change in long-term debt	(1,786)	(18,488)
Net decrease in escrow funds held for borrowers	(299)	(6)
Payments on capitalized lease obligations	(212)	(203)
Excess tax benefits on stock compensation plan	29	50
Cancellation of shares for tax withholdings on options exercised	(88)	(22)
Reissuance of treasury shares in connection with stock options exercised	45	
Reissuance of treasury shares in connection with restricted stock warrants		200
Treasury stock purchases	(3,314)	(365)
Cash dividends paid	(2,628)	(2,400)
<b>Net cash provided by financing activities</b>	<b>22,897</b>	<b>20,408</b>
Decrease in cash and cash equivalents	(19,111)	(43,617)
Cash and cash equivalents at beginning of period	61,518	83,069
Cash and cash equivalents at end of period	\$ 42,407	\$ 39,452
<b>Supplemental Disclosure of Cash Flow Information:</b>		
Cash paid during the period:		
Interest on deposits, borrowings and other interest bearing liabilities	\$ 7,864	\$ 10,048
Income taxes net	5,267	4,628
Non-cash items:		
Transfer of loans to other real estate owned	1,508	2,075
Trade date accounting for securities purchased		(3,002)

See notes to unaudited consolidated financial statements.

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**UNITED FINANCIAL BANCORP, INC. AND SUBSIDIARY**

**NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS**

**JUNE 30, 2012**

**Dollars in Thousands (except per share amounts)**

**NOTE A BASIS OF PRESENTATION**

The consolidated financial statements include the accounts of United Financial Bancorp, Inc. ( United Financial ) its wholly-owned subsidiary, United Bank (the Bank ) and the Bank s wholly-owned subsidiaries, UCB Securities, Inc. and UCB Securities, Inc. II, which are engaged in buying, selling and holding investment securities, and UB Properties, LLC, which was formed to hold real estate assets acquired through foreclosure. All significant intercompany accounts and transactions have been eliminated in consolidation. These entities are collectively referred to herein as the Company .

The accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ( GAAP ) and with general practices within the banking industry. In the opinion of management, the accompanying unaudited interim consolidated financial statements reflect all adjustments, consisting of normal recurring adjustments, which are necessary for the fair presentation of the Company s financial condition as of June 30, 2012 and the results of operations for the three and six months ended June 30, 2012 and 2011. The interim results of operations presented herein are not necessarily indicative of the results to be expected for the entire year or any other period. These financial statements should be read in conjunction with the consolidated financial statements and the notes thereto for the year ended December 31, 2011 included in the Company s Annual Report on Form 10-K, which was filed with the Securities and Exchange Commission on March 12, 2012.

**NOTE B PENDING ACQUISITION**

On May 30, 2012, United Financial entered into a definitive agreement with New England Bancshares, Inc. ( NEBS ), the holding company for New England Bank, pursuant to which NEBS will merge with and into the Company. Concurrent with the merger, it is expected that New England Bank will merge with and into United Bank. Under the terms of the merger agreement, at the effective time of the merger, each share of NEBS common stock will be converted into the right to receive 0.9575 of a share of Company common stock. The consideration received by New England Bancshares stockholders is intended to qualify as tax-free.

The transaction is subject to customary closing conditions, including the receipt of regulatory approvals and approval of the merger by shareholders of the Company and NEBS. The Merger Agreement contains provisions that provide for the termination of the Merger Agreement in certain circumstances, and such provisions may require New England Bancshares to pay the Company a termination fee of \$3.2 million. Currently, the merger is expected to be completed in the fourth quarter of 2012.

A Form 8-K was filed with the Securities and Exchange Commission (the SEC ) by United Financial on May 31, 2012 which contains additional information regarding the merger.

**NOTE C RECENT ACCOUNTING PRONOUNCEMENTS**

In May 2011, the Financial Accounting Standards Board ( FASB ) issued Accounting Standards Update ( ASU ) 2011-04, *Fair Value Measurement (Topic 820), Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRS*. The guidance clarifies and expands the disclosures pertaining to unobservable inputs used in Level 3 fair value measurements, including the disclosure of quantitative information related to (1) the valuation processes used, (2) the sensitivity of the fair value measurement to changes in unobservable inputs and the interrelationships between those unobservable inputs, and (3) use of a nonfinancial asset in a way that differs from the asset s highest and best use. The guidance also requires disclosure of the level within the fair value hierarchy for assets and liabilities not measured at fair value in the statement of financial position but for which the fair value is disclosed. The amendments in this Update are to be applied prospectively, effective during interim and annual periods beginning after December 15, 2011. Early application is not permitted. This

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ASU was adopted in the first quarter of 2012 and did not have an impact on the Company's consolidated financial statements as the amendments relate only to changes in financial statement presentation.

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In June 2011, the FASB issued ASU 2011-05, Comprehensive Income (Topic 220), *Presentation of Comprehensive Income*. This ASU amends the disclosure requirements for the presentation of comprehensive income. The amended guidance eliminates the option to present components of other comprehensive income (OCI) as part of the statement of changes in stockholder's equity. Under the amended guidance, all changes in OCI are to be presented either in a single continuous statement of comprehensive income or in two separate but consecutive financial statements. The changes are effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. Early application is permitted. In December 2011, the FASB issued ASU 2011-12 to defer changes that relate to the presentation of reclassification adjustments but the other requirements of ASU 2011-05 remain in effect. This ASU was adopted in the first quarter of 2012 and did not have an impact to the consolidated financial results as the amendments relate only to changes in financial statement presentation.

In September 2011, the FASB issued ASU 2011-08, Intangibles—Goodwill and Other (Topic 350), *Testing Goodwill for Impairment*. This ASU is intended to reduce the complexity and cost of performing an evaluation of impairment of goodwill. Under the new guidance, an entity will have the option of first assessing qualitative factors (events and circumstances) to determine whether it is more likely than not (meaning a likelihood of more than 50 percent) that the fair value of a reporting unit is less than its carrying amount. If, after considering all relevant events and circumstances, an entity determines it is not more likely than not that the fair value of a reporting unit is less than its carrying amount, then performing the two-step impairment test will be unnecessary. This ASU was adopted in the first quarter of 2012 and did not have an impact on the Company's consolidated financial statements.

## **NOTE D CRITICAL ACCOUNTING POLICIES**

The SEC defines critical accounting policies as those that require application of management's most difficult, subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain and may change in future periods. Management believes that the following policies would be considered critical under the SEC's definition:

***Allowance for Loan Losses.*** The allowance for loan losses is the amount estimated by management as necessary to cover credit losses inherent in the loan portfolio at the balance sheet date. The allowance is established through the provision for loan losses which is charged against income. The methodology for determining the allowance for loan losses is considered a critical accounting policy by management due to the high degree of judgment involved, the subjectivity of the assumptions utilized and the potential for changes in the economic environment that could result in adjustments to the amount of the recorded allowance for loan losses.

Management performs a quarterly evaluation of the adequacy of the allowance for loan losses. We consider a variety of factors in establishing this estimate including, but not limited to, prior loss experience, current economic conditions, trends in non-performing, classified and impaired loans, charge-offs and delinquency rates, the adequacy of the underlying collateral, the size and composition of the loan portfolio, the financial strength of the borrower, results of internal loan reviews and other relevant factors. This evaluation is inherently subjective as it requires material estimates by management that may be susceptible to significant change based on changes in economic and real estate market conditions.

A loan is considered impaired 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 determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired.



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The Company periodically may agree to modify the contractual terms of loans. A loan is classified as a troubled debt restructure ( TDR ) if the Company grants a concession to a borrower that is experiencing financial difficulties. This usually includes a modification of loan terms, such as a reduction of the interest rate to below market terms, capitalizing past due interest, extending the maturity date or a partial forgiveness of debt. A TDR loan is returned to accrual status after the borrower demonstrates the ability to pay under the restructured terms through a sustained period of repayment performance, which is generally six months. All TDRs are initially classified as impaired.

The allowance consists of a specific, general, and unallocated component, as further described below.

**Specific component.** The specific component relates to loans that are classified as impaired. Impairment is measured on a loan by loan basis for the commercial segments (commercial and industrial, commercial real estate and construction) by either the present value of expected future cash flows discounted at the loan's effective interest rate or the fair value of the collateral if the loan is collateral dependent. A specific allowance is established when the discounted cash flows (or collateral value) of the impaired loan is lower than the carrying value of the loan. Groups of smaller balance homogenous loans are collectively evaluated for impairment. Accordingly, the Company does not separately identify individual loans in the consumer segments (residential real estate, home equity and consumer loans) for impairment disclosures, unless such loans are subject to a troubled debt restructuring agreement.

The Company has established a Business Banking unit within its Commercial Lending Department. The portfolio is made up of both commercial and industrial loans less than \$250,000 and commercial real estate loans less than \$500,000 which are managed by exception. This grouping of loans is considered a homogenous pool of loans and collectively evaluated for impairment. Accordingly, the Company does not separately identify individual loans within this unit for impairment disclosures, unless such loans are subject to a troubled debt restructuring agreement.

**General component.** The general component is based on historical loss experience adjusted for qualitative factors stratified by each of the loan segments: commercial and industrial, commercial real estate, construction, business banking commercial and industrial, business banking commercial real estate, residential real estate, home equity and consumer. Management uses an average of historical losses based on a time frame appropriate to capture relevant loss data for each loan class. This historical loss factor for each loan class is adjusted for the following qualitative factors: the levels/trends in delinquencies, classified and non-accruals; levels and trends in charge-offs and recoveries; trends in volume and terms of loans; effects of changes in risk selection and underwriting standards and other changes in lending policies, procedures and practices; experience, ability and depth of lending management and staff; national and local economic trends and industry conditions; and effects of changes in credit concentrations. This analysis establishes factors that are applied to each loan segment to determine the amount of the general component of the allowance for loan losses.

**Unallocated component.** An unallocated component is maintained to cover uncertainties that could affect management's estimate of probable losses. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating allocated and general reserves in the portfolio.

In the second quarter of 2012, management made refinements to its allowance for loan loss methodology to incorporate the Business Banking unit into the Company's formula-based approach. This refinement did not have a significant effect on the second quarter's loan loss provision or the total allowance for loan loss.

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The Company also maintains a reserve for unfunded credit commitments to provide for the risk of loss inherent in these arrangements. The reserve is determined using a methodology similar to the analysis of the allowance for loan losses, taking into consideration probabilities of future funding requirements. The reserve for unfunded commitments is included in other liabilities and was \$89,000 and \$0 at June 30, 2012 and 2011.

***Evaluation of the Investment Portfolio for Other-Than-Temporary Impairment.*** The evaluation of the investment portfolio for other-than-temporary impairment is also a critical accounting estimate. On a quarterly basis, management reviews securities with a decline in fair value below the amortized cost of the investment to determine whether the decline in fair value is temporary or other-than-temporary. Declines in the fair value of marketable equity securities below their cost that are deemed to be other-than-temporary based on the severity and duration of the impairment are reflected in earnings as realized losses. In estimating other-than-temporary impairment losses for held to maturity and available for sale debt securities, impairment is required to be recognized (1) if we intend to sell the security; (2) if it is more likely than not that we will be required to sell the security before recovery of its amortized cost basis; or (3) the present value of expected cash flows is not sufficient to recover the entire amortized cost basis. For all impaired held to maturity and available for sale securities that management intends to sell, or more likely than not will be required to sell, the full amount of the other-than-temporary impairment is recognized through earnings. For all other impaired held to maturity or available for sale securities, credit-related other-than-temporary impairment is recognized through earnings, while non-credit related other-than-temporary impairment is recognized in other comprehensive income, net of applicable taxes.

***Income Taxes.*** The Company uses the asset and liability method of accounting for income taxes in which deferred tax assets and liabilities are established for the temporary differences between the financial reporting basis and the tax basis of the Company's asset and liabilities. The realization of the net deferred tax asset generally depends upon future levels of taxable income and the existence of prior years' taxable income, to which carry back refund claims could be made. A valuation allowance is maintained for deferred tax assets that management estimates are more likely than not to be unrealizable based on available evidence at the time the estimate is made. Significant management judgment is required in determining income tax expense and deferred tax assets and liabilities. In determining the valuation allowance, the Company uses historical and forecasted future operating results, based upon approved business plans, including a review of the eligible carryforward periods, tax planning opportunities and other relevant considerations. These underlying assumptions can change from period to period. For example, tax law changes or variances in future projected operating performance could result in a change in the valuation allowance. Should actual factors and conditions differ materially from those considered by management, the actual realization of the net deferred tax asset could differ materially from the amounts recorded in the financial statements. If the Company is not able to realize all or part of its net deferred tax asset in the future, an adjustment to the deferred tax asset valuation allowance would be charged to income tax expense in the period such determination was made.

***Goodwill and Identifiable Intangible Assets.*** Goodwill and identifiable intangible assets are recorded as a result of business acquisitions and combinations. These assets are evaluated for impairment annually or whenever events or changes in circumstances indicate the carrying value of these assets may not be recoverable. If the carrying amount exceeds fair value, an impairment charge is recorded to income. The fair value is based on observable market prices, when practicable. Other valuation techniques may be used when market prices are unavailable, including estimated discounted cash flows and market multiples analyses. These types of analyses contain uncertainties because they require management to make assumptions and to apply judgment to estimate industry economic factors and the profitability of future business strategies. In the event of future changes in fair value, the Company may be exposed to an impairment charge that could be material.

***Valuation of Financial Instruments.*** The Company uses fair value measurements to record fair value adjustments to certain financial instruments and to determine fair value disclosures. Securities available for sale are recorded at fair value on a recurring basis. Additionally, from time to time, the Company may be required to record at fair value other assets on a non-recurring basis, or to establish a loss allowance or write-down based on the fair value of impaired assets. Further, the notes to financial statements include information about the extent to which fair value is used to measure assets and liabilities, the valuation methodologies used and its impact to earnings. Additionally, for financial instruments not recorded at fair value, the notes to financial statements disclose the estimate of their fair value. Due to the judgments and uncertainties involved in the estimation process, the estimates could result in materially different results under different assumptions and conditions.

**Table of Contents****NOTE E EARNINGS PER SHARE**

Earnings per share ( EPS ) has been computed by dividing net income by weighted average shares outstanding before any dilution and excluding the weighted average number of unallocated shares held by the Bank's employee stock ownership plan (the ESOP ). Diluted earnings per share has been calculated by dividing net income by weighted average shares outstanding after giving effect to the potential dilution that could occur if potential common shares were converted into common stock using the treasury stock method.

The calculation of basic and diluted earnings per common share for the periods indicated is presented below.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Net income	\$ 2,582	\$ 2,690	\$ 5,431	\$ 5,119
Weighted average common shares applicable to basic EPS (1)	14,542,642	15,028,468	14,606,624	15,022,249
Effect of dilutive potential common shares (2) (3)	245,048	280,688	280,737	262,997
Weighted average common shares applicable to diluted EPS	14,787,690	15,309,156	14,887,361	15,285,246
Earnings per share:				
Basic	\$ 0.18	\$ 0.18	\$ 0.37	\$ 0.34
Diluted	\$ 0.17	\$ 0.18	\$ 0.36	\$ 0.33

- (1) Share-based compensation awards that qualify as participating securities (entitled to receive non-forfeitable dividends) are included in basic EPS using the two-class method.
- (2) Options to purchase 187,300 and 245,589 shares for the three months ended June 30, 2012 and 2011, respectively, and 167,036 and 240,037 shares for the six months ended June 30, 2012 and 2011, respectively, were outstanding but not included in the computation of earnings per share because they were anti-dilutive.
- (3) Includes incremental shares related to dilutive stock options.

**NOTE F ACCUMULATED OTHER COMPREHENSIVE INCOME**

Accounting principles generally require that recognized revenue, expenses, gains and losses be included in net income. Although certain changes in assets and liabilities are reported as a separate component of the equity section of the statement of condition, such items are components of accumulated other comprehensive income.

The components of accumulated other comprehensive income and related tax effects are as follows:

	June 30, 2012	December 31, 2011
Net unrealized gain on securities available for sale	\$ 11,880	\$ 11,841
Tax effect	(4,496)	(4,480)
Net-of-tax amount	7,384	7,361
Pension liability	(1,045)	(1,045)
Tax effect	436	436
Net-of-tax amount	(609)	(609)

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Accumulated other comprehensive income	\$ 6,775	\$ 6,752
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The amortized cost and fair value of securities classified as available for sale and held to maturity are as follows:

	Amortized Cost	Unrealized		Fair Value
		Gains	Losses	
<b>Securities Available for Sale</b>				
<b>June 30, 2012:</b>				
Debt Securities:				
Government-sponsored enterprises	\$ 160	\$ 3	\$	\$ 163
Government-sponsored and government- guaranteed mortgage-backed securities	220,958	11,020	(22)	231,956
Private label mortgage-backed securities	1,685	36	(1)	1,720
Municipal bonds	7,759	627	(1)	8,385
Corporate bonds	1,455	324	(106)	1,673
<b>Total</b>	<b>\$ 232,017</b>	<b>\$ 12,010</b>	<b>\$ (130)</b>	<b>\$ 243,897</b>

<b>December 31, 2011:</b>				
Debt Securities:				
Government-sponsored enterprises	\$ 187	\$ 5	\$	\$ 192
Government-sponsored and government- guaranteed mortgage-backed securities	198,446	11,047		209,493
Private label mortgage-backed securities	2,127	68	(17)	2,178
Municipal bonds	7,759	625		8,384
Corporate bonds	1,453	244	(131)	1,566
<b>Total</b>	<b>\$ 209,972</b>	<b>\$ 11,989</b>	<b>\$ (148)</b>	<b>\$ 221,813</b>

	Amortized Cost	Unrealized		Fair Value
		Gains	Losses	
<b>Securities Held to Maturity</b>				
<b>June 30, 2012:</b>				
Government-sponsored and government- guaranteed mortgage-backed securities	\$ 73,808	\$ 2,418	\$	\$ 76,226
Private label mortgage-backed securities	113	4		117
Industrial revenue bonds	18,992			18,992
State of Israel bonds	150		(2)	148
Municipal bonds	6,358	449		6,807
<b>Total</b>	<b>\$ 99,421</b>	<b>\$ 2,871</b>	<b>\$ (2)</b>	<b>\$ 102,290</b>

<b>December 31, 2011:</b>				
Government-sponsored and government- guaranteed mortgage-backed securities	\$ 89,955	\$ 2,026	\$ (32)	\$ 91,949
Private label mortgage-backed securities	163	4		167
Industrial revenue bonds	19,000			19,000
State of Israel bonds	150			150
Municipal bonds	6,629	416		7,045

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Total	\$ 115,897	\$ 2,446	\$ (32)	\$ 118,311
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The scheduled maturities of debt securities available for sale and held to maturity at June 30, 2012 are shown below. Actual maturities will differ from contractual maturities because issuers generally have the right to call or prepay obligations with or without call or prepayment penalties.

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	At June 30, 2012			
	Securities Available for Sale		Securities Held to Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due in one year or less	\$ 161	\$ 163	\$ 155	\$ 156
Due from one year to five years	98	106	597	620
Due from five years to ten years	5,296	5,702	1,729	1,870
Due after ten years	3,819	4,250	23,019	23,301
	\$ 9,374	\$ 10,221	\$ 25,500	\$ 25,947
Mortgage-backed securities	222,643	233,676	73,921	76,343
	\$ 232,017	\$ 243,897	\$ 99,421	\$ 102,290

Maturities are based on the final contractual payment dates, and do not reflect the impact of potential prepayments or early redemptions.

The Company's portfolio of mortgage-backed securities, which represent interests in pools of residential mortgage loans, consists primarily of securities issued by the Federal Home Loan Mortgage Corporation (Freddie Mac), the Federal National Mortgage Association (Fannie Mae), and the Government National Mortgage Association (Ginnie Mae), all of which are federal government owned or sponsored enterprises.

Gross unrealized losses and fair values at June 30, 2012 and December 31, 2011 aggregated by investment category and the length of time that individual securities have been in a continuous unrealized loss position follow:

	Less than 12 months		12 months or longer		Number of Securities	Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses		Fair Value	Unrealized Losses
<b>At June 30, 2012:</b>							
<b>Securities Available for Sale</b>							
Debt Securities:							
Government-sponsored and government-guaranteed mortgage-backed securities	\$ 10,087	\$ (22)	\$	\$	3	\$ 10,087	\$ (22)
Private label mortgage-backed securities			474	(1)	1	474	(1)
Municipal bonds	288	(1)			1	288	(1)
Corporate bonds			224	(106)	1	224	(106)
Total	\$ 10,375	\$ (23)	\$ 698	\$ (107)	6	\$ 11,073	\$ (130)
<b>Securities Held to Maturity</b>							
State of Israel bonds	\$ 123	\$ (2)	\$	\$	1	\$ 123	\$ (2)
Total	\$ 123	\$ (2)	\$	\$	1	\$ 123	\$ (2)

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	Less than 12 months		12 months or longer		Number of Securities	Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses		Fair Value	Unrealized Losses
<b>At December 31, 2011:</b>							
<b>Securities Available for Sale</b>							
Debt Securities:							
Private label mortgage-backed securities	\$	\$	\$ 614	\$ (17)	1	\$ 614	\$ (17)
Corporate bonds			198	(131)	1	198	(131)
Total	\$	\$	\$ 812	\$ (148)	2	\$ 812	\$ (148)
<b>Securities Held to Maturity</b>							
Government-sponsored and government-guaranteed mortgage-backed securities	\$ 7,444	\$ (32)	\$	\$	2	\$ 7,444	\$ (32)
Total	\$ 7,444	\$ (32)	\$	\$	2	\$ 7,444	\$ (32)

Management has determined that no declines in the fair value of the Company's securities portfolio represent other-than-temporary impairment as of June 30, 2012. In its evaluation, management considered the types of securities, including if the securities were U.S. Government issued, the credit rating on the securities, credit outlook, payment status and financial condition, the length of time the security has been in a loss position, the size of the loss position, our intent and ability to hold the securities to expected recovery of value and other meaningful information. The Company does not intend to sell any debt securities and is unlikely to be required to sell any security before its maturity or market price recovery.

**NOTE H LOANS**

The components of the loan portfolio were as follows at June 30, 2012 and December 31, 2011:

	June 30, 2012	December 31, 2011
<b>Commercial:</b>		
Commercial and industrial	\$ 193,430	\$ 176,086
Commercial mortgages	476,447	450,180
Construction	30,011	30,271
<b>Consumer:</b>		
Residential mortgages	311,270	314,839
Home equity	137,658	135,518
Consumer	13,540	14,985
Total loans	1,162,356	1,121,879
Net deferred loan costs and fees	2,284	2,194
Allowance for loan losses	(11,751)	(11,132)
Loans, net	\$ 1,152,889	\$ 1,112,941

The Company transferred a portion of its originated commercial real estate and commercial and industrial loans to participating lenders. The amounts transferred have been accounted for as sales and are therefore not included in the Company's accompanying consolidated statements of condition. The Company and participating lenders share ratably in any losses that may result from a borrower's lack of compliance with contractual terms of the loan. The Company continues to service the loans on behalf of the participating lenders and, as such, collects cash payments from the borrowers, remits payments (net of servicing fees) to participating lenders and disburses required escrow funds to relevant parties. At June 30, 2012 and December 31, 2011, the Company was servicing loans for participants aggregating \$43.5 million and \$43.8 million, respectively.





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As of June 30, 2012, the Company had two loans that were transferred to participants, which did not meet the requirements to be considered a participating interest. The transferred portion is reported as secured borrowings on the statement of condition, in the amount of \$1.6 million. Total secured borrowings were \$2.1 million at June 30, 2012 and are reported in long-term debt on the consolidated statement of condition.

A summary of the activity pertaining to the allowance for loan losses for the three and six months ended June 30, 2012 and 2011 is as follows:

	Commercial and Industrial	Commercial Real Estate	Construction	Business Banking Commercial and Industrial	Business Banking Commercial Real Estate	Residential	Home Equity	Consumer	Unallocated	Total
<b>Three Months Ended</b>										
<b>June 30, 2012:</b>										
Beginning balance	\$ 3,420	\$ 5,610	\$ 805	\$	\$	\$ 844	\$ 410	\$ 106	\$ 130	\$ 11,325
Charge-offs	(110)	(57)	(51)	(56)	(40)		(30)			(344)
Recoveries	9	10		1						20
Provision	(491)	(331)	(12)	782	723	(154)	(1)	(9)	243	750
Ending balance	\$ 2,828	\$ 5,232	\$ 742	\$ 727	\$ 683	\$ 690	\$ 379	\$ 97	\$ 373	\$ 11,751

	Commercial and Industrial	Commercial Real Estate	Construction	Residential	Home Equity	Consumer	Unallocated	Total
<b>Three Months Ended</b>								
<b>June 30, 2011:</b>								
Beginning balance		\$ 3,112	\$ 5,278	\$ 867	\$ 621	\$ 477	\$ 113	\$ 10,468
Charge-offs		(189)	(422)		(3)	(7)	(4)	(625)
Recoveries		69	52	3				124
Provision		316	271	(82)	160	7	1	673
Ending balance		\$ 3,308	\$ 5,179	\$ 788	\$ 778	\$ 477	\$ 110	\$ 10,640

	Commercial and Industrial	Commercial Real Estate	Construction	Business Banking Commercial and Industrial	Business Banking Commercial Real Estate	Residential	Home Equity	Consumer	Unallocated	Total
<b>Six Months Ended</b>										
<b>June 30, 2012:</b>										
Beginning balance	\$ 3,446	\$ 5,572	\$ 860	\$	\$	\$ 666	\$ 474	\$ 114	\$	\$ 11,132
Charge-offs	(206)	(273)	(127)	(88)	(40)	(88)	(30)	(5)		(857)
Recoveries	39	35	1	1						76
Provision	(451)	(102)	8	814	723	112	(65)	(12)	373	1,400
Ending balance	\$ 2,828	\$ 5,232	\$ 742	\$ 727	\$ 683	\$ 690	\$ 379	\$ 97	\$ 373	\$ 11,751

The Company has established a Business Banking unit within its Commercial Lending Department. The portfolio is made up of both commercial and industrial and commercial real estate loans. As a result, the Company has reallocated charge offs, recoveries, and allowance for loan losses accordingly.

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	Commercial and Industrial	Commercial Real Estate	Construction	Residential	Home Equity	Consumer	Unallocated	Total
<b>Six Months Ended</b>								
<b>June 30, 2011:</b>								
Beginning balance	\$ 2,801	\$ 5,000	\$ 668	\$ 740	\$ 623	\$ 155	\$	\$ 9,987
Charge-offs	(514)	(534)	(28)	(3)	(7)	(4)		(1,090)
Recoveries	205	52	3			2		262
Provision	816	661	145	41	(139)	(43)		1,481
Ending balance	\$ 3,308	\$ 5,179	\$ 788	\$ 778	\$ 477	\$ 110	\$	\$ 10,640

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Further information pertaining to the allowance for loan losses at June 30, 2012 and December 31, 2011 is as follows:

	Commercial and Industrial	Commercial Real Estate	Construction	Residential	Home Equity	Consumer	Unallocated	Total
<b>At June 30, 2012:</b>								
Amount of allowance for loan losses for loans deemed to be impaired and individually evaluated for impairment	\$	\$ 210	\$	\$	\$	\$	\$	\$ 210
Amount of allowance for loan losses for loans not deemed to be impaired and collectively evaluated for impairment	\$ 2,793	\$ 5,022	\$ 742	\$ 690	\$ 379	\$ 97	\$ 373	\$ 10,096
Amount of allowance for loan losses for loans acquired with deteriorated credit quality	\$ 35	\$	\$	\$	\$	\$	\$	\$ 35
<b>Total loans</b>	<b>\$ 193,430</b>	<b>\$ 476,447</b>	<b>\$ 30,011</b>	<b>\$ 311,270</b>	<b>\$ 137,658</b>	<b>\$ 13,540</b>	<b>\$</b>	<b>\$ 1,162,356</b>
Loans deemed to be impaired and individually evaluated for impairment	\$ 2,808	\$ 4,352	\$ 592	\$	\$	\$	\$	\$ 7,752
Loans not deemed to be impaired and collectively evaluated for impairment	\$ 190,536	\$ 471,587	\$ 29,419	\$ 311,270	\$ 137,658	\$ 13,540	\$	\$ 1,154,010
Loans acquired with deteriorated credit quality and deemed to be impaired	\$ 86	\$ 508	\$	\$	\$	\$	\$	\$ 594

	Commercial and Industrial	Commercial Real Estate	Construction	Residential	Home Equity	Consumer	Unallocated	Total
<b>At December 31, 2011:</b>								
Amount of allowance for loan losses for loans deemed to be impaired and individually evaluated for impairment	\$ 65	\$	\$ 70	\$	\$	\$	\$	\$ 135
Amount of allowance for loan losses for loans not deemed to be impaired and collectively evaluated for impairment	\$ 3,381	\$ 5,472	\$ 790	\$ 666	\$ 474	\$ 114	\$	\$ 10,897
Amount of allowance for loan losses for loans acquired with deteriorated credit quality	\$	\$ 100	\$	\$	\$	\$	\$	\$ 100

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Total loans	\$ 176,086	\$ 450,180	\$ 30,271	\$ 314,839	\$ 135,518	\$ 14,985	\$	\$ 1,121,879
Loans deemed to be impaired and individually evaluated for impairment	\$ 3,084	\$ 1,770	\$ 330	\$ 1,169	\$ 56	\$ 163	\$	\$ 6,572
Loans not deemed to be impaired and collectively evaluated for impairment	\$ 172,582	\$ 446,939	\$ 29,941	\$ 313,422	\$ 135,462	\$ 14,822	\$	\$ 1,113,168
Loans acquired with deteriorated credit quality and deemed to be impaired	\$ 420	\$ 1,471	\$	\$ 248	\$	\$	\$	\$ 2,139

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The following is a summary of past due loans at June 30, 2012 and December 31, 2011:

	30-59 Days Past Due	60-89 Days Past Due	90 Days and Over Past Due	Total Past Due	Current	Total Financing Receivables	Recorded Investments > 90 Days and Accruing
<b>At June 30, 2012:</b>							
<b>Commercial:</b>							
Commercial and industrial	\$ 72	\$ 150	\$ 2,590	\$ 2,812	\$ 190,618	\$ 193,430	\$
Commercial real estate	1,133	464	2,295	3,892	472,555	476,447	
Construction	241			241	29,770	30,011	
<b>Consumer:</b>							
Residential real estate	2,360	263	1,715	4,338	306,932	311,270	
Home equity	821	75	120	1,016	136,642	137,658	
Consumer	71	90		161	13,379	13,540	
<b>Total</b>	<b>\$ 4,698</b>	<b>\$ 1,042</b>	<b>\$ 6,720</b>	<b>\$ 12,460</b>	<b>\$ 1,149,896</b>	<b>\$ 1,162,356</b>	<b>\$</b>

**At December 31, 2011:**

<b>Commercial:</b>							
Commercial and industrial	\$ 544	\$ 205	\$ 2,728	\$ 3,477	\$ 172,609	\$ 176,086	\$
Commercial real estate	2,518	1,028	2,131	5,677	444,503	450,180	
Construction			330	330	29,941	30,271	
<b>Consumer:</b>							
Residential real estate	8,747	1,984	1,417	12,148	302,691	314,839	
Home equity	1,087		56	1,143	134,375	135,518	
Consumer	376	1	163	540	14,445	14,985	
<b>Total</b>	<b>\$ 13,272</b>	<b>\$ 3,218</b>	<b>\$ 6,825</b>	<b>\$ 23,315</b>	<b>\$ 1,098,564</b>	<b>\$ 1,121,879</b>	<b>\$</b>

The following is a summary of impaired loans at June 30, 2012 and December 31, 2011:

	At June 30, 2012			At December 31, 2011		
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Recorded Investment	Unpaid Principal Balance	Related Allowance
<b>With no related allowance recorded:</b>						
Commercial and industrial	\$ 2,808	\$ 2,808		\$ 1,379	\$ 2,115	
Commercial real estate	4,173	4,173		1,961	2,073	
Construction	592	592		190	259	
Residential real estate				1,417	1,417	
Home Equity				56	56	
Consumer				164	164	
<b>Total</b>	<b>\$ 7,573</b>	<b>\$ 7,573</b>		<b>\$ 5,167</b>	<b>\$ 6,084</b>	
<b>With an allowance recorded:</b>						
Commercial and industrial	\$ 86	\$ 86	\$ 35	\$ 2,125	\$ 2,125	\$ 65
Commercial real estate	687	687	210	1,279	1,279	100
Construction				140	140	70
<b>Total</b>	<b>\$ 773</b>	<b>\$ 773</b>	<b>\$ 245</b>	<b>\$ 3,544</b>	<b>\$ 3,544</b>	<b>\$ 235</b>

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**By portfolio segment:**

Commercial portfolio segment	\$ 8,346	\$ 8,346	\$ 245	\$ 7,074	\$ 7,991	\$ 235
Consumer portfolio segment				1,637	1,637	
<b>Total impaired loans</b>	<b>\$ 8,346</b>	<b>\$ 8,346</b>	<b>\$ 245</b>	<b>\$ 8,711</b>	<b>\$ 9,628</b>	<b>\$ 235</b>

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The following is a summary of information pertaining to impaired loans:

	Three Months Ended June 30, 2012			Three Months Ended June 30, 2011		
	Average Recorded Investment on Impaired Loans	Interest Income Recognized on a Cash Basis		Average Recorded Investment on Impaired Loans	Interest Income Recognized on a Cash Basis	
<b>Commercial:</b>						
Commercial and industrial	\$ 4,456	\$ 1	\$	\$ 3,322	\$	\$
Commercial real estate	3,877	10	2	3,230	33	33
Construction	781	6		1,204	7	3
<b>Consumer:</b>						
Residential real estate			2	1,351	16	16
Home Equity				81	1	1
Consumer				94		
<b>Total</b>	<b>\$ 9,114</b>	<b>\$ 17</b>	<b>\$ 4</b>	<b>\$ 9,282</b>	<b>\$ 57</b>	<b>\$ 53</b>

	Six Months Ended June 30, 2012			Six Months Ended June 30, 2011		
	Average Recorded Investment on Impaired Loans	Interest Income Recognized on a Cash Basis		Average Recorded Investment on Impaired Loans	Interest Income Recognized on a Cash Basis	
<b>Commercial:</b>						
Commercial and industrial	\$ 4,073	\$ 9	\$ 8	\$ 3,104	\$ 4	\$ 4
Commercial real estate	3,731	25	7	5,045	63	63
Construction	743	13		1,212	23	19
<b>Consumer:</b>						
Residential real estate			2	977	21	21
Home Equity				75	1	1
Consumer				80	2	2
<b>Total</b>	<b>\$ 8,547</b>	<b>\$ 47</b>	<b>\$ 17</b>	<b>\$ 10,493</b>	<b>\$ 114</b>	<b>\$ 110</b>

The following is a summary of non-accrual loans, at June 30, 2012 and December 31, 2011:

	June 30, 2012	December 31, 2011
<b>Commercial:</b>		
Commercial and industrial	\$ 2,942	\$ 3,504
Commercial real estate	4,117	2,984
Construction		330
<b>Consumer:</b>		
Residential real estate	1,262	1,417
Home equity	292	56
Consumer		163
<b>Total</b>	<b>\$ 8,613</b>	<b>\$ 8,454</b>





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The following table represents modifications that were deemed to be troubled debt restructures for the three and six months ended June 30, 2012 and 2011:

	Three Months Ended June 30, 2012			Three Months Ended June 30, 2011		
	Number of Contracts	Outstanding Pre-Modification	Recorded Investment Post-Modification	Number of Contracts	Outstanding Pre-Modification	Recorded Investment Post-Modification
<b>Troubled Debt Restructurings:</b>						
Commercial and industrial	1	\$ 140	\$ 140	1	\$ 873	\$ 873
Commercial real estate	4	1,211	1,211			
Construction	2	613	613			
Total	7	\$ 1,964	\$ 1,964	1	\$ 873	\$ 873

	Six Months Ended June 30, 2012			Six Months Ended June 30, 2011		
	Number of Contracts	Outstanding Pre-Modification	Recorded Investment Post-Modification	Number of Contracts	Outstanding Pre-Modification	Recorded Investment Post-Modification
<b>Troubled Debt Restructurings:</b>						
Commercial and industrial	1	\$ 140	\$ 140	1	\$ 873	\$ 873
Commercial real estate	4	1,211	1,211	1	248	263
Construction	2	613	613			
Total	7	\$ 1,964	\$ 1,964	2	\$ 1,121	\$ 1,136

The modifications provided on one commercial and industrial loan and four commercial real estate loans are related to one borrower relationship. The modification extended the maturity of demand notes that had reached maturity. The modifications provided on the two construction loans are related to one borrower relationship. The modification extended the maturity of demand notes that had reached maturity. Management performs a discounted cash flow calculation or collateral analysis if the loan is collateral dependent to determine the amount of impaired reserve required on each of the troubled debt restructures. Any reserve required is recorded through the provision for loan losses.

As of June 30, 2012, there have been no TDRs that have subsequently defaulted within one year of modification.

**CREDIT QUALITY INFORMATION**

The Company utilizes a nine grade risk rating system for commercial and industrial, commercial real estate and construction loans as follows:

Pass: Loans within these five categories are considered low to average risk.

Special Mention: Loans in this category portray one or more weaknesses that may be tolerated in the short run. Assets in this category are currently protected but are potentially weak and are being closely monitored by management.

Substandard: Loans in this category are considered inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged. There is a distinct possibility that the Company will sustain some loss if the weakness is not corrected.

Doubtful: Loans in this category have all the weaknesses inherent in those classified substandard with the added characteristic that the weaknesses make the collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable and improbable. The possibility of loss is extremely high, however, its classification as an estimated loss is deferred until a more exact determination of the extent of the loss is ascertained.



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Loss: Loans in this category are considered uncollectible and of such little value that their continuance as loans is not warranted.

The Company does not assign risk ratings to residential real estate, home equity and mobile home consumer loans unless they are contractually past due 90 days or more or where legal action has commenced against the borrower. All other consumer loans are charged off when they become contractually past due 120 days. Loans not assigned a rating are considered pass.

Business banking loans are assigned a Pass rating unless they are contractually past due 90 days or more, legal action has commenced against the borrower or other criteria for a risk rating change as defined within the business banking loan policy have been triggered. Upon one or more of these events, the loan will be risk rated Substandard.

On an annual basis, or more often if needed, the Company formally reviews the ratings on all commercial and industrial, commercial real estate and construction loans. Semi-annually, the Company engages an independent third party to review loans within these segments. Management uses the results of these reviews as part of its annual review process.

The following table presents the Company's loan segment by internally assigned grades:

	At June 30, 2012			
Commercial:	Commercial & Industrial	Commercial Real Estate	Construction	Total
<b>Grade:</b>				
Pass	\$ 177,066	\$ 453,757	\$ 24,277	\$ 655,100
Special Mention	6,319	5,814	433	12,566
Substandard	9,376	16,876	5,301	31,553
Doubtful	669			669
<b>Total</b>	<b>\$ 193,430</b>	<b>\$ 476,447</b>	<b>\$ 30,011</b>	<b>\$ 699,888</b>
<b>Consumer:</b>				
Grade:	Residential	Home Equity	Consumer	Total
Pass	\$ 309,394	\$ 137,423	\$ 13,482	\$ 460,299
Special Mention				
Substandard	1,876	235	58	2,169
Doubtful				
<b>Total</b>	<b>\$ 311,270</b>	<b>\$ 137,658</b>	<b>\$ 13,540</b>	<b>\$ 462,468</b>
<b>At December 31, 2011</b>				
Commercial:	Commercial & Industrial	Commercial Real Estate	Construction	Total
<b>Grade:</b>				
Pass	\$ 157,026	\$ 419,818	\$ 23,955	\$ 600,799
Special Mention	7,730	10,965	1,057	19,752
Substandard	11,230	19,397	5,259	35,886
Doubtful	100			100
<b>Total</b>	<b>\$ 176,086</b>	<b>\$ 450,180</b>	<b>\$ 30,271</b>	<b>\$ 656,537</b>
<b>Consumer:</b>				
Grade:	Residential	Home Equity	Consumer	Total
Pass	\$ 311,921	\$ 135,253	\$ 14,723	\$ 461,897
Special Mention	52			52

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Substandard Doubtful	2,866	265	262	3,393
Total	\$ 314,839	\$ 135,518	\$ 14,985	\$ 465,342

**Table of Contents****NOTE I COMMITMENTS**

Financial instruments with off-balance sheet risk at June 30, 2012 and December 31, 2011 were as follows:

	June 30, 2012	December 31, 2011
Unused lines of credit	\$ 255,995	\$ 250,034
Amounts due mortgagors	20,428	27,495
Standby letters of credit	3,345	4,004
Commitments to originate loans	36,178	32,689

The Company has a commitment to invest up to \$1.0 million in a venture capital fund. As of June 30, 2012, the Company has contributed \$700,000 to the fund.

The Company has committed to invest up to \$12.0 million in two low income housing tax credit funds by the end of 2015. At June 30, 2012, the Company invested \$6.7 million in the funds, which have been reduced by net operating losses of \$1.3 million. The net carrying balance of \$5.5 million is included in other assets on the Company's consolidated statement of condition. Tax benefits in the form of net operating losses are recognized as they are incurred and recorded in non-interest expense.

**NOTE J DEPOSITS**

Deposit accounts, by type, are summarized as follows at June 30, 2012 and December 31, 2011:

	June 30, 2012	December 31, 2011
Demand	\$ 228,495	\$ 205,902
NOW	62,064	52,899
Savings	261,586	247,664
Money market	292,763	301,770
Certificates of deposit	415,705	421,740
	\$ 1,260,613	\$ 1,229,975

**NOTE K CONTINGENCIES**

The Bank, as successor in interest to Commonwealth National Bank, is involved in litigation relating to its foreclosure on a certain loan property. The litigants claim that Commonwealth National Bank acted in bad faith and in violation of applicable law and that its actions resulted in a sale of the underlying property for less than its market value, thereby causing damage to the parties. During the third quarter of 2011 the judge issued a ruling in favor of the Bank. The litigants have appealed the decision. The Bank believes these claims and the appeal are without merit and is vigorously defending the litigation. No estimate of any reasonably possible loss or range of loss to the Bank can be made at this time.

The Bank is also a defendant in other claims and legal actions arising in the ordinary course of business. In the opinion of management, after consultation with legal counsel, the ultimate disposition of these matters is not expected to have a material adverse effect on the Company's financial condition, results of operations or cash flows.

**Table of Contents****NOTE L FAIR VALUES OF ASSETS AND LIABILITIES**

The Company groups its assets and liabilities measured at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value, as follows:

Level 1 Valuations for assets and liabilities traded in active exchange markets, such as the New York Stock Exchange. Level 1 also includes U.S. Treasury, other U.S. government and government-sponsored enterprises that are traded by dealers or brokers in active markets. Valuations are obtained from readily available pricing sources for market transactions involving identical assets or liabilities.

Level 2 Valuations for assets and liabilities traded in less active dealer or broker markets. Level 2 includes U.S. government and mortgage-backed securities issued by government-sponsored enterprises. Valuations are obtained from third party pricing services for identical or comparable assets or liabilities.

Level 3 Valuations for assets and liabilities that are derived from other valuation methodologies, including option pricing models, discounted cash flow models and similar techniques, and not based on market exchange, dealer, or broker-traded transactions. Level 3 valuations incorporate certain assumptions and projections in determining the fair value assigned to such assets and liabilities. Level 3 also includes corporate bonds that have fair values derived from unobservable issuer-provided financial information and discounted cash flow models.

Assets measured at fair value on a recurring basis, are summarized below:

	Level 1	Level 2	Level 3	Total Fair Value
<b>At June 30, 2012</b>				
Securities available for sale:				
Government-sponsored enterprises	\$	\$ 163	\$	\$ 163
Government-sponsored and government- guaranteed mortgage-backed securities		231,956		231,956
Private label mortgage-backed securities		1,720		1,720
Municipal bonds		8,385		8,385
Corporate bonds			1,673	1,673
Total	\$	\$ 242,224	\$ 1,673	\$ 243,897

	Level 1	Level 2	Level 3	Total Fair Value
<b>At December 31, 2011</b>				
Securities available for sale:				
Government-sponsored enterprises	\$	\$ 192	\$	\$ 192
Government-sponsored and government- guaranteed mortgage-backed securities		209,493		209,493
Private label mortgage-backed securities		2,178		2,178
Municipal bonds		8,384		8,384
Corporate bonds			1,566	1,566
Total	\$	\$ 220,247	\$ 1,566	\$ 221,813

The Company had no liabilities measured at fair value on a recurring basis at June 30, 2012 or December 31, 2011.

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The table below presents the changes in Level 3 assets measured at fair value on a recurring basis for the six months ended June 30, 2012.

<b>Balance at December 31, 2011</b>	<b>\$ 1,566</b>
Change in unrealized gain	107
<b>Balance at June 30, 2012</b>	<b>\$ 1,673</b>

Due to the lack of observable market data, corporate bonds were included in Level 3 of the fair value hierarchy. The fair value has been derived by third party pricing services using pricing models and techniques which require significant judgment and estimation. Pricing models and techniques are dependent upon several unobservable inputs including the discount rate, the interest rate environment, credit defaults and losses and financial performance.

There were no transfers in or out of levels 1 and 2.

The Company may be required, from time to time, to measure at fair value certain other assets on a nonrecurring basis in accordance with GAAP. These adjustments to fair value usually result from application of lower-of-cost-or-fair value accounting or write-downs of individual assets. The following tables summarize the fair value hierarchy used to determine the adjustment and the carrying value of the related individual assets for the three and six months ended June 30, 2012 and 2011.

	At June 30, 2012			Three Months Ended June 30, 2012	Six Months Ended June 30, 2012
	Level 1	Level 2	Level 3	Total Gains/(Losses)	Total Gains/(Losses)
<b>Assets:</b>					
Loans	\$	\$	\$ 528	\$ 135	\$ (10)
Other real estate owned			740	(50)	(50)
<b>Total assets</b>	<b>\$</b>	<b>\$</b>	<b>\$ 1,268</b>	<b>\$ 85</b>	<b>\$ (60)</b>

	At June 30, 2011			Three Months Ended June 30, 2011	Six Months Ended June 30, 2011
	Level 1	Level 2	Level 3	Total Gains/(Losses)	Total Gains/(Losses)
<b>Assets:</b>					
Loans	\$	\$	\$ 3,593	\$ 108	\$ (13)
Other assets			541	(59)	(59)
<b>Total assets</b>	<b>\$</b>	<b>\$</b>	<b>\$ 4,134</b>	<b>\$ 49</b>	<b>\$ (72)</b>

The amount of loans represents the carrying value of impaired loans net of related write-downs and valuation allowances for which adjustments are based on the estimated fair value of the underlying collateral. The other real estate owned amount represents the carrying value for which adjustments are also based on the estimated fair value of the property.

Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial instrument. These estimates do not reflect any premium or discount that could result from offering for sale at one time the Company's entire holdings of a particular financial instrument. Because a market may not readily exist for a significant portion of the Company's financial instruments, fair value estimates are based on judgments regarding future expected loss experience, current economic conditions, risk characteristics of various



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financial instruments, and other factors. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

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The following methods and assumptions were used by the Company in estimating fair values of its financial instruments:

**Cash and Cash Equivalents and Short-term Investments.** The carrying amounts of cash and short-term instruments approximate fair values based on the short-term nature of the assets.

**Investment Securities and FHLBB Stock.** The fair value of securities to be held to maturity and securities available for sale is estimated based on quoted market prices, where available. If quoted market prices are not available, fair values are based on quoted market prices of comparable instruments. Ownership of Federal Home Loan Bank of Boston ( FHLBB ) stock is restricted to member banks; therefore, the stock is not traded. The estimated fair value of FHLBB stock is equal to its carrying value, which represents the price at which the FHLBB is obligated to redeem its stock.

**Loans.** For valuation purposes, the loan portfolio was segregated into its significant categories, which are residential mortgage, commercial real estate, commercial and industrial, construction and consumer loans. These categories were further segregated, where appropriate, into components based on significant financial characteristics such as type of interest rate (fixed or adjustable). Fair values were estimated for each component using assumptions developed by management and a valuation model provided by a third party specialist.

The fair values of residential mortgage, commercial real estate, commercial and industrial, construction and consumer loans were estimated by discounting the anticipated cash flows from the respective portfolios. Estimates of the timing and amount of these cash flows considered factors such as future loan prepayments. The discount rates reflected current market rates for loans with similar terms to borrowers of similar credit quality. The fair value of home equity lines of credit was based on the outstanding loan balances. Fair values for non-performing loans are estimated using discounted cash flow analyses or underlying collateral values, where applicable.

**Deposits.** The fair value of deposits with no stated maturity, such as demand deposits, NOW, regular savings, and money market deposit accounts, is equal to the amount payable on demand. The fair value estimates do not include the benefit that results from the generally lower cost of funding provided by the deposit liabilities compared to the cost of borrowing funds in the market. The fair value estimate of time deposits is based on the discounted value of contractual cash flows. The discount rate is estimated using the rates currently offered for deposits having similar remaining maturities.

**Short-term Borrowings.** For short-term borrowings maturing within one year, carrying values approximate fair values. Fair values of other short-term borrowings are estimated using discounted cash flow analyses based on the current incremental borrowing rates in the market for similar types of borrowing arrangements.

**Long-term Debt.** The fair values of the Company's long-term debt are estimated using discounted cash flow analyses based on the current incremental borrowing rates in the market for similar types of borrowing arrangements.

**Repurchase Agreements.** The Company enters into overnight repurchase agreements with its customers. Since these agreements are short-term instruments, the fair value of these agreements approximates their recorded balance. The Company also secures term repurchase agreements through other financial institutions. The fair value of these agreements are determined by discounting the anticipated future cash payments using rates currently available to the Bank for debt with similar terms and remaining maturities.

**Subordinated Debentures.** The Company has outstanding subordinated debt in the form of trust preferred securities issued through a private placement offering. The fair value estimate is determined by discounting the anticipated future cash payments by using the rates currently available to the Company for debt with similar terms and remaining maturities.

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**Off-Balance Sheet Instruments.** The fair value of off-balance-sheet mortgage lending commitments are based on fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the counterparties' credit standing. In the case of the commitments discussed in Note I, the fair value equals the carrying amounts which are not significant.

**Summary of Fair Values of Financial Instruments.** The estimated fair values, and related carrying or notional amounts, of the Company's financial instruments are as follows. Certain financial instruments and all nonfinancial instruments are exempt from disclosure requirements. Accordingly, the aggregate fair value amounts presented herein do not represent the underlying fair value of the Company.

The fair value of the Company's financial instruments is as follows at dates indicated:

	Carrying Value	At June 30, 2012			Estimated Fair Value
		Level 1	Level 2	Level 3	
<b>Financial Assets:</b>					
Cash and cash equivalents	\$ 42,407	\$ 42,407	\$	\$	\$ 42,407
Securities available for sale	243,897		242,224	1,673	243,897
Securities held to maturity	99,421		102,291		102,291
Stock in Federal Home Loan Bank of Boston	14,454			14,454	14,454
Net loans	1,152,889			1,175,441	1,175,441
<b>Financial Liabilities:</b>					
Deposits (with no stated maturity)	844,908			844,908	844,908
Time deposits	415,705			422,526	422,526
Federal Home Loan Bank of Boston advances	102,892			107,419	107,419
Repurchase agreements	37,772			38,301	38,301
Subordinated debentures	5,585		5,585		5,585

	Carrying Value	At December 31, 2011			Estimated Fair Value
		Level 1	Level 2	Level 3	
<b>Financial Assets:</b>					
Cash and cash equivalents	\$ 61,518	\$ 61,518	\$	\$	\$ 61,518
Securities available for sale	221,813		220,247	1,566	221,813
Securities held to maturity	115,897		118,311		118,311
Stock in Federal Home Loan Bank of Boston	15,365			15,365	15,365
Net loans	1,112,941			1,150,955	1,150,955
<b>Financial Liabilities:</b>					
Deposits (with no stated maturity)	808,235			808,235	808,235
Time deposits	421,740			429,676	429,676
Federal Home Loan Bank of Boston advances	106,417			110,201	110,201
Repurchase agreements	37,260			37,347	37,347
Subordinated debentures	5,539		5,539		5,539

**Table of Contents****NOTE M PENSION AND POSTRETIREMENT BENEFIT PLANS**

The Company maintains a Senior Executive Retirement Plan SERP and a Director Retirement Plan. These plans had no assets at June 30, 2012 and 2011. The following table presents the components of the net periodic benefit cost for the indicated periods:

	For the Three Months Ended June 30,				For the Six Months Ended June 30,			
	2012		2011		2012		2011	
	SERP	Director Retirement Plan	SERP	Director Retirement Plan	SERP	Director Retirement Plan	SERP	Director Retirement Plan
<b>Periodic benefit cost:</b>								
Service cost	\$ 79	\$ 23	\$ 83	\$ 23	\$ 158	\$ 46	\$ 167	\$ 46
Interest cost	44	14	47	14	88	28	93	28
Total pension cost	123	37	130	37	246	74	260	74
Prior service cost amortization	28	9	34	9	57	18	69	18
Net loss amortization		3		3		6		6
<b>Net periodic benefit cost</b>	<b>\$ 151</b>	<b>\$ 49</b>	<b>\$ 164</b>	<b>\$ 49</b>	<b>\$ 303</b>	<b>\$ 98</b>	<b>\$ 329</b>	<b>\$ 98</b>

Benefits expected to be paid over the next five years as presented in the Company's Annual Report on Form 10-K for the year ended December 31, 2011 have not changed. These plans are funded on a pay-as-you-go-basis and the Company does not expect to make any contributions to these plans in 2012.

**ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**  
**Forward-Looking Statements**

This report may contain forward-looking statements relating to such matters as anticipated financial performance, business prospects, future strategies, technological developments, new products, and similar matters. Forward-looking statements are generally preceded by terms such as expects, believes, anticipates, intends or similar expressions. The Private Securities Litigation Reform Act of 1995 provides a safe harbor for forward-looking statements provided that the Company notes factors that could cause the Company's actual results to differ materially from the anticipated results expressed in the Company's forward-looking statements. Factors that may cause actual results to differ materially from those projected in the forward-looking statements include, but are not limited to, general economic conditions, changes in market interest rates and real estate values, changes in the size, composition or risks in the loan and securities portfolios, loan or deposit demand, changes in asset quality, including levels of delinquent, classified and charged-off loans, legislative, accounting or regulatory changes, and significant increases in competitive pressures. Additional factors are discussed in the Company's Annual Report on Form 10-K for the year ended December 31, 2011 under Item 1A. Risk Factors. These risks and uncertainties should be considered in evaluating forward-looking statements and undue reliance should not be placed on such statements. Forward-looking statements speak only as of the date they are made and the Company does not undertake to update forward-looking statements to reflect circumstances or events that occur after the date of the forward-looking statements or to reflect the occurrence of unanticipated events. Accordingly, past results and trends should not be used by investors to anticipate future results or trends.

**Comparison of Financial Condition at June 30, 2012 and December 31, 2011**

Total assets increased \$29.9 million, or 1.8%, to \$1.65 billion at June 30, 2012 from \$1.62 billion at December 31, 2011 reflecting growth in net loans and securities available for sale, partially offset by a decrease in interest-bearing deposits and held to maturity investment securities. Net loans increased \$39.9 million, or 3.6%, to \$1.15 billion at June 30, 2012 from \$1.11 billion at December 31, 2011 mainly reflecting growth in the commercial loan portfolios. Commercial mortgages increased \$26.3 million, or 5.8%, and commercial and industrial loans increased \$17.3 million, or 9.9%, primarily the result of business development efforts, competitive products and pricing and the establishment of a loan production office in Beverly, Massachusetts in 2011. The increase in the commercial portfolios was partially offset by a decrease in residential mortgages of \$3.6 million, or 1.1%, driven by sales of 30-year fixed rate loan originations totaling \$9.6 million and payments, offset to a large extent by originations of 10- and 15-year fixed rate loans. Securities available for sale increased \$22.1 million, or 10.0%, to \$243.9 million at

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June 30, 2012 from \$221.8 million at December 31, 2011 primarily due to purchases of fixed-rate agency mortgage-backed securities totaling \$51.6 million, partially offset by repayments of government-sponsored agency debt and mortgage-backed securities of \$29.3 million. Interest-bearing deposits decreased \$20.7 million, or 49.9%, reflecting the use of excess cash to fund purchases of available for sale securities and loan originations. Securities held to maturity decreased \$16.5 million, or 14.2%, to \$99.4 million at June 30, 2012 from \$115.9 million at December 31, 2011 as a result of repayments of government-sponsored agency debt and mortgage-backed securities.

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Total deposits increased \$30.6 million, or 2.5%, to \$1.26 billion at June 30, 2012 compared to \$1.23 billion at December 31, 2011 primarily due to growth in core deposit accounts of \$36.7 million, or 4.5%, to \$844.9 million at June 30, 2012 from \$808.2 million at December 31, 2011. The growth in core deposit account balances was driven by sales and marketing initiatives, competitive products and pricing, attention to excellence in customer service and targeted promotional activities. The increase in core deposits was partially offset by a decrease in certificates of deposit of \$6.0 million, or 1.4%, to \$415.7 million at June 30, 2012 compared to \$421.7 million at December 31, 2011 resulting from customers preference for savings, demand and NOW accounts due to the low rate environment. Short-term borrowings increased \$512,000, or 3.0%, to \$17.8 million at June 30, 2012 from \$17.3 million at December 31, 2011 mainly due to growth in overnight repurchase agreements. Long-term debt decreased \$1.8 million, or 1.4%, to \$125.0 million at June 30, 2012 compared to \$126.9 million at December 31, 2011 largely reflecting the use of excess cash balances to pay down maturing FHLBB advances. At June 30, 2012, the Company continued to have considerable liquidity including significant unused borrowing capacity at the FHLBB and the Federal Reserve Bank of Boston and access to funding through the repurchase agreement and brokered deposit markets.

Total stockholders' equity increased \$768,000, or 0.3%, to \$228.1 million at June 30, 2012 from \$227.4 million at December 31, 2011 as a result of net income of \$5.4 million, stock-based compensation credits totaling \$712,000 and ESOP compensation of \$558,000 for the six months ended June 30, 2012. These increases were partially offset by repurchases of common stock totaling \$3.2 million and cash dividend payments amounting to \$2.6 million.

**Credit Quality and Reserve Coverage**

The Company actively manages credit risk through its underwriting practices, loan review activities and collection operations, and does not offer nor has it historically offered residential mortgage and other consumer loans to subprime or Alternative-A-paper borrowers. All loans where the interest payment is 90 days or more in arrears as of the closing date of each month are placed on non-accrual status. Non-accrual loans totaled \$8.6 million, or 0.74% of total loans, at June 30, 2012 compared to \$8.5 million, or 0.75% of total loans, at December 31, 2011. Classified loans decreased \$5.6 million, or 14.1%, to \$33.7 million at June 30, 2012 and included ten relationships which represent 52.3% of the total. Of the \$2.4 million in other real estate owned, \$740,000 is under a sales contract with a closing expected in the third quarter of 2012. Refer to Note H Loans in the Notes to the Unaudited Consolidated Financial Statements in this report for additional disclosures about credit quality.

At June 30, 2012 and December 31, 2011, the ratio of the allowance for loan losses to total loans was 1.01%. Excluding the impact of acquired loans totaling \$132.8 million at June 30, 2012 and \$168.0 million at December 31, 2011, the ratio of the allowance for loan losses to total loans would have been 1.14% at June 30, 2012 and 1.17% at December 31, 2011. Net charge-offs totaled \$781,000, or 0.14% of average loans outstanding on an annualized basis, for the six months ended June 30, 2012 as compared to net charge-offs of \$828,000, or 0.15% of average loans outstanding on an annualized basis, for the same period in 2011 and consisted primarily of commercial loans. Refer to Note H Loans in the Notes to the Unaudited Consolidated Financial Statements in this report for disclosures about the allowance for loan losses.

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**Comparison of Operating Results for the Three Months Ended June 30, 2012 and 2011**

**Overview**

Our results of operations depend primarily on our net interest income. Net interest income is the difference between the interest income earned on interest-earning assets, consisting primarily of loans, investment securities and other interest-earning assets, and the interest paid on interest-bearing liabilities, consisting primarily of deposits, FHLBB advances and repurchase agreements.

Our results of operations also are affected by provisions for loan losses, non-interest income and non-interest expense. Non-interest income consists primarily of deposit account fees, wealth management fees, increases in the cash surrender value of bank-owned life insurance, gains on sale of loans and securities and miscellaneous other income. Non-interest expense consists primarily of salaries and benefits, occupancy, marketing, data processing, professional fees, FDIC insurance assessments, low income housing tax credit fund and other operating expenses. Our results of operations also may be affected significantly by general and local economic and competitive conditions, changes in market interest rates, governmental policies and actions of regulatory authorities.

**Net Income.** Net income decreased \$108,000, or 4.0%, to \$2.6 million for the second quarter of 2012 compared to net income of \$2.7 million for the same period in 2011. Excluding the impact of acquisition related expenses of \$592,000 (non tax-deductible), net income would have increased by \$484,000, or 18.0%, to \$3.2 million largely due to a decrease in non-interest expense of \$527,000 (excluding acquisition related expenses) and an increase of \$359,000 in non-interest income. These positive results were offset in part by a decrease in net interest income of \$88,000 and increases of \$77,000 in provision for loan losses and \$237,000 in income tax expense. Diluted earnings per share decreased \$0.01 to \$0.17 for the three months ended June 30, 2012 compared to \$0.18 for the same period last year. Excluding the impact of acquisition related expenses, diluted earnings per share would have increased \$0.03, or 16.7%, to \$0.21.

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**Average Balances and Yields.** The following table sets forth average balances, average yields and costs, and certain other information for the periods indicated. No tax-equivalent yield adjustments were made, as the effect thereof was not material. All average balances are daily average balances. Non-accrual loans were included in the computation of average balances, but have been reflected in the table as loans carrying a zero yield.

	Three Months Ended June 30,					
	Average Balance	2012 Interest and Dividends	Yield/ Cost	Average Balance	2011 Interest and Dividends	Yield/ Cost
(Dollars in thousands)						
<b>Interest-earning assets:</b>						
Loans:						
Residential real estate <sup>(1)</sup>	\$ 312,592	\$ 3,588	4.59%	\$ 318,095	\$ 3,985	5.01%
Commercial real estate	498,354	6,875	5.52%	461,866	7,005	6.07%
Home equity	137,526	1,225	3.56%	138,462	1,330	3.84%
Commercial and industrial	188,343	2,298	4.88%	166,914	2,133	5.11%
Consumer and other	14,326	195	5.44%	17,968	250	5.57%
Total loans <sup>(2)</sup>	1,151,141	14,181	4.93%	1,103,305	14,703	5.33%
Investment securities	340,086	2,767	3.25%	356,479	3,387	3.80%
Other interest-earning assets	55,905	51	0.36%	49,654	38	0.31%
Total interest-earning assets	1,547,132	16,999	4.39%	1,509,438	18,128	4.80%
Noninterest-earning assets <sup>(3)</sup>	105,865			93,329		
Total assets	\$ 1,652,997			\$ 1,602,767		
<b>Interest-bearing liabilities:</b>						
Savings accounts	\$ 261,297	336	0.51%	\$ 233,292	442	0.76%
Money market accounts	305,501	366	0.48%	269,397	504	0.75%
NOW accounts	55,539	42	0.30%	40,931	37	0.36%
Certificates of deposit	416,857	1,854	1.78%	444,605	2,211	1.99%
Total interest-bearing deposits	1,039,194	2,598	1.00%	988,225	3,194	1.29%
FHLB advances	103,632	819	3.16%	138,215	1,245	3.60%
Other interest-bearing liabilities	53,860	288	2.14%	49,798	307	2.47%
Total interest-bearing liabilities	1,196,686	3,705	1.24%	1,176,238	4,746	1.61%
Demand deposits	217,586			190,941		
Other noninterest-bearing liabilities	10,870			9,309		
Total liabilities	1,425,142			1,376,488		
Stockholders' equity	227,855			226,279		
Total liabilities and stockholders' equity	\$ 1,652,997			\$ 1,602,767		
Net interest income		\$ 13,294			\$ 13,382	
Interest rate spread <sup>(4)</sup>			3.15%			3.19%
Net interest-earning assets <sup>(5)</sup>	\$ 350,446			\$ 333,200		
Net interest margin <sup>(6)</sup>			3.44%			3.55%



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Average interest-earning assets to average interest-bearing liabilities	129.28%	128.33%
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- (1) Includes loans held for sale.
- (2) Loans, including non-accrual loans, are net of deferred loan origination costs and advanced funds.
- (3) Includes bank-owned life insurance, the income on which is classified as non-interest income.
- (4) Net interest rate spread represents the difference between the yield on average interest-earning assets and the cost of average interest-bearing liabilities.
- (5) Net interest-earning assets represent total interest-earning assets less total interest-bearing liabilities.
- (6) Net interest margin represents annualized net interest income divided by average total interest-earning assets.

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**Rate/Volume Analysis.** The following table presents the effects of changing rates and volumes on our net interest income for the periods indicated. The rate column shows the effects attributable to changes in rate (changes in rate multiplied by prior volume). The volume column shows the effects attributable to changes in volume (changes in volume multiplied by prior rate). The net column represents the sum of the prior columns. For purposes of this table, changes attributable to both rate and volume, which cannot be segregated, have been allocated proportionately, based on the changes due to rate and the changes due to volume.

	<b>Three Months Ended June 30, 2012 vs. 2011</b>		
	<b>Increase (Decrease) Due to Volume</b>	<b>Rate</b>	<b>Net</b>
	<b>(In thousands)</b>		
<b>Interest-earning assets:</b>			
Loans:			
Residential real estate <sup>(1)</sup>	\$ (68)	\$ (329)	\$ (397)
Commercial real estate	530	(660)	(130)
Home equity	(9)	(96)	(105)
Commercial and industrial	265	(100)	165
Consumer and other	(50)	(5)	(55)
Total loans	668	(1,190)	(522)
Investment securities	(151)	(469)	(620)
Other interest-earning assets	5	8	13
Total interest-earning assets	522	(1,651)	(1,129)
<b>Interest-bearing liabilities:</b>			
Savings accounts	48	(154)	(106)
Money market accounts	61	(199)	(138)
NOW accounts	12	(7)	5
Certificates of deposit	(132)	(225)	(357)
Total interest-bearing deposits	(11)	(585)	(596)
FHLB advances	(286)	(140)	(426)
Other interest-bearing liabilities	24	(43)	(19)
Total interest-bearing liabilities	(273)	(768)	(1,041)
Change in net interest income	\$ 795	\$ (883)	\$ (88)

(1) Includes loans held for sale.

**Net Interest Income Before Provision for Loan Losses.** Net interest income before provision for loan losses decreased \$88,000, or 0.7%, to \$13.3 million for the second quarter of 2012 from \$13.4 million for the same period in 2011 mainly as a result of contraction in the net interest margin, partially offset by an increase in average interest-earning assets. The net interest margin decreased by 11 basis points to 3.44% for the three months ended June 30, 2012 reflecting the downward re-pricing of certain fixed-rate loans and investments as a result of the lower interest rate environment, offset in part by reduced funding costs. Total average interest-earning assets increased \$37.7 million, or 2.5%, to \$1.55 billion for the second quarter of 2012, mainly due to growth in commercial loans and interest-earning cash balances, partially offset by a decrease in investment securities.

**Interest Income.** Interest income decreased \$1.1 million, or 6.2%, to \$17.0 million for the three months ended June 30, 2012 from \$18.1 million for the prior year period due to a lower yield on average interest-earning assets, partially offset by growth in average interest-earning assets. The

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yield on average interest-earning assets decreased by 41 basis points to 4.39% for the second quarter of 2012 in connection with the lower interest rate environment. The decrease in market rates contributed to the downward repricing of a portion of the Company's existing assets and to lower rates for new assets.

**Interest Expense.** Interest expense decreased \$1.0 million, or 21.9%, to \$3.7 million for the three months ended June 30, 2012 from \$4.7 million for the prior year period reflecting a decrease in the average rate paid on interest-bearing liabilities, partially offset by an increase in average interest-bearing liabilities. The average rate paid on interest-bearing liabilities declined 37 basis points to 1.24% for the three months ended June 30, 2012 due to the repricing of deposits in response to the lower interest rate environment. Average interest-bearing liabilities increased \$20.4 million, or 1.7%, to \$1.20 billion for the three months ended June 30, 2012 from \$1.18 billion for the prior year period as a result of growth of \$51.0 million, or 5.2%, in interest-bearing deposits and a \$4.1 million, or 8.2%, increase in other interest-bearing liabilities. These increases were partially offset by a decrease of \$34.6 million, or 25.0%, in average FHLBB advances as a result of payoffs of maturing advances.

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**Provision for Loan Losses.** The allowance for loan losses is based on management's estimate of the probable losses inherent in the portfolio, considering the impact of certain factors. Among the factors management considers are prior loss experience, current economic conditions and their effect on borrowers, the composition and size of the portfolio, trends in non-performing loans, classified and impaired loans, and delinquency rates and the performance of individual loans in relation to contractual terms. The provision for loan losses reflects adjustments to the allowance based on management's review of the loan portfolio in light of those conditions. The provision for loan losses increased by \$77,000, or 11.4%, to \$750,000 for the three months ended June 30, 2012 from \$673,000 for the same period in 2011, driven by strong loan growth and the continuing shift to a more commercially oriented loan portfolio, offset by a decrease in charge-offs. The allowance for loan losses was \$11.8 million, or 1.01% of loans outstanding at June 30, 2012. Excluding the impact of acquired loans, the ratio of the allowance for loan losses to total loans would have been 1.14%.

**Non-interest Income.** Non-interest income increased \$359,000, or 16.2%, to \$2.6 million for the second quarter of 2012 from \$2.2 million for the same period in 2011. Fee income on depositors' accounts increased \$156,000, or 11.4%, driven by higher overdraft fees and growth in ATM and debit card income. Net gains from sales of loans increased \$112,000 due to an increase in sales of 30-year fixed rate loans and improved pricing. Wealth management income increased \$75,000, or 35.0% reflecting higher fee-based assets under management and transaction based commissions. Bank-owned life insurance income increased \$43,000, or 10.9%, reflecting the purchase of an additional \$10.0 million investment in the second quarter of 2011.

**Non-interest Expense.** Non-interest expense increased \$65,000, or 0.6%, to \$11.5 million for the second quarter of 2012 from \$11.4 million in the same period last year. Included in the 2012 second quarter were \$592,000 of acquisition related costs incurred in connection with the Company's proposed acquisition of New England Bancshares. Excluding these acquisition related costs, non-interest expense would have declined by \$527,000, or 4.6%. The low income housing tax credit fund expense decreased by \$197,000 due to a true-up of prior period expenses. Other expenses decreased \$180,000, or 10.5%, reflecting a write-down to fair value of mortgage servicing rights and decreases in postage and contribution expenses. Marketing expense fell by \$134,000, or 21.1%, due to reduced newspaper advertising and other promotional activities. Salaries and benefits decreased by \$128,000, or 2.0%, mainly attributable to lower stock-based compensation, offset to a large extent by annual wage increases, a larger incentive accrual due to improved operating performance and staffing costs for a new loan production office opened in 2011. These items were partially reduced by a \$65,000, or 8.1%, increase in occupancy expense driven by higher building maintenance costs.

**Income Tax Expense.** Income tax expense increased \$237,000, or 28.7%, to \$1.1 million for the second quarter of 2012 from \$827,000 in the same period last year primarily due to an increase in pretax income and the effective tax rate. The effective tax rate increased to 29.2% in the second quarter of 2012 from 23.5% for the same period last year as acquisition related expenses totaling \$592,000 were non-deductible.

**Comparison of Operating Results for the Six Months Ended June 30, 2012 and 2011**

**Net Income.** Net income for the six months ended June 30, 2012 amounted to \$5.4 million, or \$0.36 per diluted share, compared to \$5.1 million, or \$0.33 per diluted share, for the same period in 2011. Excluding acquisition related expenses of \$592,000 (non tax deductible), net income would have increased by \$904,000, or 18.0%, to \$6.0 million, or \$0.40 per diluted share, for the first six months of 2012. The 2012 results were positively impacted by a \$783,000 increase in non-interest income and a \$221,000 increase in net interest income, as well as decreases of \$192,000 in non-interest expense (excluding acquisition related expenses) and \$81,000 in the provision for loan losses. These items were offset in part by an increase of \$373,000 in income tax expense.

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**Average Balances and Yields.** The following table sets forth average balance sheets, average yields and costs, and certain other information for the periods indicated. No tax-equivalent yield adjustments were made, as the effect thereof was not material. All average balances are daily average balances. Non-accrual loans were included in the computation of average balances, but have been reflected in the table as loans carrying a zero yield.

	Six Months Ended June 30,					
	Average Balance	2012 Interest and Dividends	Yield/ Cost	Average Balance	2011 Interest and Dividends	Yield/ Cost
(Dollars in thousands)						
<b>Interest-earning assets:</b>						
Loans:						
Residential real estate <sup>(1)</sup>	\$ 314,016	\$ 7,301	4.65%	\$ 315,871	\$ 7,912	5.01%
Commercial real estate	494,952	13,819	5.58%	458,513	13,771	6.01%
Home equity	136,709	2,455	3.59%	138,134	2,637	3.82%
Commercial and industrial	182,016	4,290	4.71%	165,976	4,355	5.25%
Consumer and other	14,650	391	5.34%	18,591	515	5.54%
Total loans <sup>(2)</sup>	1,142,343	28,256	4.95%	1,097,085	29,190	5.32%
Investment securities	339,246	5,622	3.31%	349,182	6,578	3.77%
Other interest-earning assets	54,986	92	0.33%	55,468	78	0.28%
Total interest-earning assets	1,536,575	33,970	4.42%	1,501,735	35,846	4.77%
Noninterest-earning assets <sup>(3)</sup>	103,959			89,238		
Total assets	\$ 1,640,534			\$ 1,590,973		
<b>Interest-bearing liabilities:</b>						
Savings accounts	\$ 257,982	704	0.55%	\$ 222,585	848	0.76%
Money market accounts	304,592	808	0.53%	265,829	998	0.75%
NOW accounts	52,009	82	0.32%	40,263	81	0.40%
Certificates of deposit	417,639	3,757	1.80%	450,615	4,564	2.03%
Total interest-bearing deposits	1,032,222	5,351	1.04%	979,292	6,491	1.33%
FHLB advances	104,467	1,641	3.14%	143,022	2,548	3.56%
Other interest-bearing liabilities	52,880	584	2.21%	50,968	634	2.49%
Total interest-bearing liabilities	1,189,569	7,576	1.27%	1,173,282	9,673	1.65%
Demand deposits	211,810			183,033		
Other noninterest-bearing liabilities	11,301			9,976		
Total liabilities	1,412,680			1,366,291		
Stockholders' equity	227,854			224,682		
Total liabilities and stockholders' equity	\$ 1,640,534			\$ 1,590,973		
Net interest income		\$ 26,394			\$ 26,173	
Interest rate spread <sup>(4)</sup>			3.15%			3.13%
Net interest-earning assets <sup>(5)</sup>	\$ 347,006			\$ 328,453		
Net interest margin <sup>(6)</sup>			3.44%			3.49%

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Average interest-bearing assets to average interest-bearing liabilities

129.17%

127.99%

- (1) Includes loans held for sale.
- (2) Loans, including non-accrual loans, are net of deferred loan origination costs and advanced funds.
- (3) Includes bank-owned life insurance, the income on which is classified as non-interest income.
- (4) Net interest rate spread represents the difference between the yield on average interest-earning assets and the cost of average interest-bearing liabilities.
- (5) Net interest-earning assets represent total interest-earning assets less total interest-bearing liabilities.
- (6) Net interest margin represents annualized net interest income divided by average total interest-earning assets.

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**Rate/Volume Analysis.** The following table presents the effects of changing rates and volumes on our net interest income for the periods indicated. The rate column shows the effects attributable to changes in rate (changes in rate multiplied by prior volume). The volume column shows the effects attributable to changes in volume (changes in volume multiplied by prior rate). The net column represents the sum of the prior columns. For purposes of this table, changes attributable to both rate and volume, which cannot be segregated, have been allocated proportionately, based on the changes due to rate and the changes due to volume.

	<b>Six Months Ended June 30, 2012 vs. 2011</b>		
	<b>Increase (Decrease) Due to Volume</b>	<b>Increase (Decrease) Due to Rate</b>	<b>Net</b>
	<b>(In thousands)</b>		
<b>Interest-earning assets:</b>			
Loans:			
Residential real estate <sup>(1)</sup>	\$ (46)	\$ (565)	\$ (611)
Commercial real estate	1,053	(1,005)	48
Home equity loans	(27)	(155)	(182)
Commercial and industrial	400	(465)	(65)
Consumer and other	(106)	(18)	(124)
<b>Total loans</b>	<b>1,274</b>	<b>(2,208)</b>	<b>(934)</b>
Investment securities	(183)	(773)	(956)
Other interest-earning assets	(1)	15	14
<b>Total interest-earning assets</b>	<b>1,090</b>	<b>(2,966)</b>	<b>(1,876)</b>
<b>Interest-bearing liabilities:</b>			
Savings accounts	121	(265)	(144)
Money market accounts	132	(322)	(190)
NOW accounts	21	(20)	1
Certificates of deposit	(319)	(488)	(807)
<b>Total interest-bearing deposits</b>	<b>(45)</b>	<b>(1,095)</b>	<b>(1,140)</b>
FHLB advances	(631)	(276)	(907)
Other interest-bearing liabilities	23	(73)	(50)
<b>Total interest-bearing liabilities</b>	<b>(653)</b>	<b>(1,444)</b>	<b>(2,097)</b>
<b>Change in net interest income</b>	<b>\$ 1,743</b>	<b>\$ (1,522)</b>	<b>\$ 221</b>

(1) Includes loans held for sale.

**Net Interest Income Before Provision for Loan Losses.** Net interest income before provision for loan losses increased \$221,000, or 0.8%, to \$26.4 million for the six months ended June 30, 2012 from \$26.2 million for the comparable 2011 period as a result of growth in average interest-earning assets, offset in part by net interest margin compression. Total average interest-earning assets increased \$34.8 million, or 2.3%, to \$1.54 billion for the six months ended June 30, 2012, mainly due to growth in commercial loan balances, partially offset by a decrease in investment securities and interest-earning cash balances. The net interest margin decreased 5 basis points to 3.44% for the six months ended June 30, 2012 from 3.49% for the prior year period primarily attributable to the downward repricing of certain fixed rate loans and investments as a result of the lower interest rate environment. These items were partially offset by lower funding costs.

**Interest Income.** Interest income decreased \$1.9 million, or 5.2%, to \$34.0 million for the six months ended June 30, 2012 from \$35.8 million for the prior year period due to a decrease in the yield on earning assets partially offset by an increase in average interest-earning assets. The

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yield on average interest-earning assets decreased by 35 basis points to 4.42% for the second quarter of 2012 in connection with the lower interest rate environment. The decrease in market rates contributed to the downward repricing of a portion of the Company's existing assets and to lower rates for new assets.



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**Interest Expense.** Interest expense decreased \$2.1 million, or 21.7%, to \$7.6 million for the six months ended June 30, 2012 from \$9.7 million for the prior year period due to a decrease in the average rate paid on interest-bearing liabilities, partially offset by growth in average interest-bearing liabilities. The average rate paid on interest-bearing liabilities declined 38 basis points to 1.27% for the six months ended June 30, 2012 reflecting the repricing of deposits in response to the lower interest rate environment. Average interest-bearing liabilities increased \$16.3 million, or 1.4%, to \$1.19 billion for the six months ended June 30, 2012 from \$1.17 billion for the prior year period reflecting growth of \$52.9 million, or 5.4%, in interest-bearing deposits. The increase in average interest-bearing deposits was offset in part by a reduction of \$38.6 million, or 27.0%, in average FHLB advances to \$104.5 million for the six months ended June 30, 2012 as a result of payoffs of maturing advances.

**Provision for Loan Losses.** The provision for loan losses decreased \$81,000, or 5.5%, to \$1.4 million for the six months ended June 30, 2012, from \$1.5 million for the same period in 2011, driven by reductions in loan loss reserve factors, charge-offs, and classified loans, partially offset by increased origination activity and a shift to a more commercial oriented portfolio. The decrease in loan loss reserve factors reflects improving asset quality trends and positive changes in economic conditions.

**Non-interest Income.** Non-interest income increased \$783,000, or 18.0%, to \$5.1 million for the six months ended June 30, 2012. Fee income on depositors' accounts increased \$272,000, or 10.2%, driven by higher overdraft fees and growth in ATM and debit card income. Net gains from sales of loans increased \$197,000 due to an increase in sales of 30-year fixed rate loans and improved pricing. Bank-owned life insurance income increased \$152,000, or 21.0%, reflecting the purchase of an additional \$10.0 million investment in the second quarter of 2011. Wealth management income increased \$62,000, or 13.7%, reflecting higher fee-based assets under management and transaction-based commissions.

**Non-interest Expense.** Non-interest expense increased \$400,000, or 1.8%, to \$22.7 million for the six months ended June 30, 2012 from \$22.3 million for the prior year period. Excluding acquisition related costs of \$592,000, non-interest expense would have declined by \$192,000, or 0.9%. Professional fees decreased by \$158,000, or 14.8%, related to lower legal and consulting activities. The low income housing tax credit fund expense decreased by \$152,000 due to a true-up of prior period expenses. Marketing expense decreased by \$141,000, or 13.0%, due to reduced newspaper advertising and other promotional activities. These items were partially reduced by a \$98,000, or 3.4%, increase in other expense related to higher levels of depreciation and writedowns of mortgage servicing rights to fair value, a \$95,000, or 5.8%, increase in occupancy expense driven by higher building maintenance costs and a \$45,000, or 0.4%, increase in salaries and benefits due to annual wage increases, staffing costs related to the new loan production office and a higher incentive compensation accrual, offset in part by lower stock-based compensation.

**Income Tax Expense.** Income tax expense increased \$373,000 to \$2.0 million for six months ended June 30, 2012 from \$1.6 million for the comparable 2011 period primarily due to higher pretax income and the effective tax rate. The effective tax rate increased to 26.5% for the six months ended June 30, 2012 from 23.7% for the same period last year as acquisition related expenses totaling \$592,000 were non-deductible.

## **Market Risk, Liquidity and Capital Resources**

### **Market Risk**

The majority of our assets and liabilities are monetary in nature. Consequently, our most significant form of market risk is interest rate risk ( IRR ). Our assets, the largest portion of which are mortgage loans, have longer maturities than our liabilities, consisting primarily of deposits. As a result, a principal part of our business strategy is to manage IRR and reduce the exposure of our net interest income ( NII ) to changes in market interest rates. Accordingly, our Board of Directors has established an Asset/Liability Management Committee, which is responsible for evaluating the IRR inherent in our assets and liabilities, for determining the level of risk that is appropriate given our business strategy, operating environment, capital, liquidity and performance objectives, and for managing this risk consistent with the guidelines approved by the Board of Directors. With the assistance of an IRR management consultant, the committee monitors the level of IRR on a regular basis and meets at least quarterly to review our asset/liability policies and IRR position.

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We have sought to manage our IRR in order to minimize the exposure of our earnings and capital to changes in interest rates. As part of our ongoing asset-liability management, we currently use the following strategies to manage our IRR: (i) using alternative funding sources, such as advances from the FHLBB, to match fund certain longer-term loans; (ii) continued emphasis on increasing core deposits; (iii) offering adjustable-rate and shorter-term residential real estate, home equity loans, commercial real estate loans, construction loans and commercial and industrial loans; (iv) offering a variety of consumer loans, which typically have shorter-terms; (v) investing in mortgage-backed securities with variable rates or fixed rates with shorter durations; and (vi) sales of thirty-year fixed-rate residential real estate loans. Reducing the average maturity of our interest-earning assets by increasing our investments in shorter-term loans and securities, as well as loans and securities with variable rates of interest, helps to better match the maturities and interest rates of our assets and liabilities, thereby reducing the exposure of our NII to changes in market interest rates.

Net interest income at-risk measures the risk of a decline in earnings due to potential short-term and long term changes in interest rates. The table below represents an analysis of our IRR as measured by the estimated changes in NII for the following twelve months, resulting from an instantaneous and sustained parallel shift in the yield curve of +200 and -100 basis points at June 30, 2012 and December 31, 2011.

Change in Interest Rates (Basis Points)	Net Interest Income At-Risk	
	Estimated Increase (Decrease) in NII (June 30, 2012)	Estimated Increase (Decrease) in NII (December 31, 2011)
-100	(3.4)%	(3.9)%
Stable	0.0%	0.0%
+200	2.7%	(0.3)%

The preceding income simulation analysis is for the Bank and its subsidiaries only and does not represent a forecast of NII and should not be relied upon as being indicative of expected operating results. These hypothetical estimates are based upon numerous assumptions, which are subject to change, including: the nature and timing of interest rate levels including the yield curve shape, prepayments on loans and securities, deposit decay rates, pricing decisions on loans and deposits, reinvestment/replacement of asset and liability cash flows, and others. Also, market conditions, prepayment/refinancing levels, the varying impact of interest rate changes on caps and floors embedded in adjustable rate loans, early withdrawal of deposits, changes in product preferences, and other internal/external variables and other factors may vary significantly from assumptions used.

**Economic Value of Equity Simulation Analysis.** The computation of amounts by which the net present value of an institution's cash flows from assets, liabilities and off-balance sheet items (the institution's economic value of equity or EVE) would change in the event of a range of assumed changes in market interest rates. The model has estimated the economic value of each type of asset, liability and off-balance sheet contract under the assumption that the United States Treasury yield curve increases or decreases instantaneously by 100 to 300 basis points in 100 basis point increments. However, given the low level of market interest rates, an economic value of equity calculation for an interest rate decrease of greater than 100 basis points was not prepared. A basis point equals one-hundredth of one percent, and 200 basis points equals two percent. An increase in interest rates from 3% to 5% would mean, for example, a 200 basis point increase in the Change in Interest Rates column below.

The tables below set forth, at the dates indicated, the estimated changes in our economic value of equity that would result from the designated instantaneous changes in the United States Treasury yield curve.

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Computations of prospective effects of hypothetical interest rate changes are based on numerous assumptions, including relative levels of market interest rates, loan prepayments and deposit decay, and should not be relied upon as indicative of actual results. This data is for the Bank and its subsidiaries only and does not include any yield curve changes in the assets of United Financial.

June 30, 2012					
Change in Interest Rates (basis points) (1)	Estimated EVE (2)	Estimated Increase (Decrease) in EVE		EVE as a Percentage of Present Value of Assets (3)	
		Amount (Dollars in thousands)	Percent	EVE Ratio (4)	Increase (Decrease) (basis points)
+300	\$ 176,338	\$ (51,936)	(23)%	11.35%	(228)
+200	207,282	(20,992)	(9)	12.96	(68)
+100	224,905	(3,368)	(1)	13.71	8
0	228,274			13.64	
-100	234,644	6,370	3	13.77	14

December 31, 2011					
Change in Interest Rates (basis points) (1)	Estimated EVE (2)	Estimated Increase (Decrease) in EVE		EVE as a Percentage of Present Value of Assets (3)	
		Amount (Dollars in thousands)	Percent	EVE Ratio (4)	Increase (Decrease) (basis points)
+300	\$ 183,875	\$ (53,540)	(23)%	12.06%	(241)
+200	213,647	(23,768)	(10)	13.61	(86)
+100	231,936	(5,479)	(2)	14.42	(6)
0	237,415			14.47	
-100	239,393	1,978	1	14.38	(10)

(1) Assumes an instantaneous uniform change in interest rates at all maturities.

(2) EVE is the discounted present value of expected cash flows from assets, liabilities and off-balance sheet contracts.

(3) Present value of assets represents the discounted present value of incoming cash flows on interest-earning assets.

(4) EVE ratio represents EVE divided by the present value of assets.

The tables above indicate that at June 30, 2012 and December 31, 2011, in the event of a 300 basis point increase in interest rates, we would experience a 23% decrease in economic value of equity. In the event of a 100 basis point decrease in interest rates at June 30, 2012 and December 31, 2011, we would experience a 3% and 1%, respectively, increase in economic value of equity.

Certain shortcomings are inherent in the methodology used in the above interest rate risk measurement. Modeling changes in economic value of equity require making certain assumptions that may or may not reflect the manner in which actual yields and costs respond to changes in market interest rates. In this regard, the economic value of equity table presented assumes that the composition of our interest-sensitive assets and liabilities existing at the beginning of a period remains constant over the period being measured and assumes that a particular change in interest rates is reflected uniformly across the yield curve regardless of the duration or repricing of specific assets and liabilities. Accordingly, although the economic value of equity table provides an indication of our interest rate risk exposure at a particular point in time, such measurements are not intended to and do not provide a precise forecast of the effect of changes in market interest rates on our net interest income and will differ from actual results.



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***Liquidity***

Liquidity is the ability to meet current and future financial obligations of a short-term nature. Our primary sources of funds consist of deposit inflows, advances from the FHLBB, loan and mortgage-backed security repayments and maturities and sales of loans and investment securities. While maturities and scheduled amortization of loans and securities are predictable sources of funds, deposit flows, mortgage prepayments and loan and investment sales are greatly influenced by market interest rates, economic conditions and competition. Our Asset/Liability Management Committee is responsible for establishing and monitoring our liquidity targets and strategies in order to ensure that sufficient liquidity exists for meeting the borrowing needs of our customers as well as unanticipated contingencies. We seek to maintain a liquidity ratio (defined as the sum of cash and liquid assets divided by the sum of total deposits and short-term interest-bearing liabilities) of 10% or greater. At June 30, 2012, our liquidity ratio was 19.68%, compared to 21.00% at December 31, 2011.

We regularly adjust our investments in liquid assets based upon our assessment of (1) expected loan demand, (2) expected deposit flows, (3) yields available on interest-earning deposits and securities, and (4) the objectives of our asset/liability management program. Excess liquid assets are generally invested in interest-earning deposits and short- and intermediate-term securities.

Our most liquid assets are cash and cash equivalents. The levels of these assets are dependent on our operating, financing, lending and investing activities during any given period. At June 30, 2012, cash and cash equivalents totaled \$42.4 million. Securities classified as available for sale and held to maturity, which provide additional sources of liquidity, totaled \$243.9 million and \$99.4 million, respectively, at June 30, 2012. In addition, at June 30, 2012, we had the ability to borrow a total of approximately \$197.0 million from the FHLBB. On that date, we had \$101.8 million in advances outstanding.

Our cash flows are derived from operating activities, investing activities and financing activities as reported in our Consolidated Statements of Cash Flows included in our Consolidated Financial Statements.

At June 30, 2012, we had \$36.2 million in loan commitments outstanding. In addition to commitments to originate loans, we had \$256.0 million in unused lines of credit to borrowers, \$3.3 million in standby letters of credit and \$20.4 million to be disbursed under existing construction loan commitments. Certificates of deposit due within one year of June 30, 2012 totaled \$244.0 million, or 19.4% of total deposits. If these deposits do not remain with us, we will be required to seek other sources of funds, including other certificates of deposit, FHLBB advances, borrowings from the Federal Reserve Bank and repurchase agreements. Depending on market conditions, we may be required to pay higher rates on such deposits or other borrowings than we currently pay on the certificates of deposit due on or before June 30, 2013. We believe however, based on past experience, that a significant portion of our certificates of deposit will remain with us. We have the ability to attract and retain deposits by adjusting the interest rates offered.

Our primary investing activities are the origination of loans and the purchase of securities. For the six months ended June 30, 2012, we originated \$174.5 million of loans and purchased \$51.8 million of securities. In the comparable 2011 period, we originated \$122.5 million of loans and purchased \$66.5 million of securities.

Financing activities consist primarily of activity in deposit accounts and FHLBB advances. We experienced a net increase in total deposits of \$30.6 million and \$46.0 million for the six months ended June 30, 2012 and 2011, respectively. Deposit flows are affected by the overall level of interest rates, the interest rates and products offered by us and our local competitors and other factors. FHLBB advances decreased by \$3.5 million and \$18.5 million during the six months ended June 30, 2012 and 2011, respectively, reflecting the use of cash flows received from the loan and investment portfolios and excess deposit funds to pay down FHLBB advances.

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Liquidity management is both a daily and long-term function of business management. If we require funds beyond our ability to generate them internally, borrowing agreements exist with the FHLBB, which provides an additional source of funds. We have also used FHLBB advances to match-fund certain longer-term one- to four-family residential mortgage loans and commercial real estate loans. The Bank's unused borrowing capacity with the FHLBB, excluding its available line of credit balance of \$12.0 million at June 30, 2012 and December 31, 2011, was approximately \$83.2 million at June 30, 2012 and \$107.1 million at December 31, 2011. At June 30, 2012 and December 31, 2011, the Bank had no borrowings against the line of credit. We also have access to funding through the repurchase agreement and brokered CD markets and have received approval from the Federal Reserve Bank to access its discount window. The Bank's unused borrowing capacity with the Federal Reserve Bank was approximately \$79.1 million at June 30, 2012.

United Financial is a separate legal entity from the Bank and must provide for its own liquidity. In addition to its operating expenses, United Financial is responsible for paying any dividends declared to its shareholders and to its holders of its subordinated debenture. United Financial also repurchases shares of its common stock. At June 30, 2012, United Financial on an unconsolidated basis had liquid assets of \$14.5 million.

***Off-Balance Sheet Arrangements and Aggregate Contractual Obligations***

**Commitments**

As a financial services provider, we routinely are a party to various financial instruments with off-balance-sheet risks, such as commitments to extend credit, standby letters of credit and unused lines of credit. While these contractual obligations represent our future cash requirements, a significant portion of commitments to extend credit may expire without being drawn upon. Such commitments are subject to the same credit policies and approval process accorded to loans made by us. We consider commitments to extend credit in determining our allowance for loan losses.

**Table of Contents****Contractual Obligations**

In the ordinary course of our operations, we enter into certain contractual obligations. Such obligations include operating leases for premises and equipment. The following table summarizes our significant fixed and determinable contractual obligations and other funding needs by payment date at June 30, 2012. The payment amounts represent those amounts due to the recipient and do not include any unamortized premiums or discounts or other similar carrying amount adjustments.

	Payments Due by Period (In Thousands)				Total
	Less Than One Year	One to Three Years	Three to Five Years	More than Five Years	
<b>Contractual Obligations:</b>					
Certificates of deposit	\$ 244,047	\$ 140,876	\$ 30,782	\$	\$ 415,705
Federal Home Loan Bank advances	23,940	44,904	14,911	18,000	101,755
Repurchase agreements	17,772			20,000	37,772
Subordinated debentures				7,732	7,732
Standby letters of credit	3,345				3,345
Operating leases	1,041	1,979	1,419	3,459	7,898
Capitalized leases	423	847	848	5,985	8,103
Future benefits to be paid under retirement plans	1,064	2,999	1,289	4,679	10,031
Total	\$ 291,632	\$ 191,605	\$ 49,249	\$ 59,855	\$ 592,341
<b>Commitments:</b>					
Commitments to extend credit	\$ 315,946	\$	\$	\$	\$ 315,946
Investment in venture capital fund	300				300
Investment in low income tax credit fund	4,105	413			4,518
Total	\$ 320,351	\$ 413	\$	\$	\$ 320,764

**Capital Resources**

The Bank is subject to various regulatory capital requirements, including a risk-based capital measure. The risk-based capital guidelines include both a definition of capital and a framework for calculating risk-weighted assets by assigning balance sheet assets and off-balance sheet items to broad risk categories. At June 30, 2012, the Bank exceeded all regulatory capital requirements and was considered well capitalized under regulatory requirements.

	Actual	For Capital Adequacy Purposes	To Be Well Capitalized Under Regulatory Framework
<b>As of June 30, 2012:</b>			
Total risk-based capital	15.23%	8.00%	10.00%
Tier 1 risk-based capital	14.32%	4.00%	6.00%
Tier 1 (core) capital	11.31%	4.00%	5.00%
Tangible equity	11.31%	1.50%	N/A
<b>As of December 31, 2011:</b>			
Total risk-based capital	17.09%	8.00%	10.00%
Tier 1 risk-based capital	16.17%	4.00%	6.00%
Tier 1 (core) capital	12.23%	4.00%	5.00%
Tangible equity	12.23%	1.50%	N/A

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### **ITEM 3. Quantitative and Qualitative Disclosures About Market Risk**

The information required by this item is included above in Item 2, Management's Discussion and Analysis of Financial Condition and Results of Operations, under the caption Market Risk, Liquidity and Capital Resources.

### **ITEM 4. Controls and Procedures**

Under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer, the Company has evaluated the effectiveness of the design and operation of its disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d-15(e) under the Exchange Act) as of the end of the period covered by this report. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that, as of the end of the period covered by this report, the Company's disclosure controls and procedures were effective to ensure that information required to be disclosed in the reports that the Company files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms and in a timely manner alerting them to material information relating to the Company (or its consolidated subsidiary) required to be filed in its periodic SEC filings.

No change in our internal controls over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934) occurred during the most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting. In the ordinary course of business, we routinely enhance our internal controls and procedures for financial reporting by either upgrading our current systems or implementing new systems. Changes have been made and will be made to our internal controls and procedures for financial reporting as a result of these efforts.

## **PART II. OTHER INFORMATION**

### **ITEM 1. Legal Proceedings**

The Bank, as successor in interest to Commonwealth National Bank, is involved in litigation relating to its foreclosure on a certain loan property. The litigants claim that Commonwealth National Bank acted in bad faith and in violation of applicable law and that its actions resulted in a sale of the underlying property for less than its market value, thereby causing damage to the parties. A trial was held in the third quarter of 2011 and the judge ruled in the Bank's favor. The litigants have appealed the decision. The Bank believes these claims and the appeal are without merit and is vigorously defending the litigation. No estimate of any reasonably possible loss or range of loss to the Bank can be made at this time.

The Bank is also a defendant in other claims and legal actions arising in the ordinary course of business. In the opinion of management, after consultation with legal counsel, the ultimate disposition of these matters is not expected to have a material adverse effect on the Company's financial condition, results of operations or cash flows.

### **ITEM 1A. Risk Factors**

In addition to the other information set forth in this report, the factors discussed in Part I, Item 1A. Risk Factors in our Annual Report on Form 10-K for the year ended December 31, 2011, which could materially affect our business, financial condition or future results, should be carefully considered. At June 30, 2012, the risk factors for the Company have not changed materially from those reported in our Annual Report on Form 10-K.



**Table of Contents****ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds**

(a) No unregistered securities were sold by the Company during the quarter ended June 30, 2012.

(b) Not applicable.

(c) The following table provides certain information with regard to shares repurchased by the Company in the second quarter of 2012.

Period	(a) Total Number of Shares (or Units) Purchased	(b) Average Price Paid Per Share (or Unit)	(c) Total Number of Shares (or Units) Purchased as Part of Publicly Announced Plans or Programs	(d) Maximum Number (or Approximate Dollar Value) of Shares (or Units) that May Yet Be Purchased Under the Plans or Programs (1)
April 1 - 30, 2012	70,200	\$ 15.84	70,200	130,703
May 1 - 31, 2012				130,703
June 1 - 30, 2012	10,834 (2)	13.68		130,703
Total	81,034	\$ 15.56	70,200	

- (1) On October 26, 2010, the Board of Directors approved a plan to repurchase up to 5%, or approximately 807,803 shares, of the Company's common stock. Under the plan, the Company intends to repurchase shares from time to time, depending on market conditions until it is completed. As of June 30, 2012, the Company has repurchased 677,100 shares at a cost of approximately \$10.3 million and an average price of \$15.14 per share, under this plan.
- (2) Represents withholdings subject to restricted stock awards under the United Financial Bancorp, Inc. 2008 Equity Incentive Plan as payment of taxes due upon the vesting of the restricted stock awards.

**ITEM 3. Defaults Upon Senior Securities**

Not applicable.

**ITEM 4. Mine Safety Disclosures**

Not applicable.

**ITEM 5. Other Information**

Not applicable.

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**ITEM 6. Exhibits.**

- 3.1 Articles of Incorporation of United Financial Bancorp, Inc. (1)
  - 3.2 Amended and Restated Bylaws of United Financial Bancorp, Inc. (2)
  - 4.0 Form of Common Stock Certificate of United Financial Bancorp, Inc. (1)
  - 31.1 Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer
  - 31.2 Rule 13a-14(a)/15d-14(a) Certification of Chief Financial Officer
  - 32.0 Section 1350 Certification of Chief Executive Officer and Chief Financial Officer
  - 101.0 The following materials from the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2012, formatted in XBRL (Extensible Business Reporting Language): (i) the Consolidated Statements of Condition, (ii) the Consolidated Statements of Earnings, (iii) the Consolidated Statement of Changes in Equity and Comprehensive Income, (iv) the Consolidated Statements of Cash Flows and (v) the Notes to the Consolidated Financial Statements.\*
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- (1) Incorporated by reference to the Registration Statement on Form S-1 of United Financial Bancorp, Inc. (File No. 333-144245), originally filed with the Securities and Exchange Commission on June 29, 2007.
  - (2) Incorporated by reference to the Form 10-K of United Financial Bancorp, Inc. filed with the Securities and Exchange Commission on March 13, 2009.
- \* Furnished, not filed

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**SIGNATURES**

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

**United Financial Bancorp, Inc.**

Date: August 8, 2012

By: /s/ Richard B. Collins  
Richard B. Collins  
Chairman, President and Chief Executive Officer

Date: August 8, 2012

By: /s/ Mark A. Roberts  
Mark A. Roberts  
Executive Vice President and Chief Financial Officer