PATRIOT NATIONAL BANCORP INC
Form 10-Q
November 10, 2011

Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q
QUARTERLY REPORT UNDER SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934
For the Quarter Ended September 30, 2011
Commission file number 000-29599
PATRIOT NATIONAL BANCORP, INC.
(Exact name of registrant as specified in its charter)

Connecticut	06-1559137
(State of incorporation)	(I.R.S. Employer Identification Number)

900 Bedford Street, Stamford, Connecticut 06901
(Address of principal executive offices)
(203) 324-7500
(Registrant s telephone number)

Check whether the registrant (1) filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the past 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 þ No o

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 þ No o

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

Large Accelerated Filer o	Accelerated Filer o	Non-Accelerated Filer o	Smaller Reporting Company þ

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act):

Yes o No þ

State the number of shares outstanding of each of the registrant s classes of common equity, as of the latest practicable date.

Common stock, $0.01 par value per share, 38,362,727 shares outstanding as of the close of business October 31, 2011.

Table of Contents

Table of Contents

PART I FINANCIAL INFORMATION
Item 1: Consolidated Financial Statements
PATRIOT NATIONAL BANCORP, INC.
CONSOLIDATED BALANCE SHEETS

	September 30, 2011 (Unaudited)	December 31, 2010
ASSETS		
Cash and due from banks:		
Noninterest bearing deposits and cash	$ 9,497,603	$ 4,613,211
Interest bearing deposits	30,484,856	131,711,047
Federal funds sold		10,000,000
Short-term investments	3,206,016	453,400
Total cash and cash equivalents	43,188,475	146,777,658
Securities:		
Available for sale securities, at fair value (Note 2)	88,529,050	40,564,700
Other Investments	3,500,000	3,500,000
Federal Reserve Bank stock, at cost	1,707,000	1,192,000
Federal Home Loan Bank stock, at cost	4,508,300	4,508,300
Total securities	98,244,350	49,765,000
Loans receivable (net of allowance for loan losses: 2011: $11,157,678; 2010: $15,374,101) (Note 3)	453,133,275	534,531,213
Loans held for sale	250,000	
Accrued interest and dividends receivable	2,320,572	2,512,186
Premises and equipment, net	4,180,814	5,270,312
Cash surrender value of life insurance	20,839,710	20,348,332
Other real estate owned	4,731,890	16,408,787
Deferred tax asset (Note 9)		
Other assets	1,537,619	8,711,366
Total assets	$ 628,426,705	$ 784,324,854
LIABILITIES AND SHAREHOLDERS EQUITY		
Liabilities		
Deposits (Note 4):		
Noninterest bearing deposits	$ 56,699,418	$ 51,058,373
Interest bearing deposits	451,023,611	595,750,456
Total deposits	507,723,029	646,808,829
Borrowings:		
Repurchase agreements	7,000,000	7,000,000
Federal Home Loan Bank borrowings	50,000,000	50,000,000

Total borrowings		**57,000,000**		57,000,000
Junior subordinated debt owed to unconsolidated trust		**8,248,000**		8,248,000
Accrued expenses and other liabilities		**4,785,687**		5,095,837
Total liabilities		**577,756,716**		717,152,666
Commitments (Note 7)				
Shareholders equity				
Preferred stock, no par value; 1,000,000 shares authorized, no shares issued and outstanding				
Common stock, $.01 par value, 100,000,000 shares authorized; 38,374,432 shares issued; 38,362,727 shares outstanding		**383,744**		383,744
Additional paid-in capital		**105,050,433**		105,050,433
Accumulated deficit		**(55,301,852)**		(39,399,345)
Less: Treasury stock, at cost: 2011 and 2010, 11,705 shares		**(160,025)**		(160,025)
Accumulated other comprehensive income		**697,689**		1,297,381
Total shareholders equity		**50,669,989**		67,172,188
Total liabilities and shareholders equity	**$**	**628,426,705**	$	784,324,854

See Accompanying Notes to Consolidated Financial Statements.

Table of Contents

PATRIOT NATIONAL BANCORP, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

	Three Months Ended September 30, 2011	Three Months Ended September 30, 2010	Nine Months Ended September 30, 2011	Nine Months Ended September 30, 2010
Interest and Dividend Income				
Interest and fees on loans	$ 6,184,920	$ 7,977,476	$ 19,680,074	$ 26,011,835
Interest on investment securities	664,661	369,169	1,425,582	1,236,019
Dividends on investment securities	56,462	66,403	207,091	202,109
Interest on federal funds sold	464	4,428	6,875	12,275
Other interest income	1,485	51,436	121,738	104,706
Total interest and dividend income	**6,907,992**	**8,468,912**	**21,441,360**	**27,566,944**
Interest Expense				
Interest on deposits	1,384,540	2,765,030	4,803,634	8,830,894
Interest on Federal Home Loan Bank borrowings	428,183	428,183	1,270,587	1,270,587
Interest on subordinated debt	70,929	76,411	212,546	216,775
Interest on other borrowings	77,772	77,773	230,781	230,781
Total interest expense	**1,961,424**	**3,347,397**	**6,517,548**	**10,549,037**
Net interest income	**4,946,568**	**5,121,515**	**14,923,812**	**17,017,907**
Provision for Loan Losses		5,025,000	8,464,427	6,264,000
Net interest income after provision for loan losses	**4,946,568**	**96,515**	**6,459,385**	**10,753,907**
Non-interest Income				
Mortgage brokerage referral fees	13,500	22,465	28,110	76,139
Loan application, inspection & processing fees	20,656	21,947	61,421	115,448
Deposit fees and service charges	207,200	322,943	736,140	850,661
Gains on sale of loans			79,729	
Gains on sale of investment securities	779,685		779,685	
Earnings on cash surrender value of life insurance	170,133	161,014	491,378	429,848
Other income	90,306	108,727	398,180	264,096
Total non-interest income	**1,281,480**	**637,096**	**2,574,643**	**1,736,192**
Non-interest Expenses				
Salaries and benefits	2,840,195	3,192,396	9,244,021	9,745,036
Occupancy and equipment expense	1,038,883	1,371,108	3,685,276	4,207,405
Data processing	315,912	369,736	979,721	884,290
Advertising and promotional expenses	91,786	61,415	521,541	216,093
Professional and other outside services	545,612	566,204	2,662,277	2,508,648

Loan administration and processing expenses	88,373	41,460	173,591	217,676
Regulatory assessments	431,786	689,510	1,671,530	2,074,151
Insurance expense	227,173	194,399	686,584	598,798
Other real estate operations	(26,250)	454,608	1,018,707	1,760,235
Material and communications	163,240	195,900	527,493	597,763
Restructuring charges and asset disposals (Note 11)			2,986,441	
Other operating expenses	255,879	387,455	779,353	777,327
Total non-interest expenses	**5,972,589**	**7,524,191**	**24,936,535**	**23,587,422**
Income (loss) before income taxes	**255,459**	**(6,790,580)**	**(15,902,507)**	**(11,097,323)**
Provision for Income Taxes				225,000
Net income (loss)	**$ 255,459**	**$ (6,790,580)**	**$ (15,902,507)**	**$ (11,322,323)**
Basic and diluted income (loss) per share (Note 5)	**$ 0.01**	**$ (1.43)**	**$ (0.41)**	**$ (2.38)**

See Accompanying Notes to Consolidated Financial Statements.

4

Table of Contents

PATRIOT NATIONAL BANCORP, INC
CONSOLIDATED STATEMENTS OF SHAREHOLDERS EQUITY
(Unaudited)

	Number of Shares	Common Stock	Additional Paid-In Capital	Accumulated Deficit	Treasury Stock	Accumulated Other Comprehensive Income	Total
Nine months ended September 30, 2010							
Balance at December 31, 2009	4,762,727	$ 9,548,864	$ 49,651,534	$ (24,000,400)	$ (160,025)	$ 821,337	$ 35,861,310
Comprehensive loss							
Net loss				(11,322,323)			(11,322,323)
Unrealized holding gain on available for sale securities, net of taxes (Note 6)						626,012	626,012
Total comprehensive loss							(10,696,311)
Balance, September 30, 2010	4,762,727	$ 9,548,864	$ 49,651,534	$ (35,322,723)	$ (160,025)	$ 1,447,349	$ 25,164,999
Nine months ended September 30, 2011							
Balance at December 31, 2010	38,362,727	$ 383,744	$ 105,050,433	$ (39,399,345)	$ (160,025)	$ 1,297,381	$ 67,172,188
Comprehensive loss							

Net loss				(15,902,507)			(15,902,507)
Unrealized holding loss on available for sale securities, net of taxes (Note 6)						(599,692)	(599,692)
Total comprehensive loss							(16,502,199)
Balance, September 30, 2011	38,362,727	$ 383,744	$ 105,050,433	$ (55,301,852)	$ (160,025)	$ 697,689	$ 50,669,989

See Accompanying Notes to Consolidated Financial Statements.

Table of Contents

PATRIOT NATIONAL BANCORP, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Nine Months Ended September 30, 2011	Nine Months Ended September 30, 2010
Cash Flows from Operating Activities:		
Net loss	$ (15,902,507)	$ (11,322,323)
Adjustments to reconcile net loss to net cash used in operating activities:		
Restructuring charges and asset disposals	1,094,094	
Amortization and accretion of investment premiums and discounts, net	234,525	318,842
Amortization and accretion of purchase loan premiums and discounts, net	7,542	7,477
Provision for loan losses	8,464,427	6,264,000
Gain on sales of investments	(779,685)	
Gain on sale of loans	(79,729)	
Amortization of core deposit intangible	11,259	11,925
Earnings on cash surrender value of life insurance	(491,378)	(429,848)
Depreciation and amortization	974,798	1,131,641
Loss on disposal of fixed assets	2,624	
Loss on sale of other real estate owned	58,215	173,289
Impairment writedown on other real estate owned	165,764	961,497
Changes in assets and liabilities:		
Decrease (increase) in deferred loan costs	34,092	(237,165)
Decrease in accrued interest and dividends receivable	191,614	488,000
Decrease in other assets	7,162,488	500,942
Decrease in cash surrender value of life insurance		58,416
(Decrease) increase in accrued expenses and other liabilities	(466,973)	2,037,258
Net cash provided by (used in) operating activities	**681,170**	**(36,049)**
Cash Flows from Investing Activities:		
Purchases of available for sale securities	(65,459,630)	(15,162,500)
Purchases of other investments		(500,000)
Principal repayments on available for sale securities	7,316,078	5,819,337
Proceeds from redemptions of available for sale securities		10,000,000
Proceeds from sales of available for sale securities	9,757,118	
Purchases of Federal Reserve Bank Stock	(1,174,100)	
Redemptions of Federal Reserve Bank Stock	659,100	605,450
Proceeds from sale of loans	55,089,794	
Net decrease in loans	13,849,922	61,993,858
Purchase of other real estate owned	(481,165)	
Proceeds from sale of other real estate owned	15,715,973	11,423,343
Capital improvements of other real estate owned		(271,493)
Purchase of bank premises and equipment	(457,643)	(158,167)
Net cash provided by investing activities	**34,815,447**	**73,749,828**
Cash Flows from Financing Activities:		

Net decrease in demand, savings and money market deposits	(25,697,339)	(22,942,716)
Net decrease in time certificates of deposits	(113,388,461)	(47,424,309)
Net cash used in financing activities	**(139,085,800)**	**(70,367,025)**
Net (decrease) increase in cash and cash equivalents	**(103,589,183)**	**3,346,754**
Cash and Cash Equivalents:		
Beginning	146,777,658	107,799,432
Ending	$ 43,188,475	$ 111,146,186

6

Table of Contents

PATRIOT NATIONAL BANCORP, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS ,Continued
(Unaudited)

	Nine Months Ended September 30, 2011	Nine Months Ended September 30, 2010
Supplemental Disclosures of Cash Flow Information		
Interest paid	$ 6,319,721	$ 10,374,774
Income taxes paid	$ 10,534	$ 2,080
Supplemental disclosures of noncash investing and financing activities:		
Unrealized holding (loss) gain on available for sale securities arising during the period	$ (967,244)	$ 1,009,749
Transfer of loans to other real estate owned	$ 3,781,890	$ 556,600
Transfer of loans to held for sale	$ 250,000	$

See Accompanying Notes to Consolidated Financial Statements.

Table of Contents

PATRIOT NATIONAL BANCORP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

Note 1: Basis of Financial Statement Presentation

The Consolidated Balance Sheet at December 31, 2010 has been derived from the audited financial statements of Patriot National Bancorp, Inc. (Bancorp or the Company) at that date, but does not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements.

The accompanying unaudited financial statements and related notes have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. Accordingly, certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been omitted. The accompanying consolidated financial statements and related notes should be read in conjunction with the audited financial statements of Bancorp and notes thereto for the year ended December 31, 2010.

The information furnished reflects, in the opinion of management, all normal recurring adjustments necessary for a fair presentation of the results for the interim periods presented. The results of operations for the nine months September 30, 2011 are not necessarily indicative of the results of operations that may be expected for the remainder of 2011.

Note 2: Investment Securities

The amortized cost, gross unrealized gains, gross unrealized losses and approximate fair values of available-for-sale securities at September 30, 2011 and December 31, 2010 are as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
September 30, 2011:				
U. S. Government agency mortgage-backed securities	$ 70,131,473	$ 1,519,219	$ (5,694)	$ 71,644,998
U. S. Government agency bonds	5,000,000	36,100		5,036,100
Corporate bonds	12,272,271	212,749	(637,068)	11,847,952
	$ 87,403,744	$ 1,768,068	$ (642,762)	$ 88,529,050
December 31, 2010:				
U. S. Government agency mortgage-backed securities	$ 36,572,430	$ 900,286	$ (838)	$ 37,471,878
Auction rate preferred equity securities	1,899,720	1,193,102		3,092,822
	$ 38,472,150	$ 2,093,388	$ (838)	$ 40,564,700

Table of Contents

The following table presents the gross unrealized loss and fair value of Bancorp s available-for-sale securities, aggregated by the length of time the individual securities have been in a continuous loss position, at September 30, 2011 and December 31, 2010:

	Less Than 12 Months		12 Months or More		Total	
	Fair Value	**Unrealized Loss**	**Fair Value**	**Unrealized Loss**	**Fair Value**	**Unrealized Loss**
September 30, 2011:						
Corporate bonds	$ 5,362,932	$ (637,068)	$	$	$ 5,362,932	$ (637,068)
U. S. Government mortgage - backed securities	$ 4,662,632	$ (5,040)	$ 68,702	$ (654)	$ 4,731,334	$ (5,694)
Totals	$ 10,025,564	$ (642,108)	$ 68,702	$ (654)	$ 10,094,266	$ (642,762)
December 31, 2010:						
U. S. Government mortgage - backed securities	$ 86,375	$ (838)	$	$	$ 86,375	$ (838)
Totals	$ 86,375	$ (838)	$	$	$ 86,375	$ (838)

At September 30, 2011, 7 securities had unrealized holding losses with aggregate depreciation of 5.99% from the amortized cost. There was one security with unrealized losses greater than 5% of amortized cost. At December 31, 2010, two securities had unrealized losses with aggregate depreciation of 1.0% from the amortized cost. There were no securities with unrealized losses greater than 5% of amortized cost.

Bancorp performs a quarterly analysis of those securities that are in an unrealized loss position to determine if those losses qualify as other-than-temporary impairments. This analysis considers the following criteria in its determination: the ability of the issuer to meet its obligations, an impairment due to a deterioration in credit, management s plans and ability to maintain its investment in the security, the length of time and the amount by which the security has been in a loss position, the interest rate environment, the general economic environment and prospects or projections for improvement or deterioration.

Management believes that none of the unrealized losses on available-for-sale securities noted above are other than temporary due to the fact that they relate to interest rate changes on mortgage-backed securities issued by U.S. Government agencies, and generally weak economic news and global concerns regarding the financial services industry that is impacting the corporate bonds. Management considers the issuers of the mortgage-backed securities, as well as the corporate bonds, to be financially sound, and the Company expects to receive all contractual principal and interest related to these investments. Because the Company does not intend to sell the investments, and it is not more-likely-than-not that the Company will be required to sell the investments before recovery of their amortized cost basis, which may be maturity, the Company does not consider those investments to be other-than-temporarily impaired at September 30, 2011.

The amortized cost and fair value of available-for-sale debt securities at September 30, 2011, by contractual maturity, are presented below. Actual maturities of mortgage-backed securities may differ from contractual maturities because the mortgages underlying the securities may be repaid without any penalties. Because mortgage-backed securities are not due at a single maturity date, they are not included in the maturity categories in the following maturity summary:

	Amortized Cost	Fair Value
Maturity:		
> 10 years	$	$
Corporate bonds < 5 years	3,272,271	3,465,040
Corporate bonds 5 to 10 years	9,000,000	8,382,912
U. S. Government bonds 5 to 10 years	5,000,000	5,036,100
Mortgage-backed securities	70,131,473	71,644,998
Total	$ 87,403,744	$ 88,529,050

Note 3: Loans Receivable and Allowance for Loan Losses

A summary of the Company s loan portfolio at September 30, 2011 and December 31, 2010 is as follows:

	September 30, 2011	December 31, 2010
Real Estate		
Commercial	$ 210,128,617	$ 228,842,489
Residential	151,147,445	187,058,318
Construction	12,857,291	63,889,083
Construction to permanent	10,864,395	10,331,043
Commercial	28,553,155	14,573,790
Consumer home equity	48,225,020	42,884,962
Consumer installment	2,163,798	1,932,763
Total Loans	463,939,721	549,512,448
Premiums on purchased loans	234,884	242,426
Net deferred costs	116,348	150,440
Allowance for loan losses	(11,157,678)	(15,374,101)
Loans receivable, net	$ 453,133,275	$ 534,531,213

The changes in the allowance for loan losses for the periods shown are as follows:

	Three months ended September 30,		Nine months ended September 30,	
	2011	2010	2011	2010
Balance, beginning of period	$ 11,399,727	$ 13,989,069	$ 15,374,101	$ 15,794,118
Provision for loan losses		5,025,000	8,464,427	6,264,000
Loans charged-off	(217,788)	(1,917,286)	(7,405,926)	(5,094,670)
Recoveries of loans previously charged-off	16,086	53,345	779,736	186,680
Transferred to loans held-for-sale	(40,347)		(6,054,660)	
Balance, end of period	$ 11,157,678	$ 17,150,128	$ 11,157,678	$ 17,150,128

At September 30, 2011 and December 31, 2010, the unpaid balances of loans delinquent 90 days or more and still accruing interest were $5.8 million and $3.4 million, respectively. At September 30, 2011, this was comprised of seven loans. Six of the loans totaling $5.3 million are past their maturity dates but are current for payment and are well secured. One loan is delinquent 60 days as for payment, is past maturity, but is well secured and in the process of collection. The Company has agreed to forbear from pursuing its remedies while the borrowers arrange refinancing from other financial institutions.

The unpaid principal balances of loans on nonaccrual status and considered impaired were $21.8 million at September 30, 2011 and $89.1 million at December 31, 2010. On March 24, 2011, the Company completed the sale of certain non-performing assets that included 21 non-accruing loans with an aggregate net book value of $52.4 million (net of related specific reserves) and 4 other real estate owned (OREO) properties with an aggregate carrying value of $14.4 million. The sale of $66.8 million of non-performing assets was consummated for a cash purchase price of $60,602,036 which represented 90.7% of the Bank s net book value for these assets.

If non-accrual loans had been performing in accordance with their contractual terms, the Company would have recorded approximately $0.4 million of additional income during the quarter ended September 30, 2011 and $1.9 million during the quarter ended September 30, 2010. If non-accrual loans had been performing in accordance with their contractual terms, the Company would have recorded approximately $1.9 million of additional income for the nine months ended September 30, 2011 and $5.3 million during the nine months ended September 30, 2010.

For the three months ended September 30, 2011 and 2010, the interest collected and recognized as income on impaired loans was approximately $4,000 and $362,000, respectively. For the nine months ended September 30, 2011 and 2010, the interest income collected and recognized on impaired loans was approximately $465,000 and $1,641,000 respectively. The average recorded investment in impaired loans for the three and nine months ended September 30, 2011 was $40.4 million and $54.0 million respectively.

At September 30, 2011, there were 13 loans totaling $27.7 million that were considered troubled debt restructurings, all of which are included in impaired loans, as compared to December 31, 2010 when there were 19 loans totaling $38.0 million, all of which were included in impaired loans. At September 30, 2011, 6 of the 13 loans aggregating $16.1 million were accruing loans and 7 loans aggregating $11.6 million were non-accruing loans.

The Company s lending activities are conducted principally in Fairfield and New Haven Counties in Connecticut and Westchester County, New York City and Long Island, New York. The Company originates commercial real estate loans, commercial business loans and a variety of consumer loans. In addition, the Company had originated loans for the construction of residential homes, residential developments and for land development projects. A moratorium on all new construction loans was instituted by management in July 2008. All residential and commercial mortgage loans are collateralized primarily by first or second mortgages on real estate. The ability and willingness of borrowers to satisfy their loan obligations is dependent in large part upon the status of the regional economy and regional real estate market. Accordingly, the ultimate collectability of a substantial portion of the loan portfolio and the recovery of a substantial portion of any resulting real estate acquired is susceptible to changes in market conditions.

The Company has established credit policies applicable to each type of lending activity in which it engages, evaluates the creditworthiness of each customer and, in most cases, extends credit of up to 75% of the market value of the collateral at the date of the credit extension depending on the Company s evaluation of the borrowers creditworthiness and type of collateral. In the case of construction loans, the maximum loan-to-value was 65% of the as completed market value. The market value of collateral is monitored on an ongoing basis and additional collateral is obtained when warranted. Real estate is the primary form of collateral. Other important forms of collateral are accounts receivable, inventory, other business assets, marketable securities and time deposits. While collateral provides assurance as a secondary source of repayment, the Company ordinarily requires the primary source of repayment to be based on the borrower s ability to generate continuing cash flows on all loans not related to construction.

Table of Contents

Risk characteristics of the Company s portfolio classes include the following:

Commercial Real Estate Loans In underwriting commercial real estate loans, the Company evaluates both the prospective borrower s ability to make timely payments on the loan and the value of the property securing the loans. Repayment of such loans may be negatively impacted should the borrower default or should there be a substantial decline in the value of the property securing the loan or a decline in the general economic conditions. Where the owner occupies the property, the Company also evaluates the business s ability to repay the loan on a timely basis. In addition, the Company may require personal guarantees, lease assignments and/or the guarantee of the operating company when the property is owner occupied. These types of loans may involve greater risks than other types of lending, because payments on such loans are often dependent upon the successful operation of the business involved, therefore, repayment of such loans may be negatively impacted by adverse changes in economic conditions affecting the borrowers business.

Construction Loans Construction loans are short-term loans (generally up to 18 months) secured by land for both residential and commercial development. The loans are generally made for acquisition and improvements. Funds are disbursed as phases of construction are completed.

In the past, the Company funded construction of single family homes, when no contract of sale exists, based upon the experience of the builder, the financial strength of the owner, the type and location of the property and other factors. Construction loans are generally personally guaranteed by the principal(s). Repayment of such loans may be negatively impacted by the builders inability to complete construction, by a downturn in the new construction market, by a significant increase in interest rates or by a decline in general economic conditions. The Company has had a moratorium in place since mid-2008 on new speculative construction loans.

Residential Real Estate Loans Various loans secured by residential real estate properties are offered by the Company, including 1-4 family residential mortgages, multi-family residential loans and a variety of home equity line of credit products. Repayment of such loans may be negatively impacted should the borrower default, should there be a significant decline in the value of the property securing the loan or should there be a decline in general economic conditions.

Commercial and Industrial Loans The Company s commercial and industrial loan portfolio consists primarily of commercial business loans and lines of credit to businesses and professionals. These loans are usually made to finance the purchase of inventory, new or used equipment or other short or long-term working capital purposes. These loans are generally secured by corporate assets, often with real estate as secondary collateral, but are also offered on an unsecured basis. In granting this type of loan, the Company primarily looks to the borrower s cash flow as the source of repayment with collateral and personal guarantees, where obtained, as a secondary source. Commercial loans are often larger and may involve greater risks than other type of loans offered by the Company. Payments on such loans are often dependent upon the successful operation of the underlying business involved and, therefore, repayment of such loans may be negatively impacted by adverse changes in economic conditions, management s inability to effectively manage the business, claims of others against the borrower s assets which may take priority over the Company s claims against assets, death or disability of the borrower or loss of market for the borrower s products or services.

Other Loans The Company also offers installment loans and reserve lines of credit to individuals. Repayments of such loans are often dependent on the personal income of the borrower which may be negatively impacted by adverse changes in economic conditions. The Company does not place an emphasis on originating these types of loans.

The Company does not have any lending programs commonly referred to as subprime lending. Subprime lending generally targets borrowers with weakened credit histories typically characterized by payment delinquencies, previous charge-offs, judgments, bankruptcies, or borrowers with questionable repayment capacity as evidenced by low credit scores or high debt-burdened ratios.

Table of Contents

The following table sets forth activity in our allowance for loan losses, by loan type, for the period ended September 30, 2011. The following table also details the amount of loans receivable, net, that are evaluated individually, and collectively, for impairment, and the related portion of allowance for loan losses that is allocated to each loan portfolio segment.

s ended September 30, 2011	Commercial	Commercial Real Estate	Construction	Construction to Permanent	Residential	Consumer	Unallocated	
loan losses:								
ance	$ 885,310	$ 6,437,699	$ 1,340,939	$ 885,052	$ 1,245,489	$ 604,058	$ 1,180	$
			(217,788)					
		14,987	499			600		
loans held-for-sale			(40,347)					
	206,481	(118,612)	(365,592)	(1,741)	(45,348)	48,312	276,500	
ce	$ 1,091,791	$ 6,334,074	$ 717,711	$ 883,311	$ 1,200,141	$ 652,970	$ 277,680	$
e: individually evaluated for	$ 383,678	$ 1,349,634	$ 31,520	$ 791,962	$ 182,071	$ 151,500	$	$
e: collectively evaluated for	$ 708,113	$ 4,984,440	$ 686,191	$ 91,349	$ 1,018,070	$ 501,470	$ 277,680	$
ce for Loan Losses	$ 1,091,791	$ 6,334,074	$ 717,711	$ 883,311	$ 1,200,141	$ 652,970	$ 277,680	$
nding balance	$ 28,553,155	$ 210,128,617	$ 12,857,291	$ 10,864,395	$ 151,147,445	$ 50,388,818	$	$
e: individually evaluated for	$ 699,379	$ 11,708,562	$ 1,545,001	$ 8,555,062	$ 13,926,561	$ 1,417,742	$	$
e: collectively evaluated for	$ 27,853,776	$ 198,420,055	$ 11,312,290	$ 2,309,333	$ 137,220,884	$ 48,971,076	$	$

ended September 30, 2011	Commercial	Commercial Real Estate	Construction	Construction to Permanent	Residential	Consumer	Unallocated	
r loan losses:								
lance	$ 441,319	$ 7,632,355	$ 3,478,058	$ 491,446	$ 2,363,838	$ 578,612	$ 388,473	$
		(2,736,140)	(3,049,828)		(1,458,199)	(161,759)		
	240	18,776	461,781			298,939		
loans held-for-sale		(963,461)	(1,409,701)		(3,681,498)			
	650,232	2,382,544	1,237,401	391,865	3,976,000	(62,822)	(110,793)	
ce	$ 1,091,791	$ 6,334,074	$ 717,711	$ 883,311	$ 1,200,141	$ 652,970	$ 277,680	$
ce: individually evaluated for	$ 383,678	$ 1,349,634	$ 31,520	$ 791,962	$ 182,071	$ 151,500	$	$
ce: collectively evaluated for	$ 708,113	$ 4,984,440	$ 686,191	$ 91,349	$ 1,018,070	$ 501,470	$ 277,680	$
nce for Loan Losses	$ 1,091,791	$ 6,334,074	$ 717,711	$ 883,311	$ 1,200,141	$ 652,970	$ 277,680	$
nding balance	$ 28,553,155	$ 210,128,617	$ 12,857,291	$ 10,864,395	$ 151,147,445	$ 50,388,818	$	$
ce: individually evaluated for	$ 699,379	$ 11,708,562	$ 1,545,001	$ 8,555,062	$ 13,926,561	$ 1,417,742	$	$
ce : collectively evaluated for	$ 27,853,776	$ 198,420,055	$ 11,312,290	$ 2,309,333	$ 137,220,884	$ 48,971,076	$	$

The Company monitors the credit quality of its loans receivable in an ongoing manner. Credit quality is monitored by reviewing certain credit quality indicators. Management has determined that loan-to-value ratios (LTVs), (at period end) and internally assigned risk ratings are the key credit quality indicators that best help management monitor the credit quality of the Company s loans receivable. Loan-to-value ratios used by management in monitoring credit quality are based on current period loan balances and original values at time of origination (unless a current appraisal has been obtained as a result of the loan being deemed impaired or the loan is a maturing construction loan).

Appraisals on properties securing impaired loans and Other Real Estate Owned are updated annually. Additionally, appraisals on construction loans are updated four months in advance of scheduled maturity dates. We update our impairment analysis monthly based on the most recent appraisal as well as other factors (such as senior lien positions, e.g. property taxes), and we are using published information regarding actual median home sales prices in the towns/counties where our collateral is located in CT and NY.

The majority of the Company s impaired loans have been resolved through courses of action other than via bank liquidations of real estate collateral through OREO. These include normal loan payoffs, the traditional workout process, triggering personal guarantee obligations, and troubled debt restructurings. However, as loan workout efforts progress to a point where the bank s liquidation of real estate collateral is the likely outcome, the impairment analysis is updated to reflect actual recent experience with bank sales of OREO properties.

A disposition discount is built into our impairment analysis and reflected in our allowance once a property is determined to be a likely OREO (e.g. foreclosure is probable). To determine the discount we compare the actual sales prices of our OREO properties to the appraised value that was obtained as of the date when we took title to the property. The difference is the bank-owned disposition discount.

The Company has a risk rating system as part of the risk assessment of its loan portfolio. The Company s lending officers are required to assign a risk rating to each loan in their portfolio at origination. When the lender learns of important financial developments, the risk rating is reviewed accordingly, and adjusted if necessary. Similarly, the Loan Committee can adjust a risk rating. The Loan Workout Committee meets on a regular basis and reviews loans rated special mention or worse. In addition, the Company engages a third party independent loan reviewer that performs semi-annual reviews of a sample of loans, validating the Bank s risk ratings assigned to such loans. The risk ratings play an important role in the establishment of the loan loss provision and to confirm the adequacy of the allowance for loan losses.

When assigning a risk rating to a loan, management utilizes the Bank s internal nine-point risk rating system. Loans deemed to be acceptable quality are rated 1 through 5, with a rating of 1 established for loans with minimal risk and borrowers exhibiting the strongest financial condition. Loans rated 1 5 are considered Pass . Loans that are deemed to be of questionable quality are rated 6 (special mention). An asset is considered special mention when it has a potential weakness based on objective evidence, but does not currently expose the Company to sufficient risk to warrant classification in one of the following categories. Loans with adverse classifications (substandard, doubtful or loss) are rated 7, 8 or 9, respectively. An asset is considered substandard if it is not adequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Substandard assets have well defined weaknesses based on objective evidence, and are characterized by the distinct possibility that the Company will sustain some loss if the deficiencies are not corrected. Assets classified as doubtful have all of the weaknesses inherent in those classified substandard with the added characteristic that the weaknesses present make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable.

Charge-off generally commences in the month that the loan is classified doubtful and is fully charged off within six months of such classification. If the account is classified loss the full balance is charged off immediately. The full balance is charged off regardless of the potential recovery from the sale of the collateral. This amount is recognized as a recovery once the collateral is sold.

In accordance with FFIEC (Federal Financial Institutions Examination Council) published policies establishing uniform criteria for the classification of retail credit based on delinquency status, Open-end credits are charged-off when 180 days delinquent and Closed-end credits are charged-off when 120 days delinquent. Typically, consumer installment loans are charged off no later than 90 days past due.

15

Table of Contents

The following table details the credit risk exposure of loans receivable, by loan type and credit quality indicator at September 30, 2011:

CREDIT RISK PROFILE BY CREDITWORTHINESS CATEGORY

	Commercial Real Estate		Construction		Construction to Permanent		Residential Real Estate		Co	
	< 75%	>= 75%	< 75%	>= 75%	< 75%	>= 75%	< 75%	>= 75%	< 75%	>
54	$ 138,358,750	$ 6,203,715	$	$	$ 600,000	$	$ 95,563,057	$ 32,641,241	$ 44,474,523	$
75	25,926,653	4,601,276	9,594,291		1,709,333		5,318,049	2,400,000	274,390	3
38	13,821,012	21,217,211	154,396	3,108,604		8,555,062	4,111,951	11,113,147	11,294	1
17	$ 178,106,415	$ 32,022,202	$ 9,748,687	$ 3,108,604	$ 2,309,333	$ 8,555,062	$ 104,993,057	$ 46,154,388	$ 44,760,207	$ 4

CREDIT RISK PROFILE

	Commercial	Commercial Real Estate	Construction	Construction to Permanent	Residential Real Estate	Consumer	Totals
Performing	$ 27,853,776	$ 198,660,360	$ 11,312,289	$ 7,214,333	$ 147,727,635	$ 49,395,078	$ 442,163,471
Non Performing	699,379	11,468,257	1,545,002	3,650,062	3,419,810	993,740	21,776,250
Total	$ 28,553,155	$ 210,128,617	$ 12,857,291	$ 10,864,395	$ 151,147,445	$ 50,388,818	$ 463,939,721

Table of Contents

The following table details the credit risk exposure of loans receivable, by loan type and credit quality indicator at December 31, 2010:

CREDIT RISK PROFILE BY CREDITWORTHINESS CATEGORY

Commercial Real Estate		Construction		Construction to Permanent		Residential Real Estate		Co	
< 75%	>= 75%	< 75%	>= 75%	< 75%	>= 75%	< 75%	>= 75%	< 75%	>
$ 124,645,152	$ 9,449,059	$ 1,272,028	$ 350,000	$	$	$ 91,534,348	$ 51,996,851	$ 35,192,214	$
35,253,018	4,645,738	15,059,704	4,485,209	1,709,333		2,088,700	2,907,285	3,146,244	2
13,792,482	41,057,040	10,712,146	32,009,996		8,621,710	18,052,003	20,479,131	99,235	
$ 173,690,652	$ 55,151,837	$ 27,043,878	$ 36,845,205	$ 1,709,333	$ 8,621,710	$ 111,675,051	$ 75,383,267	$ 38,437,693	$ 4

CREDIT RISK PROFILE

	Commercial	Commercial Real Estate	Construction	Construction to Permanent	Residential Real Estate	Consumer	Totals
Performing	$ 13,358,840	$ 202,054,317	$ 33,003,060	$ 8,951,208	$ 159,270,574	$ 43,724,749	$ 460,362,748
Non Performing	1,214,950	26,788,172	30,886,023	1,379,835	27,787,744	1,092,976	89,149,700
Total	$ 14,573,790	$ 228,842,489	$ 63,889,083	$ 10,331,043	$ 187,058,318	$ 44,817,725	$ 549,512,448

Included in loans receivable are loans for which the accrual of interest income has been discontinued due to deterioration in the financial condition of the borrowers. The recorded balance of these nonaccrual loans was $21.8 million and $89.1 million at September 30, 2011, and December 31, 2010 respectively. Generally, loans are placed on non-accruing status when they become 90 days or more delinquent, or earlier if deemed appropriate, and remain on non-accrual status until they are brought current, have six months of performance under the loan terms, and factors indicating reasonable doubt about the timely collection of payments no longer exist. Therefore, loans may be current in accordance with their loan terms, or may be less than 90 days delinquent and still be on a non-accruing status. Additionally, certain loans that cannot demonstrate sufficient global cash flow to continue loan payments in the future and certain trouble debt restructures (TDRs) are placed on non-accrual status.

The following table sets forth the detail, and delinquency status, of non-accrual loans and past due loans at September 30, 2011:

Non-Accrual and Past Due Loans

2011	31-60 Days Past Due	61-90 Days Past Due	Greater Than 90 Days	Total Past Due	Current	>90 Days Past Due and Accruing	Total Non-Accrual and Past Due Loans
Commercial							
Pass	$	$	$	$	$	$	$
Special Mention							
Substandard		172,088	410,170	582,258	117,121	448,000	1,147,379
Total Commercial	$	$ 172,088	$ 410,170	$ 582,258	$ 117,121	$ 448,000	$ 1,147,379
Commercial Real Estate							
Pass	$	$	$	$	$	$ 574,893	$ 574,893
Substandard	$	$	$ 7,745,806	$ 7,745,806	$ 3,722,450	$ 3,099,805	$ 14,568,061
Total Commercial Real Estate	$	$	$ 7,745,806	$ 7,745,806	$ 3,722,450	$ 3,674,698	$ 15,142,954
Construction Substandard	$	$	$ 289,397	$ 289,397	$ 1,255,604	$ 1,717,999	$ 3,263,000
Total Construction	$	$	$ 289,397	$ 289,397	$ 1,255,604	$ 1,717,999	$ 3,263,000
Construction to Permanent Substandard	$	$	$ 1,127,875	$ 1,127,875	$ 2,522,187	$	$ 3,650,062
Total Construction to Permanent	$	$	$ 1,127,875	$ 1,127,875	$ 2,522,187	$	$ 3,650,062
Residential Real Estate Substandard	$	$	$ 3,419,810	$ 3,419,810	$	$	$ 3,419,810
Total Residential Real Estate	$	$	$ 3,419,810	$ 3,419,810	$	$	$ 3,419,810

Consumer Substandard	$	$	$ 993,742	$ 993,742	$	$	$ 993,742
Total Consumer	$	$	$ 993,742	$ 993,742	$	$	$ 993,742
Total	$	$ 172,088	$ 13,986,800	$ 14,158,888	$ 7,617,362	$ 5,840,697	$ 27,616,947

Table of Contents

The following table sets forth the detail, and delinquency status, of non-accrual loans and past due loans at December 31, 2010:

	Non-Accrual and Past Due Loans						
2010	31-60 Days Past Due	61-90 Days Past Due	Greater Than 90 Days	Total Past Due	Current	>90 Days Past Due and Accruing	Total Non-Accrual and Past Due Loans
Commercial							
Special Mention	$	$	$	$	$	$ 63,289	$ 63,289
Substandard	350,000	100,000	698,767	1,148,767	66,183	175,000	1,389,950
Total Commercial	$ 350,000	$ 100,000	$ 698,767	$ 1,148,767	$ 66,183	$ 238,289	$ 1,453,239
Commercial Real Estate Substandard	$ 269,672	$ 6,449,096	$ 13,521,123	$ 20,239,891	$ 6,548,281	$	$ 26,788,172
Total Commercial Real Estate	$ 269,672	$ 6,449,096	$ 13,521,123	$ 20,239,891	$ 6,548,281	$	$ 26,788,172
Construction Substandard	$ 1,517,943	$ 4,059,516	$ 13,736,985	$ 19,314,444	$ 11,571,579	$ 3,135,953	$ 34,021,976
Total Construction	$ 1,517,943	$ 4,059,516	$ 13,736,985	$ 19,314,444	$ 11,571,579	$ 3,135,953	$ 34,021,976
Construction to Permanent Substandard	$	$	$	$	$ 1,379,835	$	$ 1,379,835
Total Construction to Permanent	$	$	$	$	$ 1,379,835	$	$ 1,379,835
Residential Real Estate Substandard	$	$	$ 15,897,248	$ 15,897,248	$ 11,890,496	$	$ 27,787,744
Total Residential Real Estate	$	$	$ 15,897,248	$ 15,897,248	$ 11,890,496	$	$ 27,787,744
Consumer Substandard	$	$	$ 1,092,976	$ 1,092,976	$	$	$ 1,092,976

Total Consumer	$	$	$ 1,092,976	$ 1,092,976	$	$	$ 1,092,976
Total	$ 2,137,615	$ 10,608,612	$ 44,947,099	$ 57,693,326	$ 31,456,374	$ 3,374,242	$ 92,523,942

These non-accrual and past due amounts included loans deemed to be impaired of $21.8 million and $89.1 million at September 30, 2011, and December 31, 2010, respectively. Loans past due ninety days or more and still accruing interest were approximately $5.8 million and $3.4 million at September 30, 2011, and December 31, 2010 respectively, and consisted of 7 loans at September 30, 2011. Six of the loans are past their maturity, but are well secured and in the process of collection. One loan is 60 days delinquent as for payment, is past maturity, but is well secured and in the process of collection.

Table of Contents

The following table sets forth the detail and delinquency status of loans receivable, by performing and non-performing loans at September 30, 2011.

	Performing (Accruing) Loans						
2011	31-60 Days Past Due	Greater Than 60 Days	Total Past Due	Current	Total Performing Loans	Total Non-Accrual and Past Due Loans	Total Loans
Commercial							
Pass	$ 18,862	$	$ 18,862	$ 22,757,629	$ 22,776,491	$	$ 22,776,491
Special Mention				754,955	754,955		754,955
Substandard	242,868		242,868	3,631,462	3,874,330	1,147,379	5,021,709
Total Commercial	$ 261,730	$	$ 261,730	$ 27,144,046	$ 27,405,776	$ 1,147,379	$ 28,553,155
Commercial Real Estate							
Pass	$ 1,918,308	$	$ 1,918,308	$ 142,069,265	$ 143,987,573	$ 574,893	$ 144,562,466
Special Mention	400,516		400,516	30,127,412	30,527,928		30,527,928
Substandard	617,139		617,139	19,853,023	20,470,162	14,568,061	35,038,223
Total Commercial Real Estate	$ 2,935,963	$	$ 2,935,963	$ 192,049,700	$ 194,985,663	$ 15,142,954	$ 210,128,617
Construction							
Pass	$	$	$	$	$	$	$
Special Mention				9,594,291	9,594,291		9,594,291
Substandard						3,263,000	3,263,000
Total Construction	$	$	$	$ 9,594,291	$ 9,594,291	$ 3,263,000	$ 12,857,291