

TF FINANCIAL CORP  
Form 10-Q  
May 13, 2011

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SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934

For the period ended March 31, 2011

- 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: 0-24168

TF FINANCIAL CORPORATION  
(Exact Name of Registrant as Specified in Its Charter)

Pennsylvania  
(State or Other Jurisdiction of Incorporation  
or Organization)

74-2705050  
(I.R.S. Employer Identification No.)

3 Penns Trail, Newtown, Pennsylvania  
(Address of Principal Executive Offices)

18940  
(Zip Code)

Registrant's telephone number, including area code: (215) 579-4000

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

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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 the definitions of "large accelerated filer," "accelerated filer," and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 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: May 12, 2011

Class	Outstanding
\$.10 par value common stock	2,822,449 shares

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Exhibits

<u>31.1</u>	<u>Certification of CEO pursuant to Section 302 of the Sarbanes-Oxley Act of 2002</u>
<u>31.2</u>	<u>Certification of CFO pursuant of Section 302 of the Sarbanes-Oxley Act of 2002</u>
<u>32.</u>	<u>Certification pursuant of Section 906 of the Sarbanes-Oxley Act of 2002</u>

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## TF Financial Corporation and Subsidiaries

## ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS

CONSOLIDATED BALANCE SHEETS  
(Unaudited)

	March 31, 2011	December 31, 2010
	(in thousands)	
<b>ASSETS</b>		
Cash and cash equivalents	\$ 10,668	\$ 7,437
Investment securities	119,909	127,490
Loans receivable, net	498,664	501,528
Loans receivable held for sale	215	130
Federal Home Loan Bank stock—at cost	8,931	9,401
Accrued interest receivable	2,584	2,738
Premises and equipment, net	6,669	6,797
Goodwill	4,324	4,324
Bank-owned life insurance	18,026	17,868
Other assets	14,231	14,044
<b>TOTAL ASSETS</b>	<b>\$ 684,221</b>	<b>\$ 691,757</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>Liabilities</b>		
Deposits	\$ 547,753	\$ 550,135
Borrowings from the Federal Home Loan Bank	55,387	61,987
Advances from borrowers for taxes and insurance	1,824	2,166
Accrued interest payable	2,214	1,784
Other liabilities	2,773	2,269
<b>Total liabilities</b>	<b>609,951</b>	<b>618,341</b>
<b>Stockholders' equity</b>		
Preferred stock, no par value; 2,000,000 shares authorized at March 31, 2011 and December 31, 2010, none issued	—	—
Common stock, \$0.10 par value; 10,000,000 shares authorized, 5,290,000 shares issued and, 2,822,449 shares outstanding at March 31, 2011 and December 31, 2010, respectively, net of shares in treasury of 2,467,551, respectively	529	529
Additional paid-in capital	54,012	53,964
Unearned ESOP shares	(1,186)	(1,217)
Treasury stock-at cost	(51,220)	(51,220)
Retained earnings	71,237	70,749
Accumulated other comprehensive income	898	611
<b>Total stockholders' equity</b>	<b>74,270</b>	<b>73,416</b>
<b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>	<b>\$ 684,221</b>	<b>\$ 691,757</b>

The accompanying notes are an integral part of these statements



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TF Financial Corporation and Subsidiaries

CONSOLIDATED STATEMENTS OF INCOME  
(Unaudited)

	For the three months ended March 31,	
	2011	2010
<b>Interest income</b>		
Loans, including fees	\$ 6,584	\$ 7,302
<b>Investment securities</b>		
Fully taxable	896	1,075
Exempt from federal taxes	355	297
Interest-bearing deposits and other	—	1
<b>TOTAL INTEREST INCOME</b>	<b>7,835</b>	<b>8,675</b>
<b>Interest expense</b>		
Deposits	1,460	1,995
Borrowings	559	848
<b>TOTAL INTEREST EXPENSE</b>	<b>2,019</b>	<b>2,843</b>
<b>NET INTEREST INCOME</b>	<b>5,816</b>	<b>5,832</b>
Provision for loan losses	900	961
<b>NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES</b>	<b>4,916</b>	<b>4,871</b>
<b>Non-interest income</b>		
Service fees, charges and other operating income	465	529
Bank-owned life insurance	157	172
Gain on sale of loans	117	60
Gain (loss) on sale of foreclosed real estate	11	(145)
<b>TOTAL NON-INTEREST INCOME</b>	<b>750</b>	<b>616</b>
<b>Non-interest expense</b>		
Compensation and benefits	2,746	2,700
Occupancy and equipment	818	759
Professional fees	478	228
Marketing and advertising	67	120
FDIC insurance premiums	233	194
Other operating	634	591

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TOTAL NON-INTEREST EXPENSE	4,976	4,592
INCOME BEFORE INCOME TAXES	690	895
Income taxes	72	178
NET INCOME	\$ 618	\$ 717
Earnings per share—basic	\$ 0.23	\$ 0.27
Earnings per share—diluted	\$ 0.23	\$ 0.27
Dividends paid per share	\$ 0.05	\$ 0.19

The accompanying notes are an integral part of these statements

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## TF Financial Corporation and Subsidiaries

CONSOLIDATED STATEMENTS OF CASH FLOWS  
(Unaudited)

	For the three months ended March 31,	
	2011	2010
	(in thousands)	
<b>OPERATING ACTIVITIES</b>		
Net income	\$ 618	\$ 717
Adjustments to reconcile net income to net cash provided by operating activities		
Amortization of:		
Mortgage loan servicing rights	50	(3)
Deferred loan origination fees	67	51
Premiums and discounts on investment securities, net	101	17
Premiums and discounts on loans, net	2	43
Provision for loan losses	900	961
Depreciation of premises and equipment	219	212
Increase in value of bank-owned life insurance	(157)	(172)
Share-based compensation	79	73
Proceeds from sale of loans originated for sale	5,767	6,327
Origination of loans held for sale	(5,785)	(6,114)
(Gain) loss on sale of:		
Loans held for sale	(117)	(60)
Foreclosed real estate	(11)	145
Decrease (increase) in:		
Accrued interest receivable	154	76
Other assets	324	(225)
Increase (decrease) in:		
Accrued interest payable	430	71
Other liabilities	408	(773)
<b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>	<b>3,049</b>	<b>1,346</b>
<b>INVESTING ACTIVITIES</b>		
Loan originations	(22,525)	(16,357)
Loan principal payments	23,578	20,855
Principal repayments on investment securities	7,882	6,613
Purchase of investment securities	—	(9,942)
Redemption of FHLB stock	470	—



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Proceeds from the sale of foreclosed real estate	322	—
Purchase of premises and equipment	(91)	(482)
<b>NET CASH PROVIDED BY INVESTING ACTIVITIES</b>	<b>9,636</b>	<b>687</b>

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	For the three months ended March 31,	
	2011	2010
	(in thousands)	
<b>FINANCING ACTIVITIES</b>		
Net (decrease) increase in customer deposits	(2,382)	709
Proceeds of long-term Federal Home Loan Bank borrowings	—	8,000
Repayment of long-term Federal Home Loan Bank borrowings	(6,600)	(6,503)
Net decrease in advances from borrowers for taxes and insurance	(342)	(268)
Exercise of stock options	—	72
Common stock dividends paid	(130)	(505)
<b>NET CASH (USED IN) PROVIDED BY FINANCING ACTIVITIES</b>	<b>(9,454)</b>	<b>1,505</b>
<b>NET INCREASE IN CASH AND CASH EQUIVALENTS</b>	<b>3,231</b>	<b>3,538</b>
Cash and cash equivalents at beginning of period	7,437	12,801
Cash and cash equivalents at end of period	\$ 10,668	\$ 16,339
<b>Supplemental disclosure of cash flow information</b>		
Cash paid for:		
Interest on deposits and borrowings	\$ 1,589	\$ 2,772
Income taxes	\$ 300	\$ 30
Non-cash transactions:		
Transfers from loans to foreclosed real estate	\$ 843	\$ —

The accompanying notes are an integral part of these statements

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TF FINANCIAL CORPORATION AND SUBSIDIARIES  
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

## NOTE 1 - PRINCIPLES OF CONSOLIDATION

The consolidated financial statements as of March 31, 2011 (unaudited) and December 31, 2010 and for the three month period ended March 31, 2011 and 2010 (unaudited) include the accounts of TF Financial Corporation (the “Company”) and its wholly owned subsidiaries Third Federal Bank (the “Bank”), TF Investments Corporation and Penns Trail Development Corporation. The accompanying consolidated balance sheet at December 31, 2010, has been derived from the audited consolidated balance sheet but does not included all of the information and notes required by accounting principles generally accepted in the United States of America (“US GAAP”) for complete financial statements. The Company’s business is conducted principally through the Bank. All significant intercompany accounts and transactions have been eliminated in consolidation.

## NOTE 2 - BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements were prepared in accordance with the instructions for Form 10-Q and, therefore, do not include all of the disclosures or footnotes required by US GAAP. In the opinion of management, all adjustments, consisting of normal recurring accruals, necessary for fair presentation of the consolidated financial statements have been included. The results of operations for the period ended March 31, 2011 are not necessarily indicative of the results which may be expected for the entire fiscal year or any other period. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company’s Annual Report on Form 10-K for the fiscal year ended December 31, 2010.

## NOTE 3 - CONTINGENCIES

The Company, from time to time, is a party to routine litigation that arises in the normal course of business. In the opinion of management, the resolution of this litigation, if any, would not have a material adverse effect on the Company’s consolidated financial position or results of operations.

## NOTE 4 - OTHER COMPREHENSIVE INCOME

Comprehensive income is the change in equity of a business enterprise during a period from transactions and other events and circumstances from non-owner sources. Total comprehensive income was \$905,000 and \$908,000 for the three months ended March 31, 2011 and 2010, respectively. The components of other comprehensive income are as follows for the three months ended:

	Before tax amount	March 31, 2011 Tax (expense) (in thousands)	Net of tax amount
Unrealized gains on securities			
Unrealized holding gains arising during period	\$ 404	\$ (137)	\$ 267
Pension plan benefit adjustment related to actuarial losses	29	(9)	20
Other comprehensive income, net	\$ 433	\$ (146)	\$ 287
	Before tax	March 31, 2010 Tax	Net of tax

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	amount	(expense) (in thousands)	amount
Unrealized gains on securities			
Unrealized holding gains arising during period	\$ 257	\$ (88)	\$ 169
Pension plan benefit adjustment related to actuarial losses	33	(11)	22
Other comprehensive income, net	\$ 290	\$ (99)	\$ 191

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## NOTE 5—EARNINGS PER SHARE

The following tables illustrate the reconciliation of the numerators and denominators of the basic and diluted earnings per share computations (dollars in thousands, except share and per share data):

	Three months ended March 31, 2011		
	Income (numerator)	Weighted average shares (denominator)	Per share Amount
Basic earnings per share			
Income available to common stockholders	\$ 618	2,703,380	\$ 0.23
Effect of dilutive securities			
Stock options and grants	—	209	
Diluted earnings per share			
Income available to common stockholders plus effect of dilutive securities	\$ 618	2,703,589	\$ 0.23

There were 71,010 options to purchase shares of common stock at a price range of \$24.12 to \$32.51 per share which were outstanding during the three months ended March 31, 2011 that were not included in the computation of diluted earnings per share because the options' exercise prices were greater than the average market price of the common shares.

	Three months ended March 31, 2010		
	Income (numerator)	Weighted average shares (denominator)	Per share Amount
Basic earnings per share			
Income available to common stockholders	\$ 717	2,669,276	\$ 0.27
Effect of dilutive securities			
Stock options and grants	—	—	
Diluted earnings per share			
Income available to common stockholders plus effect of dilutive securities	\$ 717	2,669,276	\$ 0.27

There were 269,675 options to purchase shares of common stock at a price range of \$19.33 to \$32.51 per share which were outstanding during the three months ended March 31, 2010 that were not included in the computation of diluted earnings per share because the options' exercise prices were greater than the average market price of the common shares.

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## NOTE 6—INVESTMENT SECURITIES

The amortized cost, gross unrealized gains and losses, and fair value of the Company's investment securities at March 31, 2011 and December 31, 2010, are summarized as follows:

	March 31, 2011			
	Amortized cost	Gross unrealized gains (in thousands)	Gross unrealized losses	Fair value
Available for sale				
U.S. Government and federal agencies	\$ 6,000	\$ 37	\$ —	\$ 6,037
Corporate debt securities	3,340	204	—	3,544
State and political subdivisions	47,320	1,598	(66)	48,852
Residential mortgage-backed securities issued by quasi-governmental agencies	44,142	1,593	(19)	45,716
Residential mortgage-backed securities privately issued	12,451	324	(1)	12,774
Total investment securities available for sale	113,253	3,756	(86)	116,923
Held to maturity				
Residential mortgage-backed securities issued by quasi-governmental agencies	2,986	339	—	3,325
Total investment securities	\$ 116,239	\$ 4,095	\$ (86)	\$ 120,248
	December 31, 2010			
	Amortized cost	Gross unrealized gains (in thousands)	Gross unrealized losses	Fair value
Available for sale				
U.S. Government and federal agencies	\$ 6,000	\$ 59	\$ —	\$ 6,059
Corporate debt securities	3,340	223	—	3,563
State and political subdivisions	47,348	1,120	(260)	48,208
Residential mortgage-backed securities issued by quasi-governmental agencies	50,942	1,950	(6)	52,886
Residential mortgage-backed securities, privately issued	13,425	224	(44)	13,605
Total investment securities available for sale	121,055	3,576	(310)	124,321
Held to maturity				
Residential mortgage-backed securities held to maturity issued by quasi-governmental agencies	3,169	341	—	3,510
Total investment securities	\$ 124,224	\$ 3,917	\$ (310)	\$ 127,831

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The table below indicates the length of time individual securities have been in a continuous unrealized loss position at March 31, 2011:

Description of Securities	Number of Securities	Less than 12 months		12 months or longer		Total	
		Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair value	Unrealized Loss
(in thousands)							
State and political subdivisions	7	\$ 4,352	\$ (66)	\$ —	\$ —	\$ 4,352	\$ (66)
Residential mortgage-backed securities issued by quasi-governmental agencies	1	2,954	(19)	—	—	2,954	(19)
Residential mortgage-backed securities privately issued	1	177	(1)	—	—	177	(1)
Total temporarily impaired securities	9	\$ 7,483	\$ (86)	\$ —	\$ —	\$ (7,483)	\$ (86)

The table below indicates the length of time individual securities have been in a continuous unrealized loss position at December 31, 2010:

Description of Securities	Number of Securities	Less than 12 months		12 months or longer		Total	
		Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair value	Unrealized Loss
(in thousands)							
State and political subdivisions	17	\$ 14,210	\$ (260)	\$ —	\$ —	\$ 14,210	\$ (260)
Residential mortgage-backed securities issued by quasi-governmental agencies	1	3,027	(6)	—	—	3,027	(6)
Residential mortgage-backed securities privately issued	3	7,048	(44)	—	—	7,048	(44)
Total temporarily impaired securities	21	\$ 24,285	\$ (310)	\$ —	\$ —	\$ 24,285	\$ (310)

On a quarterly basis, temporarily impaired securities are evaluated to determine whether such impairment is other-than-temporary impairment (“OTTI”). The Company has performed this evaluation and has determined that the unrealized losses at March 31, 2011 and December 31, 2010, respectively, are not considered other-than-temporary

but are the results of changes in interest rates, and are therefore reflected in other comprehensive income.



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## NOTE 7—LOANS RECEIVABLE

Loans receivable are summarized as follows:

	March 31, 2011	December 31, 2010
	(in thousands)	
Held for investment:		
First mortgage loans		
Secured by one-to four-family residences	\$ 267,265	\$ 269,077
Secured by non-residential properties or non—owner occupied residential properties	140,905	137,307
Construction loans	18,462	18,799
Total first mortgage loans	426,632	425,183
Other loans		
Commercial-business, real estate secured	24,628	26,603
Commercial-business, non-real estate secured	5,114	5,575
Home equity and second mortgage	48,150	49,430
Other consumer	2,408	2,407
Total other loans	80,300	84,015
Total loans	506,932	509,198
Net deferred loan origination costs and unamortized premiums	638	658
Less allowance for loan losses	(8,906)	(8,328)
Total loans receivable	\$ 498,664	\$ 501,528
Held for sale:		
First mortgage loans		
Secured by one-to four-family residences	\$ 215	\$ 130

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The following table presents the composition of the commercial loan portfolio by credit quality indicators:

Commercial credit exposure-credit risk profile by internally assigned grade  
March 31, 2011

	Pass	Special mention	Substandard (in thousands)	Doubtful	Total
Secured by non-residential properties or non—owner occupied residential properties	\$ 111,328	\$ 19,561	\$ 10,016	\$ —	\$ 140,905
Construction loans	3,102	5,849	9,511	—	18,462
Commercial-business, real estate secured	13,827	1,001	9,800	—	24,628
Commercial-business, non-real estate secured	5,114	—	—	—	5,114
<b>Total</b>	<b>\$ 133,371</b>	<b>\$ 26,411</b>	<b>\$ 29,327</b>	<b>\$ —</b>	<b>\$ 189,109</b>

Commercial credit exposure-credit risk profile by internally assigned grade  
December 31, 2010

	Pass	Special mention	Substandard (in thousands)	Doubtful	Total
Secured by non-residential properties or non—owner occupied residential properties	\$ 108,484	\$ 19,299	\$ 9,524	\$ —	\$ 137,307
Construction loans	3,482	6,269	9,048	—	18,799
Commercial-business, real estate secured	15,778	1,007	9,818	—	26,603
Commercial-business, non-real estate secured	5,531	—	—	44	5,575
<b>Total</b>	<b>\$ 133,275</b>	<b>\$ 26,575</b>	<b>\$ 28,390</b>	<b>\$ 44</b>	<b>\$ 188,284</b>

In order to assess and monitor the credit risk associated with commercial loans, the Company employs a risk rating methodology whereby each commercial loan is initially assigned a risk grade. At least annually, all risk ratings are reviewed in light of information received such as tax returns, rent rolls, cash flow statements, appraisals, and any other information which may affect the then current risk rating, which is adjusted upward or downward as needed. At the end of each quarter the risk ratings are summarized and become a component of the evaluation of the allowance for loan losses. The Company's risk rating definitions mirror those promulgated by banking regulators and are as follows:

Pass: Good quality loan characterized by satisfactory liquidity; reasonable debt capacity and coverage; acceptable management in all critical positions and normal operating results for its peer group. The Company has grades 1 through 6 within the Pass category which reflect the increasing amount of attention paid to the individual loan because

of, among other things, trends in debt service coverage, management weaknesses, or collateral values.

Special mention: A loan that has potential weaknesses that deserves management's close attention. Although the loan is currently protected, if left uncorrected, potential weaknesses may result in deterioration of the loan's repayment prospects or in the borrower's future credit position. Potential weaknesses include: weakening financial condition; an unrealistic repayment program; inadequate sources of funds; lack of adequate collateral; credit information; or documentation. There is currently the capacity to meet interest and principal payments, but further adverse business, financial, or economic conditions may impair capacity or willingness to pay interest and repay principal.

Substandard: A loan that is inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged. Although no loss of principal or interest is presently apparent, there is the distinct possibility that a partial loss of interest and/or principal will be sustained if the deficiencies are not corrected. There is a current identifiable vulnerability to default and the dependence upon favorable business, financial, or economic conditions to meet timely payment of interest and repayment of principal.

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**Doubtful:** A loan which has all the weaknesses inherent in a substandard asset with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable. The possibility of loss is extremely high, but because of certain important and reasonable specific pending factors which may work to strengthen the asset, classification as an estimated loss if deferred until a more exact status is determined. Pending factors include: proposed merger, acquisition, liquidation, capital injection, perfecting liens on additional collateral, and refinancing plans.

**Loss:** Loans which are considered uncollectible and have been charged off. The Company has charged-off all loans classified as loss.

Loans classified as special mention, substandard or doubtful are evaluated for potential impairment. All impaired loans are placed on non-accrual status and are classified as substandard or doubtful.

The following table presents the composition of the residential mortgage and consumer loan portfolios by credit quality indicators:

Mortgage and consumer credit exposure-credit risk profile by payment activity  
March 31, 2011

	Performing	Non-performing (in thousands)	Total
Secured by one-to four-family residences	\$ 262,314	\$ 4,951	\$ 267,265
Home equity and second mortgage	47,520	630	48,150
Other	2,408	—	2,408
Total	\$ 312,242	\$ 5,581	\$ 317,823

Mortgage and consumer credit exposure-credit risk profile by payment activity  
December 31, 2010

	Performing	Non-performing (in thousands)	Total
Secured by one-to four-family residences	\$ 265,459	\$ 3,618	\$ 269,077
Home equity and second mortgage	48,018	1,412	49,430
Other	2,404	3	2,407
Total	\$ 315,881	\$ 5,033	\$ 320,914

In order to assess and monitor the credit risk associated with one-to four-family residential loans and consumer loans which include second mortgage loans and home equity secured lines of credit, the Company relies upon the payment status of the loan. Loans 90 days or more past due are placed on non-accrual status and evaluated for impairment on a pooled basis.

The following table presents non-performing loans including impaired loans and loan balances past due over 90 days for which the accrual of interest has been discontinued by class at:

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	March 31, 2011	December 31, 2010
	(in thousands)	
Secured by one-to four-family residences	\$ 4,951	\$ 3,618
Secured by non-residential properties or non—owner occupied residential properties	4,756	4,993
Construction loans	6,126	4,307
Commercial-business, real estate secured	4,601	4,601
Commercial-business, non-real estate secured	—	44
Home equity and second mortgage	630	1,412
Other consumer	—	3
Total non-performing loans	\$ 21,064	\$ 18,978
Total loans past due 90 days as to interest or principal and accruing interest	\$ —	\$ —

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The following table presents loans individually evaluated for impairment by class:

	March 31, 2011				
	Recorded investment	Unpaid principal balance	Related allowance (in thousands)	Average recorded investment	Interest income recognized
With an allowance recorded:					
Secured by non-residential properties or non—owner occupied residential properties	\$ 2,510	\$ 2,510	\$ 224	\$ 2,183	\$ —
Construction loans	5,706	5,706	2,496	4,797	—
Commercial-business, real estate secured	2,605	2,605	467	2,605	—
Commercial-business, non-real estate secured	—	—	—	21	—
With no allowance recorded:					
Secured by non-residential properties or non—owner occupied residential properties	\$ 1,941	\$ 1,941	\$ —	\$ 2,385	—
Construction loans	420	420	—	420	—
Commercial-business, real estate secured	1,996	1,996	—	1,996	—
Total	\$ 15,178	\$ 15,178	\$ 3,187	\$ 14,407	\$ —

	December 31, 2010				
	Recorded investment	Unpaid principal balance	Related allowance (in thousands)	Average recorded investment	Interest income recognized
With an allowance recorded:					
Secured by non-residential properties or non—owner occupied residential properties	\$ 1,855	\$ 1,855	\$ 218	\$ 925	\$ —
Construction loans	3,887	3,887	1,627	3,887	—
Commercial-business, real estate secured	2,605	2,605	373	1,563	—
Commercial-business, non-real estate secured	44	44	44	18	—
With no allowance recorded:					

Secured by non-residential properties or non—owner occupied residential properties	2,830	2,830	—	3,479	—
Construction loans	420	420	—	492	—
Commercial-business, real estate secured	1,996	1,996	—	4,717	—
Commercial-business, non-real estate secured	—	—	—	22	—
Total	\$ 13,637	\$ 13,637	\$ 2,262	\$ 15,103	\$ —

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The following table presents the contractual aging of delinquent loans by class at March 31, 2011:

	Current	30-59 Days past due	60-89 Days past due	Loans past due 90 days or more (in thousands)	Total past due	Total loans	Recorded investment over 90 days and accruing interest
Secured by one-to four-family residences	\$ 263,144	\$ —	\$ —	\$ 4,121	\$ 4,121	\$ 267,265	\$ —
Secured by non-residential properties or non-owner occupied residential properties	136,149	—	—	4,756	4,756	140,905	—
Construction loans	14,156	—	—	4,306	4,306	18,462	—
Commercial-business, real estate secured	20,027	—	—	4,601	4,601	24,628	—
Commercial-business, non-real estate secured	5,114	—	—	—	—	5,114	—
Home equity and second mortgage	47,492	28	—	630	658	48,150	—
Other	2,408	—	—	—	—	2,408	—
Total	\$ 488,490	\$ 28	\$ —	\$ 18,414	\$ 18,442	\$ 506,932	\$ —

The following table presents the contractual aging of delinquent loans by class at December 31, 2010:

	Current	30-59 days past due	60-89 days past due	Loans past due 90 days or more (in thousands)	Total past due	Total loans	Recorded investment over 90 days and accruing interest
Secured by one-to four-family residences	\$ 267,885	\$ 424	\$ 26	\$ 742	\$ 1,192	\$ 269,077	\$ —
Secured by non-residential properties or non-owner occupied residential properties	131,566	748	754	4,239	5,741	137,307	—
Construction loans	14,492	—	—	4,307	4,307	18,799	—
Commercial-business, real estate secured	18,877	3,125	—	4,601	7,726	26,603	—
Commercial-business, non-real estate secured	5,531	—	—	44	44	5,575	—
Total	48,285	60	9	1,076	1,145	49,430	—



Home equity and second mortgage

Other	2,381	13	10	3	26	2,407	—
Total	\$ 489,017	\$ 4,370	\$ 799	\$ 15,012	\$ 20,181	\$ 509,198	\$ —

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Activity in the allowance for loan losses for the three months ended March 31, 2011 is summarized as follows:

	Balance January 1, 2011	Provision	Charge- offs (in thousands)	Recoveries	Balance March 31, 2011
Secured by one-to four- family residences	\$ 1,839	\$ 268	\$ (57 )	\$ —	\$ 2,050
Secured by non-residential properties or non—owner occupied residential properties	2,124	(154)	—	—	1,970
Construction loans	2,479	564	—	—	3,043
Commercial-business, real estate secured	974	167	—	—	1,141
Commercial-business, non-real estate secured	77	67	(44)	3	103
Home equity and second mortgage	607	193	(221)		579
Other consumer	16	7	(7)	4	20
Unallocated	212	(212)	—	—	—
Total	\$ 8,328	\$ 900	\$ (329)	\$ 7	\$ 8,906

Despite the above allocation, the allowance for credit losses is general in nature and is available to absorb losses from any portfolio segment. Changes in the allowance for credit losses for the three months ended March 31, 2010 were as follows:

	2010 (in thousands)
Balance at January 1,	\$ 5,215
Provision charged to income	961
Charge-offs:	
Commercial-business, non-real estate secured	(7)
Home equity and second mortgage	(6)
Recoveries:	
Other consumer	2
Balance at March 31,	\$ 6,165

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The following tables present the ending balance of the allowance for loan losses and ending loan balance by portfolio by class based on impairment method as of March 31, 2011:

Allowance	Evaluated for impairment		Total
	Individually	Collectively (in thousands)	
Secured by one-to-four family residences	\$ —	\$ 2,050	\$ 2,050
Secured by non-residential properties or non—owner occupied residential properties	224	1,746	1,970
Construction loans	2,496	547	3,043
Commercial-business, real estate secured	467	674	1,141
Commercial-business, non-real estate secured	—	103	103
Home equity and second mortgage	—	579	579
Other consumer	—	20	20
Unallocated	—	—	—
<b>Total</b>	<b>\$ 3,187</b>	<b>\$ 5,719</b>	<b>\$ 8,906</b>

Loan balance	Evaluated for impairment		Total
	Individually	Collectively (in thousands)	
Secured by one-to-four family residences	\$ —	\$ 267,265	\$ 267,265
Secured by non-residential properties or non—owner occupied residential properties	4,451	136,454	140,905
Construction loans	6,127	12,335	18,462
Commercial-business, real estate secured	4,601	20,027	24,628
Commercial-business, non-real estate secured	—	5,114	5,114
Home equity and second mortgage	—	48,150	48,150
Other consumer	—	2,408	2,408
<b>Total</b>	<b>\$ 15,179</b>	<b>\$ 491,753</b>	<b>\$ 506,932</b>

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The following tables present the ending balance of the allowance for loan losses and ending loan balance by portfolio by class based on impairment method as of December 31, 2010:

Allowance	Evaluated for impairment		Total
	Individually	Collectively (in thousands)	
Secured by one-to-four family residences	\$ —	\$ 1,839	\$ 1,839
Secured by non-residential properties or non—owner occupied residential properties	218	1,906	2,124
Construction loans	1,627	852	2,479
Commercial-business, real estate secured	373	601	974
Commercial-business, non-real estate secured	44	33	77
Home equity and second mortgage	—	607	607
Other consumer	—	16	16
Unallocated	—	212	212
<b>Total</b>	<b>\$ 2,262</b>	<b>\$ 6,066</b>	<b>\$ 8,328</b>

Loan balance	Evaluated for impairment		Total
	Individually	Collectively (in thousands)	
Secured by one-to-four family residences	\$ —	\$ 269,077	\$ 269,077
Secured by non-residential properties or non—owner occupied residential properties	4,685	132,622	137,307
Construction loans	4,307	14,492	18,799
Commercial-business, real estate secured	4,601	22,002	26,603
Commercial-business, non-real estate secured	44	5,531	5,575
Home equity and second mortgage	—	49,430	49,430
Other consumer	—	2,407	2,407
<b>Total</b>	<b>\$ 13,637</b>	<b>\$ 495,561</b>	<b>\$ 509,198</b>

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## NOTE 8- FAIR VALUE MEASUREMENTS

The following table presents information about the Company's assets and liabilities measured at fair value on a recurring basis as of March 31, 2011. Fair value is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. A fair value measurement hierarchy has been established for inputs in valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements).

The fair value hierarchy levels are summarized below:

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2 inputs are inputs that are observable for the asset or liability, either directly or indirectly.
- Level 3 inputs are unobservable and contain assumptions of the party assessing the fair value of the asset or liability.

Determination of the appropriate level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement for the instrument or security. Assets and liabilities measured at fair value on a recurring basis segregated by fair value hierarchy level are summarized below:

At March 31, 2011	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance as of March 31, 2011
	(in thousands)			
<b>Assets</b>				
Investment securities available for sale				
U.S. Government and federal agencies	\$ —	\$ 6,037	\$ —	\$ 6,037
Corporate debt securities	—	3,544	—	3,544
State and political subdivisions	—	48,852	—	48,852
Residential mortgage-backed securities issued by quasi-governmental agencies	—	45,716	—	45,716
Residential real estate mortgage - backed securities privately issued	—	12,774	—	12,774
Total investment securities available for sale	\$ —	\$ 116,923	\$ —	\$ 116,923
<b>Liabilities</b>				
Forward loan sales	\$ —	\$ —	\$ 2	\$ 2

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At December 31, 2010	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance as of December 31, 2010
	(in thousands)			
Assets				
Investment securities available for sale				
U.S. Government and federal agencies	\$ —	\$ 6,059	\$ —	\$ 6,059
Corporate debt securities	—	3,563	—	3,563
State and political subdivisions	—	48,208	—	48,208
Residential mortgage-backed securities issued by quasi-governmental agencies	—	52,886	—	52,886
Residential real estate mortgage - backed securities privately issued	—	13,605	—	13,605
Total investment securities available for sale	\$ —	\$ 124,321	\$ —	\$ 124,321
Forward loan sales	\$ —	\$ —	\$ 3	\$ 3

Investment securities available for sale and mortgage-backed securities available for sale are valued primarily by a third party pricing agent. U.S. Government and federal agency and corporate debt securities are primarily priced through a multi-dimensional relational model, a Level 2 hierarchy, which incorporates dealer quotes and other market information including, defined sector breakdown, benchmark yields, base spread, yield to maturity, and corporate actions. State and political subdivision securities are also valued within the Level 2 hierarchy using inputs with a series of matrices that reflect benchmark yields, ratings updates, and spread adjustments. Mortgage-backed securities include FHLMC, GNMA, and FNMA certificates and privately issued real estate mortgage investment conduits which are valued under a Level 2 hierarchy using a matrix correlation to benchmark yields, spread analysis, and prepayment speeds.

The fair value of forward loan sales is determined at the time the underlying loan is identified as held for sale with changes in fair value correlated to the change in secondary market loan pricing. The value is adjusted to reflect the Company's historical loan "fallout" experience which incorporates such factors as changes in market rates, origination channels and loan purpose.

The following table presents additional information about assets measured at fair value on a recurring basis for which the Company has utilized Level 3 inputs to determine fair value:

	Forward loan sales (in thousands)
Beginning balance, January 1, 2011	\$ 3
Total gains (losses) — realized/unrealized:	
Included in earnings	(5)
Included in other comprehensive income	—
Purchases, issuances, and settlements	—

Ending balance, March 31, 2011	\$	(2)
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Assets and liabilities measured at fair value on a nonrecurring basis segregated by fair value hierarchy level are summarized below:

At March 31, 2011	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance as of March 31, 2011
(in thousands)				
Assets				
Impaired loans	\$ —	\$ —	\$ 11,992	\$ 11,992
Real estate acquired through foreclosure	\$ —	\$ —	\$ 8,002	\$ 8,002
Mortgage servicing rights	\$ —	\$ 878	\$ —	\$ 878

At December 31, 2010	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance as of December 31, 2010
(in thousands)				
Assets				
Impaired loans	\$ —	\$ —	\$ 11,375	\$ 11,375
Real estate acquired through foreclosure	\$ —	\$ —	\$ 7,482	\$ 7,482
Mortgage servicing rights	\$ —	\$ 878	\$ —	\$ 878

Impaired loans are evaluated and valued at the time the loan is identified as impaired, at the lower of the recorded investment in the loan or fair value. Real estate acquired through foreclosure is initially valued at the lower of the recorded investment in the loan or fair value at foreclosure less costs to sell and subsequently adjusted for further decreases in market value, if necessary. Fair value is determined by using the value of the collateral securing the loans and is therefore classified as a Level 3 hierarchy. The value of the real estate securing impaired loans and real estate acquired through foreclosure is based on appraisals prepared by qualified independent licensed appraisers contracted by the Company to perform the assessment.

The Company initially recognizes and measures servicing assets based on the fair value of the servicing right at the time the loan is sold. The Company uses the amortized cost method for subsequent measurement of its servicing assets and evaluates the recorded value for impairment quarterly. The Company retains a qualified valuation service to calculate the amortized cost and to determine the fair value of the mortgage servicing rights. The valuation service utilizes discounted cash flow analyses adjusted for prepayment speeds, market discount rates and conditions existing in the secondary servicing market. Hence, the fair value of mortgage servicing rights is deemed a Level 2 hierarchy. The amortized cost basis of the Company's mortgage servicing rights was \$949,000 and \$997,000 at March 31, 2011 and December 31, 2010, respectively. The fair value of the mortgage servicing rights was \$878,000 at March 31, 2011 and December 31, 2010, respectively and was included in other assets in the consolidated balance sheets.





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## NOTE 9- FAIR VALUE OF FINANCIAL INSTRUMENTS

For the Bank, as for most financial institutions, the majority of its assets and liabilities are considered financial instruments. However, many such instruments lack an available trading market as characterized by a willing buyer and willing seller engaging in an exchange transaction. Also, it is the Company's general practice and intent to hold its financial instruments to maturity or available for sale and to not engage in trading or significant sales activities. For fair value disclosure purposes, the Company substantially utilized the fair value measurement criteria as explained in Note 8- Fair Value Measurements. Additionally, the Company used significant estimations and present value calculations to prepare this disclosure.

Changes in the assumptions or methodologies used to estimate fair values may materially affect the estimated amounts. In addition, there may not be reasonable comparability between institutions due to the wide range of permitted assumptions and methodologies in the absence of active markets. This lack of uniformity gives rise to a high degree of subjectivity in estimating financial instrument fair values.

Fair values have been estimated using data which management considered the best available, as generally provided by estimation methodologies deemed suitable for the pertinent category of financial instrument. The estimation methodologies, resulting fair values and recorded carrying amounts are as follows:

The fair value of cash and cash equivalents equals historical book value. The fair value of investment securities is described and presented under fair value measurement guidelines as amended.

	March 31, 2011		December 31, 2010	
	Fair value	Carrying value	Fair value	Carrying value
	(in thousands)			
Cash and cash equivalents	\$	10,668		