PATRIOT NATIONAL BANCORP INC
Form 10-Q
August 13, 2012
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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 June 30, 2012

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 x 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 x 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 in Rule 12b-2 of the Exchange Act:

Large Accelerated Filer	¨	Accelerated Filer	¨
Non-Accelerated Filer	¨	Smaller Reporting Company	x

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

Yes ¨ No x

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, 38,467,073 shares outstanding as of the close of business July 31, 2012.

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PART I FINANCIAL INFORMATION

Item 1: Consolidated Financial Statements

PATRIOT NATIONAL BANCORP, INC.

CONSOLIDATED BALANCE SHEETS

	June 30, 2012 (Unaudited)	December 31, 2011
ASSETS		
Cash and due from banks:		
Noninterest bearing deposits and cash	**$ 3,720,985**	$ 4,241,552
Interest bearing deposits	**58,456,392**	50,474,257
Short-term investments	**710,157**	709,567
Total cash and cash equivalents	**62,887,534**	55,425,376
Securities:		
Available for sale securities, at fair value (Note 2)	**56,342,630**	66,469,972
Other Investments	**3,500,000**	3,500,000
Federal Reserve Bank stock, at cost	**1,719,550**	1,707,000
Federal Home Loan Bank stock, at cost	**4,343,800**	4,508,300
Total securities	**65,905,980**	76,185,272
Loans receivable (net of allowance for loan losses: 2012: $6,673,648 2011: $9,384,672) (Note 3)	**483,858,072**	501,227,297
Loans held for sale		250,000
Accrued interest and dividends receivable	**2,289,346**	2,453,179
Premises and equipment, net	**4,712,520**	4,108,318
Cash surrender value of life insurance	**21,247,568**	20,984,604
Other real estate owned	**1,517,755**	2,762,640
Deferred tax asset (Note 6)		
Other assets	**1,848,344**	2,419,592
Total assets	**$ 644,267,119**	$ 665,816,278
LIABILITIES AND SHAREHOLDERS EQUITY		
Liabilities		
Deposits (Note 4):		
Noninterest bearing deposits	**$ 71,722,494**	$ 65,613,374
Interest bearing deposits	**450,373,261**	479,296,019
Total deposits	**522,095,755**	544,909,393
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	**5,164,509**	5,109,225
Total liabilities	**592,508,264**	615,266,618

Commitments (Note 9)		
Shareholders equity		
Preferred stock, no par value; 1,000,000 shares authorized, no shares issued and outstanding		
Common stock, $.01 par value, 100,000,000 shares authorized; 2012: 38,478,778 shares issued; 38,467,073 shares outstanding. 2011: 38,374,432 shares issued; 38,362,727, shares outstanding	**384,787**	383,744
Additional paid-in capital	**105,182,518**	105,050,433
Accumulated deficit	**(53,968,019)**	(54,858,831)
Less: Treasury stock, at cost: 2012 and 2011 11,705 shares	**(160,025)**	(160,025)
Accumulated other comprehensive income	**319,594**	134,339
Total shareholders equity	**51,758,855**	50,549,660
Total liabilities and shareholders equity	**$ 644,267,119**	$ 665,816,278

See Accompanying Notes to Consolidated Financial Statements.

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PATRIOT NATIONAL BANCORP, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

	Three Months Ended June 30, 2012	Three Months Ended June 30, 2011	Six Months Ended June 30, 2012	Six Months Ended June 30, 2011
Interest and Dividend Income				
Interest and fees on loans	$ 5,811,733	$ 6,538,593	$ 12,477,525	$ 13,495,154
Interest on investment securities	426,658	486,738	903,688	760,921
Dividends on investment securities	31,879	80,728	65,160	150,629
Interest on federal funds sold		2,385		6,411
Other interest income	40,160	58,363	50,638	120,253
Total interest and dividend income	**6,310,430**	**7,166,807**	**13,497,011**	**14,533,368**
Interest Expense				
Interest on deposits	1,421,170	1,553,745	2,938,014	3,419,094
Interest on Federal Home Loan Bank borrowings	354,591	423,529	711,428	842,404
Interest on subordinated debt	74,677	71,219	151,244	141,617
Interest on other borrowings	76,927	76,927	153,853	153,009
Total interest expense	**1,927,365**	**2,125,420**	**3,954,539**	**4,556,124**
Net interest income	**4,383,065**	**5,041,387**	**9,542,472**	**9,977,244**
Provision for Loan Losses	(1,713,425)	1,482,798	(2,558,827)	8,464,427
Net interest income after provision for loan losses	**6,096,490**	**3,558,589**	**12,101,299**	**1,512,817**
Non-interest Income				
Mortgage brokerage referral fees	22,117	1,610	34,537	14,610
Loan application, inspection & processing fees	15,986	23,966	30,713	40,765
Deposit fees and service charges	227,064	248,039	455,732	528,940
Gain on sale of loans		79,729	263,646	79,729
Loss on sale of investment securities			(8,042)	
Earnings on cash surrender value of life insurance	120,294	152,985	262,963	321,245
Other income	69,639	203,984	165,548	307,874
Total non-interest income	**455,100**	**710,313**	**1,205,097**	**1,293,163**
Non-interest Expense				
Salaries and benefits	2,725,721	3,189,311	5,616,445	6,403,826
Occupancy and equipment expense	1,135,113	1,291,826	2,258,697	2,646,393
Data processing	345,704	336,005	691,725	663,809
Advertising and promotional expense	8,234	271,781	25,963	429,755
Professional and other outside services	854,268	1,234,958	1,469,350	2,116,665
Loan administration and processing expense	45,624	48,159	53,904	85,218
Regulatory assessments	462,153	628,476	872,154	1,239,744
Insurance expense	108,775	228,637	278,020	459,411

Other real estate operations	16,351	774,450	(133,896)	1,044,957
Material and communications	132,734	164,115	263,912	364,253
Restructuring charges and asset disposals (Note 12)	126,730	2,986,441	495,207	2,986,441
Other operating expense	244,901	290,111	524,103	523,474
Total non-interest expense	**6,206,308**	**11,444,270**	**12,415,584**	**18,963,946**
Income (loss) before income taxes	**345,282**	**(7,175,368)**	**890,812**	**(16,157,966)**
Provision for Income Taxes				
Net income (loss)	**$ 345,282**	**$ (7,175,368)**	**$ 890,812**	**$ (16,157,966)**
Basic and diluted income (loss) per share (Note 7)	**$ 0.01**	**$ (0.19)**	**$ 0.02**	**$ (0.42)**

See Accompanying Notes to Consolidated Financial Statements.

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PATRIOT NATIONAL BANCORP, INC.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Net income (loss)	$ 345,282	$ (7,175,368)	$ 890,812	$ (16,157,966)
Other comprehensive income:				
Unrealized holding gains on securities, net of taxes:				
Unrealized holding gains arising during the period	122,856	247,521	190,241	250,746
Less reclassification adjustment for losses included in net income			(4,986)	
Total	122,856	247,521	185,255	250,746
Comprehensive income (loss)	**$ 468,138**	**$ (6,927,847)**	**$ 1,076,067**	**$ (15,907,220)**

See Accompanying Notes to Consolidated Financial Statements.

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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
Six months ended June 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				(16,157,966)			(16,157,966)
Unrealized holding gain on available for sale securities, net of taxes						250,746	250,746
Total comprehensive loss							(15,907,220)
Balance, June 30, 2011	38,362,727	$ 383,744	$ 105,050,433	$ (55,557,311)	$ (160,025)	$ 1,548,127	$ 51,264,968
Six months ended June 30, 2012							
Balance at December 31, 2011	38,362,727	$ 383,744	$ 105,050,433	$ (54,858,831)	$ (160,025)	$ 134,339	$ 50,549,660
Comprehensive income							
Net income				890,812			890,812
Unrealized holding gain on available for sale securities, net of taxes						185,255	185,255
Total comprehensive income							1,076,067
Share-based compensation expense			133,128				133,128
Issuance of restricted stock	104,346	1,043	(1,043)				
Balance, June 30, 2012	38,467,073	$ 384,787	$ 105,182,518	$ (53,968,019)	$ (160,025)	$ 319,594	$ 51,758,855

See Accompanying Notes to Consolidated Financial Statements.

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PATRIOT NATIONAL BANCORP, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

	Six Months Ended June 30, 2012	Six Months Ended June 30, 2011
Cash Flows from Operating Activities:		
Net income (loss)	$ 890,812	$ (16,157,966)
Adjustments to reconcile net income (loss) to net cash used in operating activities:		
Restructuring charges and asset disposals	(5,049)	1,996,441
Amortization and accretion of investment premiums and discounts, net	213,178	116,431
Amortization and accretion of purchase loan premiums and discounts, net	7,272	5,028
Provision for loan losses	(2,558,827)	8,464,427
Gain on sale of loans	(263,646)	(79,729)
Loss on sale of investment securities	8,042	
Amortization of core deposit intangible	6,963	7,506
Earnings on cash surrender value of life insurance	(262,964)	(321,245)
Depreciation and amortization	606,350	684,904
(Gain) loss on sale of other real estate owned	(201,355)	58,215
Impairment writedown on other real estate owned		165,764
Share-based compensation	133,128	
Changes in assets and liabilities:		
Decrease in deferred loan costs	36,089	100,958
Decrease in accrued interest and dividends receivable	163,833	182,723
Decrease in other assets	564,285	6,717,760
(Decrease) increase in accrued expenses and other liabilities	(61,423)	457,203
Net cash (used in) provided by operating activities	**(723,312)**	**2,398,420**
Cash Flows from Investing Activities:		
Principal repayments on available for sale securities	5,039,296	3,976,411
Proceeds from the sale (purchases) of available for sale securities	5,165,626	(51,995,480)
Redemptions of Federal Reserve Bank Stock		455,500
Purchases of Federal Reserve Bank Stock	(12,550)	(1,174,100)
Proceeds from repurchase of excess Federal Home Loan Bank Stock	164,500	
Proceeds from sale of loans	67,126,928	55,089,794
Net (increase) decrease in loans	(47,966,735)	16,308,380
Purchase of other real estate owned		(481,165)
Proceeds from sale of other real estate owned	1,823,435	15,715,973
Capital improvements of other real estate owned	(89,051)	
Purchase of bank premises and equipment	(252,341)	(218,522)
Net cash provided by investing activities	**30,999,108**	**37,676,791**
Cash Flows from Financing Activities:		
Net increase (decrease) in demand, savings and money market deposits	7,813,928	(9,443,954)
Net decrease in time certificates of deposits	(30,627,566)	(112,860,038)
Net cash used in financing activities	**(22,813,638)**	**(122,303,992)**

Net increase in cash and cash equivalents	**7,462,158**	**(82,228,781)**
Cash and Cash Equivalents:		
Beginning	55,425,376	146,777,658
Ending	$ 62,887,534	$ 64,548,877

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PATRIOT NATIONAL BANCORP, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS, Continued

(Unaudited)

	Six Months Ended June 30, 2012	2011
Supplemental Disclosures of Cash Flow Information		
Interest paid	$ 3,807,140	$ 4,432,799
Income taxes paid	$	$ 10,534
Supplemental disclosures of noncash operating, investing and financing activities:		
Unrealized holding gain on available for sale securities arising during the period	$ 306,842	$ 459,133
Transfer of loans to other real estate owned	$ 1,238,144	$ 2,661,330
Transfer of other real estate owned to premises and equipment	$ 950,000	$

See Accompanying Notes to Consolidated Financial Statements.

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PATRIOT NATIONAL BANCORP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

Note 1: Basis of Financial Statement Presentation

The Consolidated Balance Sheet at December 31, 2011 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, 2011.

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 six months ended June 30, 2012 are not necessarily indicative of the results of operations that may be expected for the remainder of 2012.

Note 2: Investment Securities

The amortized cost, gross unrealized gains, gross unrealized losses and approximate fair values of available-for-sale securities at June 30, 2012 and December 31, 2011 are as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
June 30, 2012:				
U. S. Government agency bonds	$ 5,000,000	$ 16,920	$	$ 5,016,920
U. S. Government agency mortgage-backed securities	38,624,381	1,020,326	(1,942)	39,642,765
Corporate bonds	12,202,773	8,553	(528,381)	11,682,945
	$ 55,827,154	$ 1,045,799	$ (530,323)	$ 56,342,630
December 31, 2011:				
U. S. Government agency bonds	$ 5,000,000	$ 37,085	$	$ 5,037,085
U. S. Government agency mortgage-backed securities	49,004,232	1,051,097	(5,900)	50,049,429
Corporate bonds	12,249,064	25,338	(890,944)	11,383,458
	$ 66,253,296	$ 1,113,520	$ (896,844)	$ 66,469,972

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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 June 30, 2012 and December 31, 2011:

	Less Than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
June 30, 2012:						
U. S. Government mortgage - backed securities	$ 67,729	$ (160)	$ 285,040	$ (1,782)	$ 352,769	$ (1,942)
Corporate bonds	5,814,060	(185,940)	2,657,559	(342,441)	8,471,619	(528,381)
Totals	$ 5,881,789	$ (186,100)	$ 2,942,599	$ (344,223)	$ 8,824,388	$ (530,323)
December 31, 2011:						
U. S. Government mortgage - backed securities	$ 4,941,662	$ (5,492)	$ 68,309	$ (408)	$ 5,009,971	$ (5,900)
Corporate bonds	8,358,120	(890,944)			8,358,120	(890,944)
Totals	$ 13,299,782	$ (896,436)	$ 68,309	$ (408)	$ 13,368,091	$ (896,844)

At June 30, 2012, eight securities had unrealized holding losses with aggregate depreciation of 5.7% from the amortized cost. At December 31, 2011, nine securities had unrealized losses with aggregate depreciation of 6.3% from the 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 market interest rate changes on corporate debt and mortgage-backed securities issued by U.S. Government agencies. Management considers the issuers of the securities to be financially sound, the corporate bonds are investment grade 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 June 30, 2012.

The amortized cost and fair value of available-for-sale debt securities at June 30, 2012 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 prepaid 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:

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	Amortized Cost	Fair Value
Maturity:		
Over 10 years	$	$
Corporate bonds < 5 years	3,202,773	3,211,326
Corporate bonds 5 to 10 years	9,000,000	8,471,619
U.S. Government bonds 5 to 10 years	5,000,000	5,016,920
Mortgage-backed securities	38,624,381	39,642,765
Total	$ 55,827,154	$ 56,342,630

Note 3: Loans Receivable and Allowance for Loan Losses

A summary of the Company s loan portfolio at June 30, 2012 and December 31, 2011 is as follows:

	June 30, 2012	December 31, 2011
Real Estate		
Commercial	$ 237,217,702	$ 215,659,837
Residential	149,905,067	188,108,855
Construction	6,217,516	12,306,922
Construction to permanent	8,287,915	10,012,022
Commercial	32,379,945	31,810,735
Consumer home equity	53,587,509	49,694,546
Consumer installment	2,125,347	2,164,972
Total Loans	489,721,001	509,757,889
Premiums on purchased loans	223,853	231,125
Net deferred costs	586,866	622,955
Allowance for loan losses	(6,673,648)	(9,384,672)
Loans receivable, net	$ 483,858,072	$ 501,227,297

On March 29, 2012, the Bank completed the sale of $66.4 million of residential loans consummated for a cash purchase price of $66.7 million, which represented 101% of the Bank s net book value for these assets.

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

	Three months ended June 30,		Six months ended June 30,	
	2012	2011	2012	2011
Balance, beginning of period	$ 8,460,943	$ 12,208,476	$ 9,384,672	$ 15,374,101
Provision for loan losses	(1,713,425)	1,482,798	(2,558,827)	8,464,427
Loans charged-off	(90,739)	(3,034,591)	(193,223)	(7,188,138)
Recoveries of loans previously charged-off	16,869	743,044	41,026	763,650
Transferred to loans held-for-sale				(6,014,313)
Balance, end of period	$ 6,673,648	$ 11,399,727	$ 6,673,648	$ 11,399,727

At June 30, 2012 and December 31, 2011, the unpaid balances of loans 90 days or more past maturity, and still accruing interest were $4,234,926 and $9,461,106, respectively. All of the borrowers of said loans at June 30, 2012 continue to make interest payments, but are past maturity where payoff is pending or are in the process of being renewed.

The unpaid principal balances of loans on nonaccrual status and considered impaired were $17.5 million at June 30, 2012 and $20.7 million at December 31, 2011.

If non-accrual loans had been performing in accordance with their contractual terms, the Company would have recorded approximately $274,000 of additional income during the quarter ended June 30, 2012 and $0.5 million during the quarter ended June 30, 2011. If non-accrual loans had been performing in accordance with their contractual terms, the Company would have recorded approximately $584,000 of additional income for the six months ended June 30, 2012 and $1.5 million for the six months ended June 30, 2011.

For the three months ended June 30, 2012 and 2011, the interest collected and recognized as income on impaired loans, which includes non-accrual loans, TDRs and loans that were previously classified as TDRs that have been upgraded, was approximately $0 and $30,000, respectively. For the six months ended June 30, 2012 and 2011, the interest income collected and recognized on impaired loans was approximately $180,000 and $461,000 respectively. The average recorded investment in impaired loans for the three and six months ended June 30, 2012 was $34.0 million and $34.1 million respectively.

At June 30, 2012, there were ten loans totaling $22.9 million that were considered troubled debt restructurings, as compared to December 31, 2011 when there were twelve loans totaling $25.5 million, all of which were included in impaired loans. At June 30, 2012, six of the ten loans aggregating $16.0 million were accruing loans and four loans aggregating $6.8 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 speculative 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 to some degree on the status of the regional economy as well as upon the 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.

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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 for commercial real estate at the date of the credit extension depending on the Company s evaluation of the borrowers creditworthiness and type of collateral and up to 80% for residential 1-4 family real estate. 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.

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 some additional risks than in investor owned commercial real estate lending, because payments on such loans are 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 businesses.

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 existed, 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 occasionally 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 types 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.

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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.

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The following table sets forth activity in our allowance for loan losses, by loan type, for the three months ended June 30, 2012. The following table also details the amount of loans receivable, net, that are evaluated individually, and collectively, for impairment, and the related portion of the allowance for loan losses that is allocated to each loan portfolio segment.

Three months ended June 30, 2012	Commercial	Commercial Real Estate	Construction	Construction to Permanent	Residential	Consumer	Unallocated	Total
Allowance for loan losses:								
Beginning Balance	$ 1,094,736	$ 4,645,248	$ 842,636	$ 236,313	$ 1,049,555	$ 413,724	$ 178,731	$ 8,460,943
Charge-offs	(44,471)				(32,150)	(14,118)		(90,739)
Recoveries	1,500	14,988				381		16,869
Provision	(316,423)	(877,846)	(592,125)	(114,863)	192,498	103,345	(108,011)	(1,713,425)
Ending Balance	$ 735,342	$ 3,782,390	$ 250,511	$ 121,450	$ 1,209,903	$ 503,332	$ 70,720	$ 6,673,648
Ending balance: individually evaluated for impairment	$ 37,330	$ 139,851	$ 31,520	$ 110,045	$ 30,291	$ 151,501	$	$ 500,538
Ending balance: collectively evaluated for impairment	$ 698,012	$ 3,642,539	$ 218,991	$ 11,405	$ 1,179,612	$ 351,831	$ 70,720	$ 6,173,110
Total Allowance for Loan Losses	$ 735,342	$ 3,782,390	$ 250,511	$ 121,450	$ 1,209,903	$ 503,332	$ 70,720	$ 6,673,648
Total Loans ending balance	$ 32,379,945	$ 237,217,702	$ 6,217,516	$ 8,287,915	$ 149,905,067	$ 55,712,856	$	$ 489,721,001
Ending balance: individually evaluated for impairment	$ 191,375	$ 9,406,325	$ 3,081,562	$ 6,192,645	$ 14,400,401	$ 1,417,742	$	$ 34,690,050
Ending balance : collectively evaluated for impairment	$ 32,188,570	$ 227,811,377	$ 3,135,954	$ 2,095,270	$ 135,504,666	$ 54,295,114	$	$ 455,030,951

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The following table sets forth activity in our allowance for loan losses, by loan type, for the six months ended June 30, 2012. The following table also details the amount of loans receivable, net, that are evaluated individually, and collectively, for impairment, and the related portion of the allowance for loan losses that is allocated to each loan portfolio segment.

Six months ended June 30, 2012	Commercial	Commercial Real Estate	Construction	Construction to Permanent	Residential	Consumer	Unallocated	Total
Allowance for loan losses:								
Beginning Balance	$ 882,062	$ 4,018,746	$ 867,159	$ 547,333	$ 2,550,588	$ 458,762	$ 60,022	$ 9,384,672
Charge-offs	(44,471)	(49,922)			(84,711)	(14,119)		(193,223)
Recoveries	2,500	36,976				1,550		41,026
Provision	(104,751)	(223,410)	(616,648)	(425,883)	(1,255,972)	57,139	10,698	(2,558,827)
Ending Balance	$ 735,340	$ 3,782,390	$ 250,511	$ 121,450	$ 1,209,905	$ 503,332	$ 70,720	$ 6,673,648
Ending balance: individually evaluated for impairment	$ 37,330	$ 139,851	$ 31,520	$ 110,045	$ 30,291	$ 151,501	$	$ 500,538
Ending balance: collectively evaluated for impairment	$ 698,010	$ 3,642,539	$ 218,991	$ 11,405	$ 1,179,614	$ 351,831	$ 70,720	$ 6,173,110
Total Allowance for Loan Losses	$ 735,340	$ 3,782,390	$ 250,511	$ 121,450	$ 1,209,905	$ 503,332	$ 70,720	$ 6,673,648
Total Loans ending balance	$ 32,379,945	$ 237,217,702	$ 6,217,516	$ 8,287,915	$ 149,905,067	$ 55,712,856	$	$ 489,721,001
Ending balance: individually evaluated for impairment	$ 191,375	$ 9,406,325	$ 3,081,562	$ 6,192,645	$ 14,400,401	$ 1,417,742	$	$ 34,690,050
Ending balance : collectively evaluated for impairment	$ 32,188,570	$ 227,811,377	$ 3,135,954	$ 2,095,270	$ 135,504,666	$ 54,295,114	$	$ 455,030,951

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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 internally assigned risk ratings and loan-to-value ratios (LTVs), at period end, 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 originations (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 (OREO) 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). We are subscribers to a national real estate valuation database service and use published information regarding 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 recent actual 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 an Obligor and a Facility risk rating to each loan in their portfolio at origination, which is ratified or modified by the Committee to which the loan is submitted for approval. When the lender learns of important financial developments, the risk rating is reviewed accordingly, and adjusted if necessary. All loans are reviewed annually. Similarly, the Loan Committee can adjust a risk rating.

In addition, the Company engages a third party independent loan reviewer that performs quarterly 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. Any upgrades to criticized loans must be approved by the Board Loan Committee.

When assigning a risk rating to a loan, management utilizes the Bank s internal eleven-point risk rating system.

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. 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.

As of this quarter, the Bank implemented enhancements to the allowance methodology, resulting in a reduction of the allowance for loan losses of $1.1 million. In making this transition, the changes serve to update and enhance the methodology to reflect the direction of the current loan portfolio. The changes are threefold:

First, the Bank adopted a two year, instead of a three year, weighted average historical loss factor as the basis for the calculation of its historical loss experience. This is used to calculate expected losses in the Accounting Standards Codification (ASC) (Topic 450-20), Loss Contingencies pools prior to the application of qualitative risk adjustment factors. This change was made to be more responsive to the changing credit environment. Net charge-offs have declined, especially in 2012 when they averaged $76,000 per quarter. This shorter average historical loss period will produce results more indicative of the current and expected behavior of the portfolio.

Second, the Bank adopted an Internal Risk Ratings Based (IRB) approach to calculating historical loss rates. This approach calibrates expected losses with actual risk assessment and equates the likelihood of loss to the level of risk in a credit facility rating. Previously, loss history was applied to categories of loans and qualitative adjustments were apportioned by risk rating within the categories.

Third, the Bank increased the detail of analysis within the segments, particularly within Commercial Real Estate lending, which is currently the Bank s largest concentration overall, by expanding the number of ASC 450-20 pools. In all, ten sub-concentrations have been added to the analysis. The greater level of detail enables the Bank to better apply qualitative risk adjustment factors to the segments affected and to monitor changes in credit risk within the portfolio.

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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.

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The following table details the credit risk exposure of loans receivable, by loan type and credit quality indicator at June 30, 2012:

CREDIT RISK PROFILE BY CREDITWORTHINESS CATEGORY

mmercial		Commercial Real Estate		Construction		Construction to Permanent		Residential Real Estate		Consumer		
	>= 75%	< 75%	>= 75%	< 75%	>= 75%	< 75%	>= 75%	< 75%	>= 75%	< 75%	>= 75%	
34	$ 1,456,449	$ 176,063,752	$ 9,310,101	$	$	$ 2,095,269	$	$ 100,682,616	$ 26,642,690	$ 49,265,371	$ 1,519,501	$
25	170,214	14,315,821	5,683,817	3,135,953				5,313,385		99,532	2,711,032	
15	923,208	18,170,351	13,673,860	1,219,528	1,862,035		6,192,646	5,197,208	12,069,168		1,417,741	
74	$ 2,549,871	$ 208,549,924	$ 28,667,778	$ 4,355,481	$ 1,862,035	$ 2,095,269	$ 6,192,646	$ 111,193,209	$ 38,711,858	$ 49,364,903	$ 5,648,274	$

CREDIT RISK PROFILE

	Commercial	Commercial Real Estate	Construction	Construction to Permanent	Residential Real Estate	Consumer	Totals
Performing	$ 32,188,570	$ 229,248,655	$ 3,135,953	$ 7,000,270	$ 145,976,052	$ 54,719,115	$ 472,268,615
Non Performing	191,375	7,969,047	3,081,563	1,287,645	3,929,015	993,741	17,452,386
Total	$ 32,379,945	$ 237,217,702	$ 6,217,516	$ 8,287,915	$ 149,905,067	$ 55,712,856	$ 489,721,001

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The following table details the credit risk exposure of loans receivable, by loan type and credit quality indicator at December 31, 2011:

CREDIT RISK PROFILE BY CREDITWORTHINESS CATEGORY

mmercial		Commercial Real Estate		Construction		Construction to Permanent		Residential Real Estate		Consumer		
	>= 75%	< 75%	>= 75%	< 75%	>= 75%	< 75%	>= 75%	< 75%	>= 75%	< 75%	>= 75%	
00	$ 1,737,893	$ 151,392,526	$ 11,680,310	$	$	$ 903,035	$	$ 129,132,494	$ 34,895,858	$ 44,969,963	$ 1,531,223	$
20	170,575	22,426,235	4,585,523	9,210,344				5,316,201	2,400,000	274,365	3,029,362	
40	55,207	15,981,747	9,593,496	1,243,579	1,852,999		9,108,987	3,587,607	12,776,695		1,417,742	
60	$ 1,963,675	$ 189,800,508	$ 25,859,329	$ 10,453,923	$ 1,852,999	$ 903,035	$ 9,108,987	$ 138,036,302	$ 50,072,553	$ 45,244,328	$ 5,978,327	$

CREDIT RISK PROFILE

	Commercial	Commercial Real Estate	Construction	Construction to Permanent	Residential Real Estate	Consumer	Totals
Performing	$ 31,521,175	$ 206,322,032	$ 10,928,343	$ 5,808,035	$ 183,629,363	$ 50,865,776	$ 489,074,724
Non Performing	289,560	9,337,805	1,378,579	4,203,987	4,479,492	993,742	20,683,165
Total	$ 31,810,735	$ 215,659,837	$ 12,306,922	$ 10,012,022	$ 188,108,855	$ 51,859,518	$ 509,757,889

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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 non-accrual loans was $17.5 million and $20.7 million at June 30, 2012, and December 31, 2011 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 troubled 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 June 30, 2012:

Non-Accrual and Past Due Loans
Non-Accrual Loans

2012	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	$	$	$	$	$	$	$
Substandard			191,375	191,375		448,000	639,375
Total Commercial	$	$	$ 191,375	$ 191,375	$	$ 448,000	$ 639,375
Commercial Real Estate							
Pass	$	$	$	$	$	$	$
Special Mention						304,388	304,388
Substandard	$	$	$ 5,808,987	$ 5,808,987	$ 2,160,060	$ 3,482,538	$ 11,451,585
Total Commercial Real Estate	$	$	$ 5,808,987	$ 5,808,987	$ 2,160,060	$ 3,786,926	$ 11,755,973
Construction							
Substandard	$	$	$ 1,862,035	$ 1,862,035	$ 1,219,528	$	$ 3,081,563
Total Construction	$	$	$ 1,862,035	$ 1,862,035	$ 1,219,528	$	$ 3,081,563
Construction to Permanent							
Substandard	$	$	$	$	$ 1,287,645	$	$ 1,287,645
Total Construction to Permanent	$	$	$	$	$ 1,287,645	$	$ 1,287,645
Residential Real Estate							
Substandard	$	$ 371,920	$ 3,557,095	$ 3,929,015	$	$	$ 3,929,015
Total Residential Real Estate	$	$ 371,920	$ 3,557,095	$ 3,929,015	$	$	$ 3,929,015
Consumer							
Substandard	$	$	$ 993,741	$ 993,741	$	$	$ 993,741
Total Consumer	$	$	$ 993,741	$ 993,741	$	$	$ 993,741
Total	$	$ 371,920	$ 12,413,233	$ 12,785,153	$ 4,667,233	$ 4,234,926	$ 21,687,312

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The following table sets forth the detail, and delinquency status, of non-accrual loans and past due loans at December 31, 2011:

Non-Accrual and Past Due Loans
Non-Accrual 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							
Special Mention	$	$	$	$	$	$ 44,296	$ 44,296
Substandard			289,560	289,560		947,847	1,237,407
Total Commercial	$	$	$ 289,560	$ 289,560	$	$ 992,143	$ 1,281,703
Commercial Real Estate							
Pass	$	$	$	$	$	$ 402,663	$ 402,663
Special Mention						2,832,452	2,832,452
Substandard	$	$ 443,259	$ 6,670,730	$ 7,113,989	$ 2,223,816	$ 3,515,848	$ 12,853,653
Total Commercial Real Estate	$	$ 443,259	$ 6,670,730	$ 7,113,989	$ 2,223,816	$ 6,750,963	$ 16,088,768
Construction							
Substandard	$	$	$ 135,000	$ 135,000	$ 1,243,579	$ 1,717,999	$ 3,096,578
Total Construction	$	$	$ 135,000	$ 135,000	$ 1,243,579	$ 1,717,999	$ 3,096,578
Construction to Permanent							
Substandard	$	$	$	$	$ 4,203,987	$	$ 4,203,987
Total Construction to Permanent	$	$	$	$	$ 4,203,987	$	$ 4,203,987
Residential Real Estate							
Substandard	$	$	$ 4,479,492	$ 4,479,492	$	$	$ 4,479,492
Total Residential Real Estate	$	$	$ 4,479,492	$ 4,479,492	$	$	$ 4,479,492
Consumer							
Substandard	$	$	$ 993,742	$ 993,742	$	$	$ 993,742
Total Consumer	$	$	$ 993,742	$ 993,742	$	$	$ 993,742
Total	$	$ 443,259	$ 12,568,524	$ 13,011,783	$ 7,671,382	$ 9,461,105	$ 30,144,270

These non-accrual and past due amounts included loans deemed to be impaired of $17.5 million and $20.7 million at June 30, 2012, and December 31, 2011, respectively. Loans past due and still accruing interest were $4.2 million and $9.5 million at June 30, 2012, and December 31, 2011 respectively, and consisted of seven loans at June 30, 2012. All of the borrowers of said loans at June 30, 2012 continue to make interest payments, but are past maturity where payoff is pending or are in the process of being renewed.

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The following table sets forth the detail and delinquency status of loans receivable, by performing and non-performing loans at June 30, 2012.

	Performing (Accruing) Loans							
2012	**31-60 Days Past Due**	**61-90 Days Past Due**	**Greater Than 90 Days**	**Total Past Due**	**Current**	**Total Performing Loans**	**Total Non-Accrual and Past Due Loans**	**Total Loans**
Commercial								
Pass	$	$ 298,000	$	$ 298,000	$ 26,008,483	$ 26,306,483	$	$ 26,306,483
Special Mention					539,239	539,239		539,239
Substandard		500,000		500,000	4,394,848	4,894,848	639,375	5,534,223
Total Commercial	$	$ 798,000	$	$ 798,000	$ 30,942,570	$ 31,740,570	$ 639,375	$ 32,379,945
Commercial Real Estate								
Pass	$ 3,990,000	$	$	$ 3,990,000	$ 181,383,853	$ 185,373,853	$	$ 185,373,853
Special Mention					19,695,250	19,695,250	304,388	19,999,638
Substandard	394,137		1,907,661	2,301,798	18,090,828	20,392,626	11,451,585	31,844,211
Total Commercial Real Estate	$ 4,384,137	$	$ 1,907,661	$ 6,291,798	$ 219,169,931	$ 225,461,729	$ 11,755,973	$ 237,217,702
Construction								
Pass	$	$	$	$	$	$	$	$
Special Mention					3,135,953	3,135,953		3,135,953
Substandard							3,081,563	3,081,563
Total Construction	$	$	$	$	$ 3,135,953	$ 3,135,953	$ 3,081,563	$ 6,217,516
Construction to Permanent								
Pass	$	$	$	$	$ 2,095,269	$ 2,095,269	$	$ 2,095,269
Special Mention								
Substandard					4,905,002	4,905,002	1,287,644	6,192,646
Total Construction to Permanent	$	$	$	$	$ 7,000,271	$ 7,000,271	$ 1,287,644	$ 8,287,915
Residential Real Estate								
Pass	$	$	$	$	$ 127,325,306	$ 127,325,306	$	$ 127,325,306
Special Mention					5,313,385	5,313,385		5,313,385
Substandard	1,638,262			1,638,262	11,699,099	13,337,361	3,929,015	17,266,376
Total Residential Real Estate	$ 1,638,262	$	$	$ 1,638,262	$ 144,337,790	$ 145,976,052	$ 3,929,015	$ 149,905,067
Consumer								
Pass	$ 7,953	$	$	$ 7,953	$ 51,476,598	$ 51,484,551	$	$ 51,484,551
Special Mention					2,810,564	2,810,564		2,810,564
Substandard					423,999	423,999	993,742	1,417,741
Total Consumer	$ 7,953	$	$	$ 7,953	$ 54,711,161	$ 54,719,114	$ 993,742	$ 55,712,856
Total	$ 6,030,352	$ 798,000	$ 1,907,661	$ 8,736,013	$ 459,297,676	$ 468,033,689	$ 21,687,312	$ 489,721,001

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The following table sets forth the detail and delinquency status of loans receivable, net, by performing and non-performing loans at December 31, 2011.

	Performing (Accruing) Loans						
2011	31-60 Days Past Due	Greater Than 60 Days	Total Past Due	Current	Total Perfoming Loans	Total Non-Accrual and Past Due Loans	Total Loans
Commercial							
Pass	$ 10,971	$	$ 10,971	$ 25,504,826	$ 25,515,797	$ 44,296	$ 25,560,093
Special Mention				1,714,995	1,714,995		1,714,995
Substandard	233,781		233,781	3,064,459	3,298,240	1,237,407	4,535,647
Total Commercial	$ 244,752	$	$ 244,752	$ 30,284,280	$ 30,529,032	$ 1,281,703	$ 31,810,735
Commercial Real Estate							
Pass	$	$	$	$ 162,670,173	$ 162,670,173	$ 402,663	$ 163,072,836
Special Mention	1,915,504		1,915,504	22,263,802	24,179,306	2,832,452	27,011,758
Substandard				12,721,590	12,721,590	12,853,653	25,575,243
Total Commercial Real Estate	$ 1,915,504	$	$ 1,915,504	$ 197,655,565	$ 199,571,069	$ 16,088,768	$ 215,659,837
Construction							
Pass	$	$	$	$	$	$	$
Special Mention				9,210,344	9,210,344		9,210,344
Substandard						3,096,578	3,096,578
Total Construction	$	$	$	$ 9,210,344	$ 9,210,344	$ 3,096,578	$ 12,306,922
Construction to Permanent							
Pass	$	$	$	$ 903,035	$ 903,035	$	$ 903,035
Special Mention							
Substandard				4,905,000	4,905,000	4,203,987	9,108,987
Total Construction to Permanent	$	$	$	$ 5,808,035	$ 5,808,035	$ 4,203,987	$ 10,012,022
Residential Real Estate							
Pass	$ 42,181	$	$ 42,181	$ 163,986,171	$ 164,028,352	$	$ 164,028,352
Special Mention	4,800,000		4,800,000	2,916,201	7,716,201		7,716,201
Substandard		84,225	84,225	11,800,585	11,884,810	4,479,492	16,364,302
Total Residential Real Estate	$ 4,842,181	$ 84,225	$ 4,926,406	$ 178,702,957	$ 183,629,363	$ 4,479,492	$ 188,108,855
Consumer							
Pass	$ 1,459	$	$ 1,459	$ 47,136,590	$ 47,138,049	$	$ 47,138,049
Special Mention				3,303,727	3,303,727		3,303,727
Substandard				424,000	424,000	993,742	1,417,742
Total Consumer	$ 1,459	$	$ 1,459	$ 50,864,317	$ 50,865,776	$ 993,742	$ 51,859,518
Total	$ 7,003,896	$ 84,225	$ 7,088,121	$ 472,525,498	$ 479,613,619	$ 30,144,270	$ 509,757,889

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The following table summarizes impaired loans as of June 30, 2012:

	Recorded Investment	Unpaid Principal Balance	Related Allowance
2012			
With no related allowance recorded:			
Commercial	$ 18,167	$ 250,893	$
Commercial Real Estate	7,927,165	8,755,486	
Construction	2,946,562	2,946,592	
Construction to Permanent	4,905,000	4,905,000	
Residential	13,730,710	13,730,710	
Consumer	993,742	993,742	
Total:	$ 30,521,346	$ 31,582,423	$
With an allowance recorded:			
Commercial	$ 173,208	$ 350,000	$ 37,330
Commercial Real Estate	1,479,160	1,595,500	139,851
Construction	135,000	286,625	31,520
Construction to Permanent	1,287,645	1,425,000	110,045
Residential	669,691	669,691	30,291
Consumer	424,000	424,000	151,501
Total:	$ 4,168,704	$ 4,750,816	$ 500,538
Commercial	$ 191,375	$ 600,893	$ 37,330
Commercial Real Estate	9,406,325	10,350,986	139,851
Construction	3,081,562	3,233,217	31,520
Construction to Permanent	6,192,645	6,330,000	110,045
Residential	14,400,401	14,400,401	30,291
Consumer	1,417,742	1,417,742	151,501
Total:	$ 34,690,050	$ 36,333,239	$ 500,538

Impaired loans consist of non-accrual loans, TDRs and loans that were previously classified as TDRs that have been upgraded.

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The following table summarizes impaired loans as of December 31, 2011:

	Recorded Investment	Unpaid Principal Balance	Related Allowance
2011			
With no related allowance recorded:			
Commercial	$ 210,091	$ 581,974	$
Commercial Real Estate	4,444,315	5,174,124	
Construction	1,243,579	1,247,627	
Construction to Permanent	6,614,333	6,614,333	
Residential	9,789,727	9,789,727	
Consumer	993,742	1,038,640	
Total:	$ 23,295,787	$ 24,446,425	$
With an allowance recorded:			
Commercial	$ 79,469	$ 130,137	$ 61,145
Commercial Real Estate	5,131,655	5,354,025	319,894
Construction	135,000	286,625	31,520
Construction to Permanent	2,494,654	2,634,000	498,254
Residential	5,196,516	5,196,516	197,478
Consumer	424,000	424,000	151,500
Total:	$ 13,461,294	$ 14,025,303	$ 1,259,791
Commercial	$ 289,560	$ 712,111	$ 61,145
Commercial Real Estate	9,575,970	10,528,149	319,894
Construction	1,378,579	1,534,252	31,520
Construction to Permanent	9,108,987	9,248,333	498,254
Residential	14,986,243	14,986,243	197,478
Consumer	1,417,742	1,462,640	151,500
Total:	$ 36,757,081	$ 38,471,728	$ 1,259,791

The recorded investment of impaired loans at June 30, 2012 and December 31, 2011 was $34.7 million and $36.8 million, with related allowances of $501,000 and $1.3 million, respectively.

Included in the tables above at June 30, 2012 and December 31, 2011 are loans with carrying balances of $30.5 million and $23.3 million that required no specific reserves in our allowance for loan losses. Loans that did not require specific reserves at June 30, 2012 and December 31, 2011 have sufficient collateral values, less costs to sell, supporting the carrying balances of the loans. In some cases, there may be no specific reserves because the Company already charged-off the specific impairment. Once a borrower is in default, the Company is under no obligation to advance additional funds on unused commitments.

On a case-by-case basis, the Company may agree to modify the contractual terms of a borrower s loan to remain competitive and assist customers who may be experiencing financial difficulty, as well as preserve the Company s position in the loan. If the borrower is experiencing financial difficulties and a concession has been made at the time of such modification, the loan is classified as a troubled debt restructured loan.

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The following table presents the total troubled debt restructured loans as of June 30, 2012:

	Accrual		Non-accrual		Total	
	# of Loans	Amount	# of Loans	Amount	# of Loans	Amount
Commercial Real Estate	1	$ 233,817	2	$ 4,315,060	3	$ 4,548,877
Residential Real Estate	3	10,471,386			3	10,471,386
Construction			1	1,219,528	1	1,219,528
Construction to permanent	1	4,905,000	1	1,287,645	2	6,192,645
Consumer home equity	1	424,000			1	424,000
Total Troubled Debt Restructurings	6	$ 16,034,203	4	$ 6,822,233	10	$ 22,856,436

The following table presents the total troubled debt restructured loans as of December 31, 2011:

	Accrual		Non-accrual		Total	
	# of Loans	Amount	# of Loans	Amount	# of Loans	Amount
Commercial Real Estate	1	$ 238,165	3	$ 5,666,882	4	$ 5,905,047
Residential Real Estate	3	10,506,751			3	10,506,751
Construction			1	1,243,579	1	1,243,579
Construction to permanent	1	4,905,000	2	2,494,654	3	7,399,654
Consumer home equity	1	424,000			1	424,000
Total Troubled Debt Restructurings	6	$ 16,073,916	6	$ 9,405,115	12	$ 25,479,031

One loan was modified in a troubled debt restructuring during the three months ended June 30, 2012. The following table summarizes loans that were modified in a troubled debt restructuring during the six months ended June 30, 2012.

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	Six months ended June 30, 2012			
	Number of Relationships	Pre-Modification Outstanding Recorded Investment	Number of Relationships	Post-Modification Outstanding Recorded Investment
Troubled Debt Restructurings				
Commercial Real Estate		$		$
Residential Real Estate	1	4,661,109	1	4,661,109
Construction to permanent				
Total Troubled Debt Restructurings	1	$ 4,661,109	1	$ 4,661,109

Substantially all of our troubled debt restructured loan modifications involve lowering the monthly payments on such loans through either a reduction in interest rate below market rate, an extension of the term of the loan, or a combination of these two methods. These modifications rarely result in the forgiveness of principal or accrued interest. In addition, we frequently obtain additional collateral or guarantor support when modifying commercial loans. If the borrower had demonstrated performance under the previous terms and our underwriting process shows the borrower has the capacity to continue to perform under the restructured terms, the loan will continue to accrue interest. Non-accruing restructured loans may be returned to accrual status when there has been a sustained period of repayment performance (generally six consecutive months of payments) and both principal and interest are deemed collectible.

During the six months ended June 30, 2012, one of the troubled debt restructured loans was upgraded and is no longer classified as a troubled debt restructuring as compared to December 31, 2011. The upgrade was a commercial construction loan for $1.2 million where the bank received additional collateral. There was another troubled debt restructuring of a residential loan for $4.7 million that was upgraded to special mention due to increased liquidity of the borrower during the first quarter of 2012, which has since been downgraded to substandard, due to financial hardship of the borrower in the second quarter. One troubled debt restructuring had a payment default on a commercial real estate loan and is currently in OREO.

All troubled debt restructurings are impaired loans, which are individually evaluated for impairment.

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Note 4: Deposits

The following table is a summary of the Company s deposits at:

	June 30, 2012	December 31, 2011
Non-interest bearing	$ 71,722,494	$ 65,613,374
Interest bearing		
NOW	24,297,309	24,396,210
Savings	66,862,473	59,396,310
Money market	47,227,188	52,889,642
Time certificates, less than $100,000	179,310,667	198,207,998
Time certificates, $100,000 or more	132,675,624	144,405,859
Total interest bearing	450,373,261	479,296,019
Total Deposits	$ 522,095,755	$ 544,909,393

Included in time certificates are certificates of deposit through the Certificate of Deposit Account Registry Service (CDARS) network of $0 and $1,361,544 at June 30, 2012 and December 31, 2011, respectively. These are considered brokered deposits. Pursuant to the Agreement discussed in Note 10, the Bank s participation in the CDARS program, as an issuer of deposits to customers of other banks in the CDARS program, may not exceed 10% of total deposits.

Note 5: Share-Based Compensation

The Company maintains the Patriot National Bancorp, Inc. 2012 Stock Plan to provide an incentive by the grant of options, restricted stock awards or phantom stock units to directors and employees of the Company. The Plan provides for the issuance of up to 3,000,000 shares of the Company s common stock subject to certain Plan limitations. 2,045,654 shares of stock remain available for issuance under the Plan as of June 30, 2012. The vesting of options and restricted stock awards may accelerate in accordance with terms of the plan. The Compensation Committee shall make terms and conditions applicable to the vesting of restricted stock awards and stock options. Restricted stock grants vest in quarterly installments over a four year period from the date of grant. The Compensation Committee accelerated the vesting of the initial grant of restricted stock, whereby the first year of the tranche vested immediately. Stock options were granted at an exercise price equal to $2.20 based on a price determined by the Compensation Committee and all have an expiration period of 10 years. The fair value of stock options granted on January 24, 2012, was estimated utilizing the Black-Scholes option pricing model using the following assumptions: an expected life of 6.28 years utilizing the simplified method, risk-free rate of return of 1.28%, volatility of 61.29% and no dividend yield. The Company is expensing the grant date fair value of all share-based compensation over the requisite vesting periods on a straight-line basis.

During the three and six months ended June 30, 2012, the Company recorded $53,497 and $133,128 of total stock-based compensation, respectively.

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The following table is a summary of the Company s non-vested stock options as of June 30, 2012, and changes therein during the period then ended:

	Number of Stock Options	Weighted Average Grant Date Fair Value	Weighted Average Exercise Price	Weighted Average Contractual Life (years)
Outstanding December 31, 2011		$	$	
Granted	850,000	0.90	2.20	10
Exercised				
Outstanding June 30, 2012	850,000	$ 0.90	$ 2.20	10
Exercisable June 30, 2012		$	$	

Expected future stock option expense related to the non-vested options outstanding as of June 30, 2012, is $669,877 over an average period of 2.28 years.

The following is a summary of the status of the Company s restricted shares as of June 30, 2012, and changes therein during the period then ended.

	Number of Shares Awarded	Weighted Average Grant Date Fair Value
Non-vested at December 31, 2011		$
Granted	104,346	1.73
Vested	(25,715)	1.73
Forfeited		
Non-vested at June 30, 2012	78,631	$ 1.73

Expected future stock award expense related to the non-vested restricted awards as of June 30, 2012, is $135,638 over an average period of 3.10 years.

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Note 6: Income Taxes

The determination of the amount of deferred income tax assets which are more likely than not to be realized is primarily dependent on projections of future earnings, which are subject to uncertainty and estimates that may change given economic conditions and other factors. A valuation allowance related to deferred tax assets is required when it is considered more likely than not that all or part of the benefit related to such assets will not be realized. Management has reviewed the deferred tax position of the Company at June 30, 2012. The deferred tax position has been affected by several significant transactions in the past several years. These transactions include increased provision for loan losses, the levels of non-accrual loans and other-than-temporary impairment write-offs of certain investments, as well as a loss on the bulk sale of loans in 2011. As a result, the Company is in a cumulative net loss position at June 30, 2012, and under the applicable accounting guidance, has concluded that it is not more-likely-than-not that the Company will be able to realize its deferred tax assets and, accordingly, has established a full valuation allowance totaling $13.5 million against its deferred tax asset at June 30, 2012. The valuation allowance is analyzed quarterly for changes affecting the deferred tax asset. In the future, if the Company generates taxable income on a sustained basis, management s conclusion regarding the need for a deferred tax asset valuation allowance could change, resulting in the reversal of all or a portion of the deferred tax asset valuation allowance.

An ownership change occurred with respect to the Company in 2010 for purposes of Section 382 of the Internal Revenue Code of 1986, as amended. Consequently, the Company s ability to claim net operating loss carryforwards attributable to periods prior to the ownership change and certain recognized built-in losses and deductions (pre-ownership change losses) against income in years subsequent to the ownership change is limited. The amount of pre-ownership change losses that may be applied against income in a tax year subsequent to the ownership change is generally limited to the product of (x) the Company s fair market value on the date of the ownership change and (y) the highest federal long-term tax-exempt rate in effect for any month in the three-month period ending with the calendar month in which the ownership change occurred, plus any unused capacity to claim pre-ownership change losses from prior years.

In 2011 the Company calculated the annual limitation on its use of pre-ownership change losses under Section 382 as a result of the 2010 ownership change as $284,000. The Company also determined that the amount of its pre-ownership change losses was $36.2 million. Based on that analysis and a 20-year carryforward period, the Company may utilize approximately $5.7 million of the pre-ownership change losses. Accordingly, the Company wrote-off approximately $10.4 million of deferred tax assets in 2011. The write-off of the deferred tax asset did not affect the consolidated financial statements as there was a full valuation allowance against the deferred tax assets.

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Note 7: Income (loss) per share

The Company is required to present basic income (loss) per share and diluted income (loss) per share in its consolidated statements of operations. Basic income (loss) per share amounts are computed by dividing net income (loss) by the weighted average number of common shares outstanding. Diluted income (loss) per share reflects additional common shares that would have been outstanding if potentially dilutive common shares had been issued, as well as any adjustment to income that would result from the assumed issuance. Potential common shares that may be issued by the Company relate to outstanding stock options and are determined using the treasury stock method. The Company is also required to provide a reconciliation of the numerator and denominator used in the computation of both basic and diluted income (loss) per share.

The stock options and non-vested restricted stock awards did not have an impact on the diluted earnings per share. The following is information about the computation of income (loss) per share for the three and six months ended June 30, 2012 and 2011:

Three months ended June 30, 2012	**Net Income**	**Weighted Average Common Shares O/S**	**Amount**
Basic and Diluted Income Per Share			
Income attributable to common shareholders	$ 345,282	38,381,988	$ 0.01

Three months ended June 30, 2011	Net Loss	Weighted Average Common Shares O/S	Amount
Basic and Diluted Loss Per Share			
Loss attributable to common shareholders	$ (7,175,368)	38,362,727	$ (0.19)

Six months ended June 30, 2012	**Net Income**	**Weighted Average Common Shares O/S**	**Amount**
Basic and Diluted Income Per Share			
Income attributable to common shareholders	$ 890,812	38,377,166	$ 0.02

Six months ended June 30, 2011	Net Loss	Weighted Average Common Shares O/S	Amount
Basic and Diluted Loss Per Share			
Loss attributable to common shareholders	$ (16,157,966)	38,362,727	$ (0.42)

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Note 8: Other Comprehensive Income

Other comprehensive income, which is comprised solely of the change in unrealized gains and losses on available-for-sale securities, is as follows:

	Three Months Ended June 30, 2012			Six Months Ended June 30, 2012		
	Before Tax Amount	Tax Effect	Net of Tax Amount	Before Tax Amount	Tax Effect	Net of Tax Amount
Unrealized holding gains arising during the period	$ 198,155	$ (75,299)	$ 122,856	$ 306,842	$ (116,601)	$ 190,241
Reclassification adjustment for (losses) recognized in income				(8,042)	3,056	(4,986)
Unrealized holding gains on available for sale securities, net of taxes	$ 198,155	$ (75,299)	$ 122,856	$ 298,800	$ (113,545)	$ 185,255

	Three Months Ended June 30, 2011			Six Months Ended June 30, 2011		
	Before Tax Amount	Tax Effect	Net of Tax Amount	Before Tax Amount	Tax Effect	Net of Tax Amount
Unrealized holding gains arising during the period	$ 453,931	$ (206,410)	$ 247,521	$ 459,133	$ (208,387)	$ 250,746
Reclassification adjustment for gains recognized in income						
Unrealized holding gains on available for sale securities, net of taxes	$ 453,931	$ (206,410)	$ 247,521	$ 459,133	$ (208,387)	$ 250,746

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Note 9: Financial Instruments with Off-Balance Sheet Risk

In the normal course of business, the Company is a party to financial instruments with off-balance-sheet risk to meet the financing needs of its customers. These financial instruments include commitments to extend credit and standby letters of credit and involve, to varying degrees, elements of credit and interest rate risk in excess of the amounts recognized in the balance sheet. The contractual amounts of these instruments reflect the extent of involvement the Company has in particular classes of financial instruments.

The contractual amount of commitments to extend credit and standby letters of credit represent the total amount of potential accounting loss should: the contracts be fully drawn upon; the customers default; and the value of any existing collateral becomes worthless. The Company uses the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments and evaluates each customer s creditworthiness on a case-by-case basis. Management believes that the Company controls the credit risk of these financial instruments through credit approvals, credit limits, monitoring procedures and the receipt of collateral as deemed necessary.

Financial instruments whose contractual amounts represent credit risk at June 30, 2012 are as follows:

Commitments to extend credit:	
Future loan commitments	$ 35,782,667
Home equity lines of credit	30,738,527
Unused lines of credit	37,402,837
Undisbursed construction loans	4,304,731
Financial standby letters of credit	7,000
	$ 108,235,762

Standby letters of credit are written commitments issued by the Company to guarantee the performance of a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. Guarantees that are not derivative contracts are recorded on the Company s consolidated balance sheet at their fair value at inception.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments to extend credit generally have fixed expiration dates, or other termination clauses, and may require payment of a fee by the borrower. Since these commitments could expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The amount of collateral obtained, if deemed necessary by the Company upon extension of credit, is based on management s credit evaluation of the counterparty. Collateral held varies, but may include residential and commercial property, deposits and securities. Based on the growth in the unfunded commitments, the bank has established a reserve of $26,000 as of June 30, 2012.

Note 10: Regulatory and Operational Matters

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

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Quantitative measures established by regulation to ensure capital adequacy require the Company and the Bank to maintain minimum amounts and ratios (set forth in the table below) of total and Tier I capital (as defined in the regulations) to risk-weighted assets (as defined), and of Tier I capital (as defined) to average assets (as defined). In addition, due to the Bank s asset profile and current economic conditions in its markets, the Bank s capital plan targets a minimum 9% Tier 1 leverage capital ratio.

In February 2009 the Bank entered into a formal written agreement (the Agreement) with the Office of the Comptroller of the Currency. Under the terms of the Agreement, the Bank has appointed a Compliance Committee of outside directors and the Chief Executive Officer. The Committee must report quarterly to the Board of Directors and to the OCC on the Bank s progress in complying with the Agreement. The Agreement requires the Bank to review, adopt and implement a number of policies and programs related to credit and operational issues. The Agreement further provides for limitations on the acceptance of certain brokered deposits and the extension of credit to borrowers whose loans are criticized. The Bank may pay dividends during the term of the Agreement only with prior written permission from the OCC. The Agreement also requires that the Bank develop and implement a three-year capital plan. The Bank has taken or put into process many of the steps required by the Agreement, and does not anticipate that the restrictions included within the Agreement will impair its current business plan.

In June 2010 the company entered into a formal written agreement (the Reserve Bank Agreement) with the Federal Reserve Bank of New York (the Reserve Bank). Under the terms of the Reserve Bank Agreement, the Board of Directors of the Company are required to take appropriate steps to fully utilize the Company s financial and managerial resources to serve as a source of strength to the Bank including taking steps to insure that the Bank complies with the Agreement with the OCC. The Reserve Bank Agreement requires the Company to submit, adopt and implement a capital plan that is acceptable to the Reserve Bank. The Company must also report to the Reserve Bank quarterly on the Company s progress in complying with the Reserve Bank Agreement. The Agreement further provides for certain restrictions on the payment or receipt of dividends, distributions of interest or principal on subordinate debentures or trust preferred securities and the Company s ability to incur debt or to purchase or redeem its stock without the prior written approval of the Reserve Bank. The Company has taken or put into process many of the steps required by the Reserve Bank Agreement, and does not anticipate that the restrictions included within the Reserve Bank Agreement will impair its current business plan.

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The Company s and the Bank s actual capital amounts and ratios at June 30, 2012 and December 31, 2011 were:

(dollars in thousands)	Actual Amount	Actual Ratio	For Capital Adequacy Purposes Amount	For Capital Adequacy Purposes Ratio	To Be Well Capitalized Under Prompt Corrective Action Provisions Amount	To Be Well Capitalized Under Prompt Corrective Action Provisions Ratio
June 30, 2012						
The Company:						
Total Capital (to Risk Weighted Assets)	$ 64,556	15.85%	$ 32,583	8.00%	N/A	N/A
Tier 1 Capital (to Risk Weighted Assets)	59,439	14.60%	16,285	4.00%	N/A	N/A
Tier 1 Capital (to Average Assets)	59,439	9.13%	26,041	4.00%	N/A	N/A
The Bank:						
Total Capital (to Risk Weighted Assets)	$ 62,935	15.43%	$ 32,630	8.00%	$ 40,787	10.00%
Tier 1 Capital (to Risk Weighted Assets)	57,819	14.18%	16,310	4.00%	24,465	6.00%
Tier 1 Capital (to Average Assets)	57,819	8.88%	26,045	4.00%	32,556	5.00%
December 31, 2011						
The Company:						
Total Capital (to Risk Weighted Assets)	$ 63,658	15.22%	$ 33,469	8.00%	N/A	N/A
Tier 1 Capital (to Risk Weighted Assets)	58,377	13.95%	16,735	4.00%		