FIRST NORTHERN COMMUNITY BANCORP
Form 10-Q
May 09, 2013
UNITED STATES

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark one)

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

For the Quarterly Period Ended March 31, 2013

OR

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

For the transition period from _______________ to _______________

Commission File Number 000-30707

First Northern Community Bancorp
(Exact name of registrant as specified in its charter)

California	68-0450397
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
195 N. First Street, Dixon, California	95620
(Address of principal executive offices)	(Zip Code)

707-678-3041
(Registrant's telephone number including area code)

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or Section 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 x No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, 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 r

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company (as defined by Rule 12b-2 of the Exchange Act). 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 ¨ (Do not check if a smaller reporting company)	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

The number of shares of Common Stock outstanding as of May 9, 2013 was 9,476,800.

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PART I – FINANCIAL INFORMATION

FIRST NORTHERN COMMUNITY BANCORP

ITEM I. – FINANCIAL STATEMENTS (UNAUDITED)

CONDENSED CONSOLIDATED BALANCE SHEETS (UNAUDITED)

(in thousands, except shares and share amounts)	March 31, 2013	December 31, 2012
Assets		
Cash and cash equivalents	$166,114	$161,359
Investment securities – available-for-sale	201,861	184,491
Loans, net of allowance for loan losses of $8,846 at March 31, 2013 and $8,554 at December 31, 2012	439,635	440,449
Loans held-for-sale	3,831	4,559
Stock in Federal Home Loan Bank and other equity securities, at cost	3,607	3,607
Premises and equipment, net	7,742	7,839
Other real estate owned	1,062	1,062
Interest receivable and other assets	28,708	28,117
Total Assets	$852,560	$831,483
Liabilities and Stockholders' Equity		
Liabilities:		
Demand deposits	$251,500	$230,743
Interest-bearing transaction deposits	193,361	184,900
Savings and MMDA's	225,767	223,078
Time, under $100,000	35,058	35,617
Time, $100,000 and over	56,024	56,473
Total deposits	761,710	730,811
Interest payable and other liabilities	7,607	8,347
Total Liabilities	769,317	739,158
Stockholders' Equity:		
Preferred stock, no par value; $1,000 per share liquidation preference, 22,847 shares authorized; 22,847 shares issued and 12,847 shares outstanding at March 31, 2013 and 22,847 shares issued and outstanding at December 31, 2012	12,847	22,847
Common stock, no par value; 16,000,000 shares authorized; 9,476,800 shares issued and outstanding at March 31, 2013 and 9,272,668 shares issued and outstanding at December 31, 2012	64,391	63,410

Additional paid-in capital	977	977
Retained earnings	4,017	3,917
Accumulated other comprehensive income, net	1,011	1,174
Total Stockholders’ Equity	83,243	92,325
Total Liabilities and Stockholders’ Equity	$852,560	$831,483

See notes to unaudited condensed consolidated financial statements.

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CONDENSED CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)

(in thousands, except per share amounts)	Three months ended March 31, 2013	Three months ended March 31, 2012
Interest and dividend income:		
Loans	$5,971	$5,990
Due from banks interest bearing accounts	105	79
Investment securities		
Taxable	693	780
Non-taxable	100	104
Other earning assets	—	4
Total interest and dividend income	6,869	6,957
Interest expense:		
Deposits	334	492
Other borrowings	—	72
Total interest expense	334	564
Net interest income	6,535	6,393
Provision for loan losses	400	550
Net interest income after provision for loan losses	6,135	5,843
Other operating income:		
Service charges on deposit accounts	653	653
Gains on sales of loans held-for-sale	568	395
Investment and brokerage services income	301	221
Mortgage brokerage income	29	30
Loan servicing income	367	142
Fiduciary activities income	132	107
ATM fees	84	129
Signature based transaction fees	292	248
Gains on calls of available-for-sale securities	4	1
Other income	191	199
Total other operating income	2,621	2,125
Other operating expenses:		
Salaries and employee benefits	4,129	3,847
Occupancy and equipment	783	736
Data processing	420	385
Stationery and supplies	85	80
Advertising	81	110
Directors’ fees	57	55
Other real estate owned expense and impairment	12	22
Other expense	1,187	1,257
Total other operating expenses	6,754	6,492

Income before income tax expense	2,002	1,476
Income tax expense	639	384
Net income	$1,363	$1,092
Preferred stock dividends	(212)	(285)
Net income available to common stockholders	$1,151	$807
Basic income per share	$0.12	$0.09
Diluted income per share	$0.12	$0.09

See notes to unaudited condensed consolidated financial statements.

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CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (UNAUDITED)

(in thousands)	Three months ended March 31, 2013	Three months ended March 31, 2012
Net income	$1,363	$1,092
Other comprehensive income, net of tax:		
Unrealized holding gains on securities:		
Unrealized holding gains arising during the period, net of tax effect of $106 and $391 for the three-month periods ended March 31, 2013 and March 31, 2012, respectively	(161)	587
Less: reclassification adjustment due to gains realized on sales of securities, net of tax effect of $2 and $0 for the three-month periods ended March 31, 2013 and March 31, 2012, respectively	(2)	(1)
Other comprehensive (loss) income	$(163)	$586
Comprehensive income	$1,200	$1,678

See notes to unaudited condensed consolidated financial statements.

FIRST NORTHERN COMMUNITY BANCORP

CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY (UNAUDITED)

(in thousands, except share data)

	Preferred Stock		Common Stock		Additional	Retained	Accumulated Other Comprehensive	
	Shares	Amounts	Shares	Amounts	Paid-in Capital	Earnings	Income	Total
Balance at December 31, 2012	22,847	$22,847	9,272,668	$63,410	$977	$3,917	$ 1,174	$92,325
Net income						1,363		1,363
Other comprehensive loss							(163)	(163)
Redemption of preferred stock	(10,000)	(10,000)						(10,000)
2% stock dividend			185,291	1,047		(1,047)		—
Dividend on preferred stock						(212)		(212)
Cash in lieu of fractional shares			(159)			(4)		(4)
Stock-based compensation				40				40
Tax deficiency related to expired, vested non-qualified stock options				(106)				(106)
Common shares issued related to restricted stock grants, net			19,000					—
Balance at March 31, 2013	12,847	$12,847	9,476,800	$64,391	$977	$4,017	$ 1,011	$83,243

See notes to unaudited condensed consolidated financial statements.

FIRST NORTHERN COMMUNITY BANCORP

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

	(in thousands)	
	Three months ended March 31, 2013	Three months ended March 31, 2012
Cash Flows From Operating Activities		
Net Income	$1,363	$ 1,092
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	182	174
Accretion and amortization of investment securities premiums and discounts, net	916	740
Valuation adjustment on mortgage servicing rights	(148)	38
Decrease in deferred loan origination fees and costs, net	(63)	(15)
Provision for loan losses	400	550
Stock plan accruals	40	31
Gains on calls of available-for-sale securities	(4)	(1)
Gains on sales of loans held-for-sale	(568)	(395)
Proceeds from sales of loans held-for-sale	23,450	18,880
Originations of loans held-for-sale	(22,154)	(18,432)
Changes in assets and liabilities:		
(Increase) decrease in interest receivable and other assets	(441)	1,109
Decrease in interest payable and other liabilities	(740)	(310)
Net cash provided by operating activities	2,233	3,461
Cash Flows From Investing Activities		
Net increase in investment securities	(18,553)	(27,101)
Net decrease in loans	477	15,256
Purchases of premises and equipment, net	(85)	(192)
Net cash used in investing activities	(18,161)	(12,037)
Cash Flows From Financing Activities		
Net increase in deposits	30,899	11,265
Redemption of preferred stock	(10,000)	—
Cash dividends paid in lieu of fractional shares	(4)	(3)
Cash dividends paid on preferred stock	(212)	(285)
Net cash provided by financing activities	20,683	10,977
Net increase in Cash and Cash Equivalents	4,755	2,401
Cash and Cash Equivalents, beginning of period	161,359	140,172
Cash and Cash Equivalents, end of period	$166,114	142,573
Supplemental Disclosures of Cash Flow Information:		

Cash paid during the period for:		
Interest	$334	$ 577
Supplemental disclosures of non-cash investing and financing activities:		
Stock dividend distributed	$1,047	$ 451
Tax deficiency related to expired, vested non-qualified stock options	$(106)	$ —
Transfer of loans held-for-investment to other real estate owned	$—	$ 293
Unrealized holding (losses) gains on available for sale securities, net of taxes	$(163)	$ 586

See notes to unaudited condensed consolidated financial statements.

FIRST NORTHERN COMMUNITY BANCORP

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2013 and 2012 and December 31, 2012

1. BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements of First Northern Community Bancorp (the "Company") have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) for interim financial information and with the instructions to Form 10-Q and Articles 9 and 10 of Regulation S-X. Accordingly, they do not include all of the information and notes required by GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. The results of operations for any interim period are not necessarily indicative of results expected for the full year. These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto contained in the Company's Annual Report on Form 10-K for the year ended December 31, 2012 as filed with the Securities and Exchange Commission. The preparation of financial statements in conformity with GAAP also requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expense during the reporting period. Actual results could differ from those estimates. All material intercompany balances and transactions have been eliminated in consolidation.

Recently Issued Accounting Pronouncements:

In June 2011, FASB issued ASU 2011-05. This update allows an entity the option to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. In both choices, an entity is required to present each component of net income along with total net income, each component of other comprehensive income along with a total for other comprehensive income, and a total amount for comprehensive income. This update eliminates the option to present the components of other comprehensive income as part of the statement of stockholders' equity. The amendments in this ASU are to be applied retrospectively and are effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. Adoption of the new guidance did not have a significant impact on the Company's consolidated financial statements. In December 2011, FASB issued ASU 2011-12. This update defers the effective date for amendments to the presentation of reclassifications of items out of accumulated other comprehensive income in ASU 2011-05. In February 2013, FASB issued ASU 2013-02. This update requires an entity to provide information about the amounts reclassified out of accumulated other comprehensive income by component. In addition, an entity is required to present, either on the face of the statement where net income is presented or in the notes, significant amounts reclassified out of accumulated other comprehensive income by the respective line items of net income but only if the amount reclassified is required under U.S. GAAP to be reclassified to net income in its entirety in the same reporting period. For other amounts that are not required under U.S. GAAP to be reclassified in their entirety to net income, an entity is required to cross-reference to other disclosures required under U.S. GAAP that provide additional detail about those amounts. The amendments in ASU 2013-02 are effective prospectively for reporting periods beginning after December 15, 2012. Adoption of the new guidance did not have a significant impact on the Company's consolidated financial statements.

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In December 2011, FASB issued ASU 2011-11. The amendments in this ASU require an entity to disclose information about offsetting and related arrangements to enable users of its financial statements to understand the effect of those arrangements on its financial position. The amendments in this ASU are required for annual reporting periods beginning on or after January 1, 2013, and interim periods within those annual periods. The disclosures required by those amendments should be provided retrospectively for all comparative periods presented. The Company does not expect the adoption of this update to have a significant impact on its consolidated financial statements. In January 2013, FASB issued ASU 2013-01. This update clarifies that ordinary trade receivables and receivables are not in the scope of ASU 2011-11. ASU 2011-11 applies only to derivatives, repurchase agreements and reverse purchase agreements, and securities borrowing and securities lending transactions that are either offset in accordance with specific criteria contained in the Codification or subject to a master netting arrangement or similar agreement. This update has the same effective date as ASU 2011-11.

Reclassifications

Certain reclassifications have been made to prior period balances in order to conform to the current year presentation.

2. LOANS

The composition of the Company's loan portfolio, by loan class, is as follows:

($ in thousands)	March 31, 2013	December 31, 2012
Commercial	$94,253	$88,810
Commercial Real Estate	196,081	188,426
Agriculture	40,012	52,747
Residential Mortgage	51,760	51,266
Residential Construction	7,984	7,586
Consumer	57,553	59,393
	447,643	448,228
Allowance for loan losses	(8,846)	(8,554)
Net deferred origination fees and costs	838	775
Loans, net	$439,635	$440,449

The Company manages asset quality and credit risk by maintaining diversification in its loan portfolio and through review processes that include analysis of credit requests and ongoing examination of outstanding loans and delinquencies, with particular attention to portfolio dynamics and loan mix. The Company strives to identify loans experiencing difficulty early enough to correct the problems, to record charge-offs promptly based on realistic assessments of collectability and current collateral values and to maintain an adequate allowance for loan losses at all times. Asset quality reviews of loans and other non-performing assets are administered using credit risk rating standards and criteria similar to those employed by state and federal banking regulatory agencies.

Residential mortgage loans, which are secured by real estate, are primarily susceptible to four risks; non-payment due to diminished or lost income, over-extension of credit, a lack of borrower's cash flow to sustain payments, and shortfalls in collateral value. In general, non-payment is usually due to loss of employment and follows general economic trends in the economy, particularly the upward movement in the unemployment rate, loss of collateral value, and demand shifts.

Commercial real estate loans generally fall into two categories, owner-occupied and non-owner occupied. Loans secured by owner occupied real estate are primarily susceptible to changes in the market conditions of the related business. This may be driven by, among other things, industry changes, geographic business changes, changes in the individual financial capacity of the business owner, general economic conditions and changes in business cycles. These same risks apply to commercial loans whether secured by equipment, receivables or other personal property or unsecured. Losses on loans secured by owner occupied real estate, equipment, or other personal property generally are dictated by the value of underlying collateral at the time of default and liquidation of the collateral. When default is driven by issues related specifically to the business owner, collateral values tend to provide better repayment support and may result in little or no loss. Alternatively, when default is driven by more general economic conditions,

underlying collateral generally has devalued more and results in larger losses due to default. Loans secured by non-owner occupied real estate are primarily susceptible to risks associated with swings in occupancy or vacancy and related shifts in lease rates, rental rates or room rates. Most often, these shifts are a result of changes in general economic or market conditions or overbuilding and resulting over-supply of space. Losses are dependent on the value of underlying collateral at the time of default. Values are generally driven by these same factors and influenced by interest rates and required rates of return as well as changes in occupancy costs. Collateral values may be determined by appraisals obtained through Bank approved, licensed appraisers, qualified independent third parties, sales invoices, or other appropriate means. Collateral valuations are obtained at origination of the credit and periodically thereafter (generally every 3 – 6 months depending on the collateral type), once repayment is questionable, and the loan has been deemed classified.

Construction loans, whether owner occupied or non-owner occupied residential development loans, are not only susceptible to the related risks described above but the added risks of construction, including cost over-runs, mismanagement of the project, or lack of demand and market changes experienced at time of completion. Losses are primarily related to underlying collateral value and changes therein as described above. Problem construction loans are generally identified by periodic review of financial information that may include financial statements, tax returns and payment history of the borrower. Based on this information the Company may decide to take any of several courses of action including demand for repayment, requiring the borrower to provide a significant principal payment and/or additional collateral or requiring similar support from guarantors, or repossession or foreclosure of the underlying collateral. Collateral values may be determined by appraisals obtained through Bank approved, licensed appraisers, qualified independent third parties, purchase invoices, or other appropriate documentation. Collateral valuations are obtained at origination of the credit and periodically thereafter (generally every 3 – 6 months depending on the collateral type), once repayment is questionable, and the loan has been deemed classified.

Agricultural loans, whether secured or unsecured, generally are made to producers and processors of crops and livestock. Repayment is primarily from the sale of an agricultural product or service. Agricultural loans are generally secured by inventory, receivables, equipment, and other real property. Agricultural loans primarily are susceptible to changes in market demand for specific commodities. This may be exacerbated by, among other things, industry changes, changes in the individual financial capacity of the business owner, general economic conditions and changes in business cycles, as well as adverse weather conditions. Problem agricultural loans are generally identified by periodic review of financial information that may include financial statements, tax returns, crop budgets, payment history, and crop inspections. Based on this information, the Company may decide to take any of several courses of action including demand for repayment, requiring the borrower to provide a significant principal payment and/or additional collateral or requiring similar support from guarantors. Notwithstanding, when repayment becomes unlikely based on the borrower's income and cash flow, repossession or foreclosure of the underlying collateral may become necessary. Collateral values may be determined by appraisals obtained through Bank approved, licensed appraisers, qualified independent third parties, purchase invoices, or other appropriate documentation. Collateral valuations are obtained at origination of the credit and periodically thereafter (generally every 3 – 6 months depending on the collateral type), once repayment is questionable, and the loan has been deemed classified.

Commercial loans, whether secured or unsecured, generally are made to support the short-term operations and other needs of small businesses. These loans are generally secured by the receivables, equipment, and other real property of the business and are susceptible to the related risks described above. Problem commercial loans are generally identified by periodic review of financial information that may include financial statements, tax returns, and payment history of the borrower. Based on this information, the Company may decide to take any of several courses of action including demand for repayment, requiring the borrower to provide a significant principal payment and/or additional collateral or requiring similar support from guarantors. Notwithstanding, when repayment becomes unlikely based on the borrower's income and cash flow, repossession or foreclosure of the underlying collateral may become necessary. Collateral values may be determined by appraisals obtained through Bank approved, licensed appraisers, qualified independent third parties, purchase invoices, or other appropriate documentation. Collateral valuations are obtained at origination of the credit and periodically thereafter (generally every 3 – 6 months depending on the collateral type), once repayment is questionable, and the loan has been deemed classified.

Consumer loans, whether unsecured or secured are primarily susceptible to four risks; non-payment due to diminished or lost income, over-extension of credit, a lack of borrower's cash flow to sustain payments, and shortfall in collateral value. In general, non-payment is usually due to loss of employment and will follow general economic trends in the economy, particularly the upward movements in the unemployment rate, loss of collateral value, and demand shifts.

As of March 31, 2013, approximately 43% in principal amount of the Company's loans were secured by commercial real estate, which consists of construction and land development loans and loans secured by commercial

properties. Approximately 12% of the Company's loans were residential mortgage loans. Approximately 2% of the Company's loans were residential construction loans. Approximately 9% of the Company's loans were for agriculture and 21% of the Company's loans were for general commercial uses including professional, retail and small businesses. Approximately 13% of the Company's loans were consumer loans.

Once a loan becomes delinquent and repayment becomes questionable, a Company collection officer will address collateral shortfalls with the borrower and attempt to obtain additional collateral or a principal payment. If this is not forthcoming and payment in full is unlikely, the Company will estimate its probable loss, using a recent valuation as appropriate to the underlying collateral less estimated costs of sale, and charge-off the loan down to the estimated net realizable amount. Depending on the length of time until final collection, the Company may periodically revalue the underlying collateral and take additional charge-offs as warranted. Revaluations may occur as often as every 3-12 months depending on the underlying collateral and volatility of values. Final charge-offs or recoveries are taken when collateral is liquidated and actual loss is known. Unpaid balances on loans after or during collection and liquidation may also be pursued through legal action and attachment of wages or judgment liens on the borrower's other assets.

All loans at March 31, 2013 and December 31, 2012 were pledged under a blanket collateral lien to secure actual and potential borrowings from the Federal Home Loan Bank and Federal Reserve.

Non-accrual and Past Due Loans

The Company’s non-accrual loans by loan class, as of March 31, 2013 and December 31, 2012 were as follows:

($ in thousands)	March 31, 2013	December 31, 2012
Commercial	$2,747	$2,853
Commercial Real Estate	1,840	1,879
Agriculture	—	—
Residential Mortgage	1,940	2,095
Residential Construction	—	—
Consumer	282	441
	$6,809	$7,268

Non-accrual loans amounted to $6,809,000 at March 31, 2013 and were comprised of seven residential mortgage loans totaling $1,940,000, four commercial real estate loans totaling $1,840,000, nine commercial loans totaling $2,747,000 and five consumer loans totaling $282,000. Non-accrual loans amounted to $7,268,000 at December 31, 2012 and were comprised of seven residential mortgage loans totaling $2,095,000, five commercial real estate loans totaling $1,879,000, eleven commercial loans totaling $2,853,000 and seven consumer loans totaling $441,000. It is generally the Company’s policy to charge-off the portion of any non-accrual loan that the Company does not expect to collect by writing the loan down to the estimated net realizable value of the underlying collateral.

An age analysis of past due loans, segregated by loan class, as of March 31, 2013 and December 31, 2012 is as follows:

($ in thousands)	30-59 Days Past Due	60-89 Days Past Due	90 Days or more Past Due	Total Past Due	Current	Total Loans
March 31, 2013						
Commercial	$159	$103	$146	$408	$93,845	$94,253
Commercial Real Estate	345	—	549	894	195,187	196,081
Agriculture	156	—	—	156	39,856	40,012
Residential Mortgage	467	—	347	814	50,946	51,760
Residential Construction	52	—	—	52	7,932	7,984
Consumer	7	—	189	196	57,357	57,553
Total	$1,186	$103	$1,231	$2,520	$445,123	$447,643
December 31, 2012						
Commercial	$2,255	$—	$170	$2,425	$86,385	$88,810
Commercial Real Estate	1,272	—	566	1,838	186,588	188,426
Agriculture	—	—	—	—	52,747	52,747
Residential Mortgage	570	103	335	1,008	50,258	51,266
Residential Construction	53	—	—	53	7,533	7,586
Consumer	8	747	126	881	58,512	59,393
Total	$4,158	$850	$1,197	$6,205	$442,023	$448,228

The Company had no loans 90 days or more past due and still accruing at March 31, 2013 and December 31, 2012.

Impaired Loans

A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect all amounts due according to the contractual terms of the loan agreement, including scheduled interest payments. Loans to be considered for impairment include non-accrual loans, troubled debt restructurings and loans with a risk rating of 6 (substandard) or worse. Once identified, impaired loans are measured individually for impairment using one of three methods: present value of expected cash flows discounted at the loan's effective interest rate; the loan's observable market price; fair value of collateral if the loan is collateral dependent. In general, any portion of the recorded investment in a collateral dependent loan in excess of the fair value of the collateral that can be identified as uncollectible, and is, therefore, deemed a confirmed loss, should be promptly charged-off against the allowance for loan losses.

Impaired loans, segregated by loan class, as of March 31, 2013 and December 31, 2012 were as follows:

($ in thousands)	Unpaid Contractual Principal Balance	Recorded Investment with no Allowance	Recorded Investment with Allowance	Total Recorded Investment	Related Allowance
March 31, 2013					
Commercial	$ 3,732	$ 2,678	$ 732	$ 3,410	$ 82
Commercial Real Estate	2,993	1,840	1,153	2,993	22
Agriculture	—	—	—	—	—
Residential Mortgage	5,167	1,940	2,714	4,654	448
Residential Construction	1,141	—	1,091	1,091	370
Consumer	1,162	343	625	968	103
Total	$ 14,195	$ 6,801	$ 6,315	$ 13,116	$ 1,025
December 31, 2012					
Commercial	$ 3,628	$ 2,769	$ 519	$ 3,288	$ 95
Commercial Real Estate	3,629	1,872	1,170	3,042	26
Agriculture	—	—	—	—	—
Residential Mortgage	5,831	1,860	2,963	4,823	417
Residential Construction	1,148	—	1,097	1,097	433
Consumer	1,416	502	629	1,131	101
Total	$ 15,652	$ 7,003	$ 6,378	$ 13,381	$ 1,072

Interest income on impaired loans recognized during the three-month periods ended March 31, 2013 and March 31, 2012 was as follows:

($ in thousands)	Three Months Ended March 31, 2013		Three Months Ended March 31, 2012	
	Average Recorded Investment	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized
Commercial	$ 3,531	$ 8	$ 3,642	$ 10
Commercial Real Estate	4,018	22	7,175	23
Agriculture	345	—	1,823	25
Residential Mortgage	4,592	27	4,878	29

Residential Construction	1,115	11	1,318	13
Consumer	1,009	8	622	7
Total	$ 14,610	$ 76	$ 19,458	$ 107

None of the interest on impaired loans was recognized using a cash basis of accounting for the three-month periods ended March 31, 2013 and March 31, 2012.

Troubled Debt Restructurings

The Company's loan portfolio includes certain loans that have been modified in a Troubled Debt Restructuring ("TDR"), which are loans on which concessions in terms have been granted because of the borrowers' financial difficulties. These concessions typically result from the Company's loss mitigation activities and could include reductions in the interest rate, payment extensions, forgiveness of principal, forbearance, or other actions. Certain TDRs are placed on non-accrual status at the time of restructure and may only be returned to accruing status after considering the borrower's sustained repayment performance for a reasonable period, generally six months.

When a loan is modified, it is measured based upon the present value of future cash flows discounted at the contractual interest rate of the original loan agreement, or the fair value of collateral less selling costs if the loan is collateral dependent. If the value of the modified loan is less than the recorded investment in the loan, impairment is recognized through a specific allowance or a charge-off of the loan.

The Company had $7,085,000 and $6,905,000 in TDR loans as of March 31, 2013 and December 31, 2012, respectively. Specific reserves for TDR loans totaled $918,000 and $939,000 as of March 31, 2013 and December 31, 2012, respectively. TDR loans performing in compliance with modified terms totaled $6,234,000 and $6,040,000 as of March 31, 2013 and December 31, 2012, respectively. There are no commitments to advance more funds on existing TDR loans as of March 31, 2013.

Loans modified as troubled debt restructurings during the three-month periods ended March 31, 2013 and March 31, 2012 were as follows:

($ in thousands)	Three Months Ended March 31, 2013		
	Number of Contracts	Pre-modification outstanding recorded investment	Post-modification outstanding recorded investment
Commercial	1	$ 244	$ 244
Total	1	$ 244	$ 244

($ in thousands)	Three Months Ended March 31, 2012		
	Number of Contracts	Pre-modification outstanding recorded investment	Post-modification outstanding recorded investment
Commercial	2	$ 220	$ 220
Consumer	2	151	151
Total	4	$ 371	$ 371

The loan modifications generally involved reductions in the interest rate, payment extensions, forgiveness of principal, and forbearance. There were no loans modified as a troubled debt restructuring within the previous 12 months and for which there was a payment default during the three-month period ended March 31, 2013. There was one commercial loan with a recorded investment of $136,000 that was modified as a troubled debt restructuring within the previous 12 months and for which there was a payment default during the three-month period ended March 31, 2012.

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Credit Quality Indicators

All new loans are rated using the credit risk ratings and criteria adopted by the Company. Risk ratings are adjusted as future circumstances warrant. All credits risk rated 1, 2, 3 or 4 equate to a Pass as indicated by Federal and State regulatory agencies; a 5 equates to a Special Mention; a 6 equates to Substandard; a 7 equates to Doubtful; and 8 equates to a Loss. For the definitions of each risk rating, see Note 4 to our condensed consolidated financial statements included in our Annual Report on Form 10-K for the year ended December 31, 2012.

The following table presents the risk ratings by loan class as of March 31, 2013 and December 31, 2012.

($ in thousands)	Pass	Special Mention	Substandard	Doubtful	Loss	Total
March 31, 2013						
Commercial	$84,915	$3,735	$ 5,603	$—	$—	$94,253
Commercial Real Estate	177,639	9,225	9,217	—	—	196,081
Agriculture	37,080	152	2,780	—	—	40,012
Residential Mortgage	47,032	1,146	3,582	—	—	51,760
Residential Construction	5,709	2,012	263	—	—	7,984
Consumer	50,831	4,444	2,278	—	—	57,553
Total	$403,206	$20,714	$ 23,723	$—	$—	$447,643
December 31, 2012						
Commercial	$78,078	$4,393	$ 6,339	$—	$—	$88,810
Commercial Real Estate	170,676	9,049	8,701	—	—	188,426
Agriculture	49,613	172	2,962	—	—	52,747
Residential Mortgage	45,962	604	4,700	—	—	51,266
Residential Construction	5,512	1,212	862	—	—	7,586
Consumer	51,444	4,822	3,054	73	—	59,393
Total	$401,285	$20,252	$ 26,618	$73	$—	$448,228

Allowance for Loan Losses

The following table details activity in the allowance for loan losses by loan class for the three-month periods ended March 31, 2013 and March 31, 2012.

Three-month period ended March 31, 2013

($ in thousands)	Commercial	Commercial Real Estate	Agriculture	Residential Mortgage	Residential Construction	Consumer	Unallocated	Total
Balance as of December 31, 2012	$ 2,899	$ 1,723	$ 915	$ 1,148	$ 724	$ 1,110	$ 35	$ 8,554
Provision for loan losses	25	371	(104)	(97)	(175)	(13)	393	400
Charge-offs	(111)	—	(1)	(78)	—	(58)	—	(248)
Recoveries	75	1	3	—	41	20	—	140
Net charge-offs	(36)	1	2	(78)	41	(38)	—	(108)
Balance as of March 31, 2013	2,888	2,095	813	973	590	1,059	428	8,846
Period-end amount allocated to:								
Loans individually evaluated for impairment	82	22	—	448	370	103	—	1,025
Loans collectively evaluated for impairment	2,806	2,073	813	525	220	956	428	7,821
Balance as of March 31, 2013	$ 2,888	$ 2,095	$ 813	$ 973	$ 590	$ 1,059	$ 428	$ 8,846

Three-month period ended March 31, 2012

($ in thousands)	Commercial	Commercial Real Estate	Agriculture	Residential Mortgage	Residential Construction	Consumer	Unallocated	Total
Balance as of December 31, 2011	$ 3,598	$ 1,747	$ 1,934	$ 1,135	$ 1,198	$ 796	$ —	$ 10,408
Provision for loan losses	320	(32)	(769)	90	(74)	781	234	550
Charge-offs	(542)	—	—	(31)	—	(264)	—	(837)
Recoveries	206	—	2	—	1	27	—	236
Net charge-offs	(336)	—	2	(31)	1	(237)	—	(601)
Balance as of March 31, 2012	3,582	1,715	1,167	1,194	1,125	1,340	234	10,357
Period-end amount allocated to:								
Loans individually evaluated for	368	199	—	636	737	394	—	2,334

impairment								
Loans collectively evaluated for impairment	3,214	1,516	1,167	558	388	946	234	8,023
Balance as of March 31, 2012	$ 3,582	$ 1,715	$ 1,167	$ 1,194	$ 1,125	$ 1,340	$ 234	$ 10,357

The following table details activity in the allowance for loan losses and the amount allocated to loans individually and collectively evaluated for impairment as of and for the period ended December 31, 2012.

($ in thousands)	Commercial	Commercial Real Estate	Agriculture	Residential Mortgage	Residential Construction	Consumer	Unallocated	Total
Balance as of December 31, 2011	$ 3,598	$ 1,747	$ 1,934	$ 1,135	$ 1,198	$ 796	$ —	$ 10,408
Provision for loan losses	2,493	351	(907)	877	(648)	1,075	35	3,276
Charge-offs	(3,498)	(375)	(116)	(864)	(167)	(875)	—	(5,895)
Recoveries	306	—	4	—	341	114	—	765
Net charge-offs	(3,192)	(375)	(112)	(864)	174	(761)	—	(5,130)
Balance as of December 31, 2012	2,899	1,723	915	1,148	724	1,110	35	8,554
Period-end amount allocated to:								
Loans individually evaluated for impairment	95	26	—	417	433	101	—	1,072
Loans collectively evaluated for impairment	2,804	1,697	915	731	291	1,009	35	7,482
Balance as of December 31, 2012	$ 2,899	$ 1,723	$ 915	$ 1,148	$ 724	$ 1,110	$ 35	$ 8,554

The Company's investment in loans as of March 31, 2013, March 31, 2012, and December 31, 2012 related to each balance in the allowance for loan losses by loan class and disaggregated on the basis of the Company's impairment methodology was as follows:

($ in thousands)	Commercial	Commercial Real Estate	Agriculture	Residential Mortgage	Residential Construction	Consumer	Total
March 31, 2013							
Loans individually evaluated for impairment	$ 3,410	$ 2,993	$—	$ 4,654	$ 1,091	$ 968	$ 13,116
Loans collectively evaluated for impairment	90,843	193,088	40,012	47,106	6,893	56,585	434,527
Ending Balance	$ 94,253	$ 196,081	$ 40,012	$ 51,760	$ 7,984	$ 57,553	$ 447,643
March 31, 2012							
Loans individually	$ 3,840	$ 4,670	$ 1,570	$ 3,534	$ 1,294	$ 942	$ 15,850

evaluated for impairment							
Loans collectively evaluated for impairment	85,130	172,588	36,443	48,454	6,521	61,863	410,999
Ending Balance	$ 88,970	$ 177,258	$ 38,013	$ 51,988	$ 7,815	$ 62,805	$ 426,849
December 31, 2012							
Loans individually evaluated for impairment	$ 3,288	$ 3,042	$—	$ 4,823	$ 1,097	$ 1,131	$ 13,381
Loans collectively evaluated for impairment	85,522	185,384	52,747	46,443	6,489	58,262	434,847
Ending Balance	$ 88,810	$ 188,426	$ 52,747	$ 51,266	$ 7,586	$ 59,393	$ 448,228

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3. MORTGAGE OPERATIONS

Transfers and servicing of financial assets and extinguishments of liabilities are accounted for and reported based on consistent application of a financial-components approach that focuses on control. Transfers of financial assets that are sales are distinguished from transfers that are secured borrowings. Retained interests (mortgage servicing rights) in loans sold are measured by allocating the previous carrying amount of the transferred assets between the loans sold and retained interests, if any, based on their relative fair value at the date of transfer. Fair values are estimated using discounted cash flows based on a current market interest rate.

The Company recognizes a gain and a related asset for the fair value of the rights to service loans for others when loans are sold. The Company sold substantially its entire portfolio of conforming long-term residential mortgage loans originated during the three months ended March 31, 2013 for cash proceeds equal to the fair value of the loans.

The recorded value of mortgage servicing rights is included in other assets, and is amortized in proportion to, and over the period of, estimated net servicing revenues. The Company assesses capitalized mortgage servicing rights for impairment based upon the fair value of those rights at each reporting date. For purposes of measuring impairment, the rights are stratified based upon the product type, term and interest rates. Fair value is determined by discounting estimated net future cash flows from mortgage servicing activities using discount rates that approximate current market rates and estimated prepayment rates, among other assumptions. The amount of impairment recognized, if any, is the amount by which the capitalized mortgage servicing rights for a stratum exceeds their fair value. Impairment, if any, is recognized through a valuation allowance for each individual stratum. Changes in the carrying amount of mortgage servicing rights are reported in earnings under Other income.

At March 31, 2013, the Company had $3,831,000 of mortgage loans held-for-sale. At March 31, 2013 and December 31, 2012, the Company serviced real estate mortgage loans for others of $242,863,000 and $235,561,000, respectively.

The following table summarizes the Company’s mortgage servicing rights assets as of March 31, 2013 and December 31, 2012. Mortgage servicing rights are included in Interest Receivable and Other Assets in the consolidated balance sheets.

	(in thousands)			
	December 31, 2012	Additions	Reductions	March 31, 2013
Mortgage servicing rights	$1,760	$201	$135	$1,826
Valuation allowance	(536)	—	(148)	(388)
Mortgage servicing rights, net of valuation allowance	$1,224	$201	$(13)	$1,438

The Company received contractually specified servicing fees of $152,000 and $135,000 for the three month periods ended March 31, 2013 and March 31, 2012, respectively. Contractually specified servicing fees are included in Other Income on the consolidated statements of income.

4. OUTSTANDING SHARES AND EARNINGS PER SHARE

On January 24, 2013, the Board of Directors of the Company declared a 2% stock dividend payable as of March 29, 2013. All income per share amounts have been adjusted to give retroactive effect to stock dividends.

Earnings Per Share (EPS)

Basic EPS includes no dilution and is computed by dividing net income available to common shareholders by the weighted average number of common shares outstanding for the period. Diluted EPS includes all common stock equivalents ("in-the-money" stock options, unvested restricted stock, stock units, warrants and rights, convertible bonds and preferred stock), which reflects the potential dilution of securities that could share in the earnings of an entity.

The following table presents a reconciliation of basic and diluted EPS for the three-month periods ended March 31, 2013 and 2012.

	Three months ended March 31,	
	2013	2012
Basic earnings per share:		
Net income	$1,363	$1,092
Preferred stock dividend	$(212)	$(285)
Net income available to common stockholders	$1,151	$807
Weighted average common shares outstanding	9,405,851	9,377,213
Basic EPS	$0.12	$0.09
Diluted earnings per share:		
Net income	$1,363	$1,092
Preferred stock dividend	$(212)	$(285)
Net income available to common stockholders	$1,151	$807
Weighted average common shares outstanding	9,405,851	9,377,213
Effect of dilutive shares	30,718	26,968
Adjusted weighted average common shares outstanding	9,436,569	9,404,181
Diluted EPS	$0.12	$0.09

Stock options which were not included in the computation of diluted earnings per share because they would have had an anti-dilutive effect amounted to 321,994 shares and 349,770 shares for the three-month periods ended March 31, 2013 and 2012, respectively. Non-vested shares of restricted stock not included in the computation of diluted earnings per share because they would have an anti-dilutive effect amounted to 8,398 shares and 21,589 for the three-month periods ended March 31, 2013 and 2012, respectively.

5. STOCK PLANS

On January 24, 2013, the Board of Directors of the Company declared a 2% stock dividend payable as of March 29, 2013. All stock options and restricted stock outstanding have been adjusted to give retroactive effect to stock dividends.

The following table presents the activity related to stock options for the three months ended March 31, 2013.

	Number of Shares	Weighted Average Exercise Price	Aggregate Intrinsic Value	Weighted Average Remaining Contractual Term (in years)
Options outstanding at Beginning of Period	383,045	$11.71		
Granted	22,950	$5.88		
Expired	(48,502)	$7.74		
Cancelled / Forfeited	—	—		
Exercised	—	—		
Options outstanding at End of Period	357,493	$11.87	$72,484	3.48
Exercisable (vested) at End of Period	311,503	$12.84	$46,223	2.66

The weighted average grant date fair value per share of options granted during the three-month period ended March 31, 2013 was $2.75 per share.

As of March 31, 2013, there was $110,000 of total unrecognized compensation cost related to non-vested stock options. This cost is expected to be recognized over a weighted average period of approximately 3.18 years.

There was $10,000 of recognized compensation cost related to stock options granted for the three months ended March 31, 2013.

A summary of the weighted average assumptions used in valuing stock options during the three months ended March 31, 2013 is presented below.

	Three Months Ended March 31, 2013

Risk Free Interest Rate	0.86	%
Expected Dividend Yield	0.00	%
Expected Life in Years	5	
Expected Price Volatility	54.36	%

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The following table presents the activity related to non-vested restricted stock for the three months ended March 31, 2013.

	Number of Shares	Weighted Average Exercise Price	Aggregate Intrinsic Value	Weighted Average Remaining Contractual Term (in years)
Restricted stock outstanding at Beginning of Period	47,707	$ 4.53		
Granted	19,380	$ 5.88		
Cancelled / Forfeited	—	—		
Exercised/Released/Vested	(8,805)	$ 4.37		
Restricted stock oustanding at End of Period	58,282	$ 5.00	$ 338,036	8.61

The weighted average fair value of restricted stock granted during the three month period ended March 31, 2013 was $5.88 per share.

As of March 31, 2013, there was $201,000 of total unrecognized compensation cost related to non-vested restricted stock. This cost is expected to be recognized over a weighted average period of approximately 3.11 years.

There was $18,000 of recognized compensation cost related to restricted stock awards for the three months ended March 31, 2013.

The Company has an Employee Stock Purchase Plan ("ESPP"). Under the ESPP, the Company is authorized to issue to eligible employees shares of common stock. There are 300,958 (adjusted for the 2013 stock dividend) shares authorized under the ESPP. The ESPP will terminate March 15, 2016. The ESPP is implemented by participation periods of not more than twenty-seven months each. The Board of Directors determines the commencement date and duration of each participation period. The Board of Directors approved the current participation period of November 24, 2012 to November 23, 2013. An eligible employee is one who has been continually employed for at least 90 days prior to commencement of a participation period. Under the terms of the ESPP, employees can choose to have up to 10 percent of their compensation withheld to purchase the Company's common stock each participation period. The purchase price of the stock is 85 percent of the lower of the fair market value on the last trading day before the date of participation or the fair market value on the last trading day during the participation period.

As of March 31, 2013, there was $18,000 of unrecognized compensation cost related to ESPP issuances. This cost is expected to be recognized over a weighted average period of approximately 0.75 years.

There was $12,000 of recognized compensation cost related to ESPP issuances for the three-month period ended March 31, 2013.

The weighted average fair value at issuance date during the three-month period ended March 31, 2013 was $1.04.

A summary of the weighted average assumptions used in valuing ESPP issuances during the three months ended March 31, 2013 is presented below.

	Three Months Ended March 31, 2013	
Risk Free Interest Rate	0.19	%
Expected Dividend Yield	0.00	%
Expected Life in Years	1.00	
Expected Price Volatility	20.00	%

6. FAIR VALUE MEASUREMENT

The Company utilizes fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. Securities available-for-sale and trading securities are recorded at fair value on a recurring basis. Additionally, from time to time, the Company may be required to record at fair value other assets on a non-recurring basis, such as loans held-for-sale, loans held-for-investment and certain other assets. These non-recurring fair value adjustments typically involve application of lower of cost or market accounting or write-downs of individual assets. Transfers between levels of the fair value hierarchy are recognized on the actual date of the event or circumstances that caused the transfer, which generally corresponds with the Company's quarterly valuation process.

Fair Value Hierarchy
The Company groups assets and liabilities at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. These levels are:

Level 1 Valuation is based upon quoted prices for identical instruments traded in active markets.

Level 2 Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active and model-based valuation techniques for which all significant assumptions are observable or can be corroborated by observable market data.

Level 3 Valuation is generated from model-based techniques that use at least one significant assumption not observable in the market. These unobservable assumptions reflect estimates of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include use of option pricing models, discounted cash flow models, and similar techniques and include management judgment and estimation which may be significant.

Following is a description of valuation methodologies used for assets and liabilities recorded at fair value.

Investment Securities Available-for-Sale

Investment securities available-for-sale are recorded at fair value on a recurring basis. Fair value measurement is based upon quoted market prices, if available. If quoted market prices are not available, fair values are measured using independent pricing models or other model-based valuation techniques such as the present value of future cash flows, adjusted for the security's credit rating, prepayment assumptions, and other factors such as credit loss assumptions. Level 1 securities include those traded on an active exchange, such as the New York Stock Exchange, U.S. Treasury securities that are traded by dealers or brokers in active over-the-counter markets and money market funds. Level 2 securities include mortgage-backed securities issued by government sponsored entities, municipal bonds and corporate debt securities. Securities classified as Level 3 include asset-backed securities in less liquid markets.

Loans Held-for-Sale

Loans held-for-sale are carried at the lower of cost or fair value. The fair value of loans held-for-sale is based on what secondary markets are currently offering for portfolios with similar characteristics. As such, the Company classifies loans subjected to non-recurring fair value adjustments as Level 2. At March 31, 2013 there were no loans

held-for-sale that required a write-down.

Impaired Loans

The Company does not record loans at fair value on a recurring basis. However, from time to time, a loan is considered impaired and an allowance for loan losses is established. Loans for which it is probable that payment of interest and principal will not be made in accordance with the contractual terms of the loan agreement are considered impaired. Once a loan is identified as individually impaired, the Company measures impairment. The fair value of impaired loans is estimated using one of several methods, including collateral value, market value of similar debt, enterprise value, liquidation value and discounted cash flows. Those impaired loans not requiring an allowance represent loans for which the fair value of the expected repayments or collateral exceed the recorded investments in such loans.

At March 31, 2013, certain impaired loans were considered collateral dependent and were evaluated based on the fair value of the underlying collateral securing the loan. Impaired loans where an allowance is established based on the fair value of collateral require classification in the fair value hierarchy. When a loan is evaluated based on the fair value of the underlying collateral securing the loan, the Company records the impaired loan as non-recurring Level 3.

Other Real Estate Owned

Other real estate assets ("OREO") acquired through, or in lieu of, foreclosure are held-for-sale and are initially recorded at the lower of cost or fair value, less selling costs. Any write-downs to fair value at the time of transfer to OREO are charged to the allowance for loan losses, subsequent to foreclosure. Appraisals or evaluations are then done periodically thereafter charging any additional write-downs or valuation allowances to the appropriate expense accounts. Values are derived from appraisals of underlying collateral and discounted cash flow analysis. OREO is classified within Level 3 of the hierarchy.

Loan Servicing Rights

Loan servicing rights are subject to impairment testing. The Company utilizes a third party service provider to calculate the fair value of the Company's loan servicing rights. Loan servicing rights are measured at fair value as of the date of sale. The Company uses quoted market prices when available. Subsequent fair value measurements are determined using a discounted cash flow model. In order to determine the fair value of the loan servicing rights, the present value of expected future cash flows is estimated. Assumptions used include market discount rates, anticipated prepayment speeds, delinquency and foreclosure rates, and ancillary fee income. This model is periodically validated by an independent external model validation group. The model assumptions and the loan servicing rights fair value estimates are also compared to observable trades of similar portfolios as well as to loan servicing rights broker valuations and industry surveys, as available. If the valuation model reflects a value less than the carrying value, loan servicing rights are adjusted to fair value through a valuation allowance as determined by the model. As such, the Company classifies loan servicing rights subjected to non-recurring fair value adjustments as Level 3.

Assets Recorded at Fair Value on a Recurring Basis

The table below presents the recorded amount of assets and liabilities measured at fair value on a recurring basis as of March 31, 2013.

	(in thousands)			
March 31, 2013	Total	Level 1	Level 2	Level 3
U.S. Treasury securities	$1,004	$1,004	$—	$—
Securities of U.S. government agencies and corporations	50,964	—	50,964	—
Obligations of states and political subdivisions	29,162	—	29,162	—
Collateralized mortgage obligations	7,368	—	7,368	
Mortgage-backed securities	113,363	—	113,363	—
Total investments at fair value	$201,861	$1,004	$200,857	$—

The table below presents the recorded amount of assets and liabilities measured at fair value on a recurring basis as of December 31, 2012.

	(in thousands)			
December 31, 2012	Total	Level 1	Level 2	Level 3
U.S. Treasury securities	$1,005	$1,005	$—	$—
Securities of U.S. government agencies and corporations	28,305	—	28,305	—
Obligations of states and political subdivisions	28,786	—	28,786	—
Collateralized mortgage obligations	8,278	—	8,278	
Mortgage-backed securities	118,117	—	118,117	—
Total investments at fair value	$184,491	$1,005	$183,486	$—

Assets Recorded at Fair Value on a Non-Recurring Basis

Assets measured at fair value on a non-recurring basis are included in the table below by level within the fair value hierarchy as of March 31, 2013.

	(in thousands)			
March 31, 2013	Total	Level 1	Level 2	Level 3
Impaired loans	$121	$—	$—	$121
Other real estate owned	1,062	—	—	1,062
Loan servicing rights	1,438	—	—	1,438
Total assets at fair value	$2,621	$—	$—	$2,621

Assets measured at fair value on a non-recurring basis are included in the table below by level within the fair value hierarchy as of December 31, 2012.

	(in thousands)			
December 31, 2012	Total	Level 1	Level 2	Level 3
Impaired loans	$2,513	$—	$—	$2,513
Other real estate owned	1,062	—	—	1,062
Loan servicing rights	1,224	—	—	1,224
Total assets at fair value	$4,799	$—	$—	$4,799

There were no liabilities measured at fair value on a recurring or non-recurring basis at March 31, 2013 and December 31, 2012.

7. PREFERRED STOCK

On September 15, 2011, the Company issued to the U.S. Treasury under the United States Department of Treasury Small Business Lending Fund (SBLF) 22,847 shares of the Company's Non-Cumulative Perpetual Preferred Stock, Series A (SBLF Shares), having a liquidation preference per share equal to $1,000, for an aggregate purchase price of $22,847,000.

On September 15, 2011, the Company redeemed from the U.S. Treasury, using the partial proceeds from the issuance of the SBLF Shares, all 17,390 outstanding shares of its Fixed Rate Cumulative Perpetual Preferred Stock, Series A, liquidation amount $1,000 per share, for a redemption price of $17,390,000, plus accrued but unpaid dividends at the date of redemption.

On February 8, 2013, the Company redeemed $10,000,000 of the $22,847,000 in preferred stock it issued to the U.S. Treasury under the SBLF program.

8. FAIR VALUES OF FINANCIAL INSTRUMENTS

The following methods and assumptions were used by the Company in estimating its fair value disclosures for financial instruments:

Cash and Cash Equivalents

The carrying amounts reported in the balance sheet for cash and short-term instruments are a reasonable estimate of fair value. The carrying amount is a reasonable estimate of fair value because of the relatively short term between the origination of the instrument and its expected realization. Therefore, the Company believes the measurement of fair value of cash and cash equivalents is derived from Level 1 inputs.

Other Equity Securities

The carrying amounts reported in the balance sheet approximate fair value. The Company believes the measurement of the fair value of other equity securities is derived from Level 2 inputs.

Loans Receivable

For variable-rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying values. The fair values for other loans (e.g., commercial real estate and rental property mortgage loans, commercial and industrial loans, and agricultural loans) are estimated using discounted cash flow analyses, using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality. The allowance for loan losses is considered to be a reasonable estimate of loan discount due to credit risks. Given that there are loans with specific terms that are not readily available, the Company believes the fair value of loans receivable is derived from Level 3 inputs.

Loans Held-for-Sale

For loans held for sale, carrying value approximates fair value. See FN(6), Fair Value Measurement.

Interest receivable and payable

The carrying amount of interest receivable and payable approximates its fair value. The Company believes the measurement of the fair value of interest receivable and payable is derived from Level 3 inputs.

Deposit Liabilities

The Company measures fair value of deposits using Level 2 and Level 3 inputs. The fair value of deposits were derived by discounting their expected future cash flows back to their present values based on the FHLB yield curve, and their expected decay rates for non maturing deposits. The Company is able to obtain FHLB yield curve rates as of the measurement date, and believes these inputs fall under Level 2 of the fair value hierarchy. Decay rates were developed through internal analysis, and are supported by recent years of the Bank's transaction history. The inputs used by the Company to derive the decay rate assumptions are unobservable inputs, and therefore fall under Level 3 of the fair value hierarchy.

FHLB Advances and Other Borrowings

The fair values of borrowed funds were estimated by discounting future cash flows related to these financial instruments using current market rates for financial instruments with similar characteristics. The Company believes the measurement of the fair value of FHLB advances and other borrowings is derived from Level 2 inputs.

Limitations

Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial instrument. These estimates do not reflect any premium or discount that could result from offering for sale at one time the Company's entire holdings of a particular financial instrument. Because no market exists for a significant portion of the Company's financial instruments, fair value estimates are based on judgments regarding future expected loss experience, current economic conditions, risk characteristics of various financial instruments, and other factors. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

Fair value estimates are based on existing on-and off-balance sheet financial instruments without attempting to estimate the value of anticipated future business and the value of assets and liabilities that are not considered financial instruments. Other significant assets and liabilities that are not considered financial assets or liabilities include deferred tax liabilities and premises and equipment. In addition, the tax ramifications related to the realization of the unrealized gains and losses can have a significant effect on fair value estimates and have not been considered in many of the estimates.

The estimated fair values of the Company's financial instruments for the periods ended March 31, 2013 and December 31, 2012 are approximately as follows:

		March 31, 2013		December 31, 2012	
	Level	Carrying amount	Fair value	Carrying amount	Fair value
Financial assets:					
Cash and cash equivalents	1	$166,114	$166,114	$161,359	$161,359
Other equity securities	2	3,607	3,607	3,607	3,607
Loans receivable:					
Net loans	3	439,635	437,052	440,449	437,818
Loans held-for-sale	2	3,831	3,920	4,559	4,704
Interest receivable	3	2,723	2,723	2,542	2,542
Financial liabilities:					
Deposits	3	761,710	749,299	730,811	720,690
Interest payable	3	94	94	94	94

9. INVESTMENT SECURITIES

The amortized cost, unrealized gains and losses and estimated fair values of investments in debt and other securities at March 31, 2013 are summarized as follows:

(in thousands)	Amortized cost	Unrealized gains	Unrealized losses	Estimated fair value
Investment securities available-for-sale:				
U.S. Treasury securities	$998	$6	$—	$1,004
Securities of U.S. government agencies and corporations	50,992	92	(120)	50,964
Obligations of states and political subdivisions	27,876	1,309	(23)	29,162
Collateralized mortgage obligations	7,405	1	(38)	7,368
Mortgage-backed securities	111,804	1,656	(97)	113,363
Total debt securities	$199,075	$3,064	$(278)	$201,861

The amortized cost, unrealized gains and losses and estimated fair values of investments in debt and other securities at December 31, 2012 are summarized as follows:

(in thousands)	Amortized cost	Unrealized gains	Unrealized losses	Estimated fair value
Investment securities available-for-sale:				
U.S. Treasury securities	$997	$8	$—	$1,005
Securities of U.S. government agencies and corporations	28,200	105	——––	28,305
Obligations of states and political subdivisions	27,226	1,563	(3)	28,786
Collateralized mortgage obligations	8,156	123	(1)	8,278
Mortgage-backed securities	116,855	1,524	(262)	118,117
Total debt securities	$181,434	$3,323	$(266)	$184,491

There were no proceeds from sales of available-for-sale securities for the three-month periods ended March 31, 2013 and March 31, 2012. Gross realized gains from calls of available-for-sale securities were $4 and $1 for the three-month periods ended March 31, 2013 and March 31, 2012 respectively.

The amortized cost and estimated market value of debt and other securities at March 31, 2013, by contractual and expected maturity, are shown in the following table.

(in thousands)	Amortized cost	Estimated fair value
Due in one year or less	$22,430	$22,493
Due after one year through five years	124,873	126,440
Due after five years through ten years	43,758	44,481
Due after ten years	8,014	8,447
	$199,075	$201,861

Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. Securities due after one year through five years included mortgage-backed securities with expected maturities totaling $104,453,000. The maturities on these securities were based on the average lives of the securities.

An analysis of gross unrealized losses of the available-for-sale investment securities portfolio as of March 31, 2013, follows:

	Less than 12 months		12 months or more		Total	
(in thousands)	Fair Value	Unrealized losses	Fair Value	Unrealized losses	Fair Value	Unrealized losses
Securities of U.S. government agencies and corporations	$28,684	$(120)	$—	$—	$28,684	$(120)
Obligations of states and political subdivisions	2,286	(23)	—	—	2,286	(23)
Collateralized mortgage obligations	6,336	(38)	—	—	6,336	(38)
Mortgaged-backed securities	18,383	(97)	—	—	18,383	(97)
Total	$55,689	$(278)	$—	$—	$55,689	$(278)

No decline in value was considered “other-than-temporary” during 2013. Thirty-five securities that had a fair value of $55,689,000 and a total unrealized loss of $278,000 have been in an unrealized loss position for less than twelve months as of March 31, 2013. The declines in fair value were primarily attributable to changes in interest rates. As the Company does not intend to sell these securities and it is not more likely than not that the Company will be required to sell these securities prior to their anticipated recovery, these investments are not considered other-than-temporarily impaired.

An analysis of gross unrealized losses of the available-for-sale investment securities portfolio as of December 31, 2012, follows:

	Less than 12 months		12 months or more		Total	
(in thousands)	Fair Value	Unrealized losses	Fair Value	Unrealized losses	Fair Value	Unrealized losses
Obligations of states and political subdivisions	$1,262	$(3)	$—	$—	$1,262	$(3)
Collateralized mortgage obligations	1,198	(1)	—	—	1,198	(1)
Mortgage-backed securities	29,779	(262)	—	—	29,779	(262)
Total	$32,239	$(266)	$—	$—	$32,239	$(266)

Investment securities carried at $30,337,000 and $32,227,000 at March 31, 2013 and December 31, 2012, respectively, were pledged to secure public deposits or for other purposes as required or permitted by law.

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10. ACCUMULATED OTHER COMPREHENSIVE INCOME

The following table details activity in accumulated other comprehensive income for the three-month period ended March 31, 2013.

($ in thousands)	Unrealized Gains on Securities	Directors' and officers' retirement plans	Accumulated Other Comprehensive Income
Balance as of December 31, 2012	$1,834	$(660)	$ 1,174
Current period other comprehensive loss	(163)	—	(163)
Balance as of March 31, 2013	$1,671	$(660)	$ 1,011

The following table details activity in accumulated other comprehensive income for the three-month period ended March 31, 2012.

($ in thousands)	Unrealized Gains on Securities	Directors' and officers' retirement plans	Accumulated Other Comprehensive Income
Balance as of December 31, 2011	$758	$(495)	$ 263
Current period other comprehensive income	586	—	586
Balance as of March 31, 2012	$1,344	$(495)	$ 849

11. FINANCIAL INSTRUMENTS WITH OFF-BALANCE SHEET RISK

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

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

Financial instruments, whose contract amounts represent credit risk at the indicated periods, were as follows:

(in thousands)	March 31, 2013	December 31, 2012
Undisbursed loan commitments	$168,107	$159,329
Standby letters of credit	2,441	2,376
Commitments to sell loans	2,450	7,480
	$172,998	$169,185

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 generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Bank evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Bank upon extension of credit, is based on management's credit evaluation. Collateral held varies but may include accounts receivable, inventory, property, plant and equipment, and income-producing commercial properties.

Standby letters of credit are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. The Bank issues both financial and performance standby letters of credit. The financial standby letters of credit are primarily to guarantee payment to third parties. At March 31, 2013, there were no financial standby letters of credit outstanding. The performance standby letters of credit are typically issued to municipalities as specific performance bonds. At March 31, 2013, there was $2,441,000 issued in performance standby letters of credit and the Bank carried no liability. The terms of the guarantees will expire primarily in 2013. The Bank has experienced no draws on these letters of credit, and does not expect to in the future; however, should a triggering event occur, the Bank either has collateral in excess of the letter of credit or imbedded agreements of recourse from the customer. The Bank has set aside a reserve for unfunded commitments in the amount of $793,000 at March 31, 2013, which is recorded in "interest payable and other liabilities."

Commitments to extend credit and standby letters of credit bear similar credit risk characteristics as outstanding loans. As of March 31, 2013, the Company has no off-balance sheet derivatives requiring additional disclosure.

Mortgage loans sold to investors may be sold with servicing rights retained, for which the Company makes only standard legal representations and warranties as to meeting certain underwriting and collateral documentation

standards. In the past two years, the Company has had to repurchase no loans due to deficiencies in underwriting or loan documentation. Management believes that any liabilities that may result from such recourse provisions are not significant.

FIRST NORTHERN COMMUNITY BANCORP

ITEM 2. – MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

FORWARD-LOOKING STATEMENTS

This report includes forward-looking statements, which include forecasts of our financial results and condition, expectations for our operations and business, and our assumptions for those forecasts and expectations. Do not rely unduly on forward-looking statements. Actual results might differ significantly compared to our forecasts and expectations. See Part I, Item 1A. "Risk Factors," and the other risks described in our 2012 Annual Report on Form 10-K for factors to be considered when reading any forward-looking statements in this filing.
This report includes forward-looking statements, which are subject to the "safe harbor" created by section 27A of the Securities Act of 1933, as amended, and section 21E of the Securities Exchange Act of 1934, as amended. We may make forward-looking statements in our Securities and Exchange Commission (SEC) filings, press releases, news articles and when we are speaking on behalf of the Company. Forward-looking statements can be identified by the fact that they do not relate strictly to historical or current facts. Often, they include the words "believe," "expect," "target," "anticipate," "intend," "plan," "seek," "strive," "estimate," "potential," "project," or words of similar meaning, or future or co verbs such as "will," "would," "should," "could," "might," or "may." These forward-looking statements are intended to pro investors with additional information with which they may assess our future potential. All of these forward-looking statements are based on assumptions about an uncertain future and are based on information available to us at the date of these statements. We do not undertake to update forward-looking statements to reflect facts, circumstances, assumptions or events that occur after the date the forward-looking statements are made.
In this document and in other SEC filings, for example we make forward-looking statements relating to the following topics:

- Our business objectives, strategies and initiatives, our organizational structure, the growth of our business and our competitive position
- Our assessment of significant factors and developments that have affected or may affect our results
- Pending and recent legal and regulatory actions, and future legislative and regulatory developments, including the effects of the Dodd-Frank Wall Street Reform and Protection Act (the "Dodd-Frank Act") and other legislation and governmental measures introduced in response to the financial crises affecting the banking system, financial markets and the U.S. economy
- Regulatory controls and processes and their impact on our business
- The costs and effects of legal or regulatory actions
- We do not expect draws on performance letters of credit
- Our regulatory capital requirements
- We do not anticipate paying a cash dividend in the foreseeable future
- Credit quality and provision for credit losses
-

Our allowances for credit losses, including the conditions we consider in determining the unallocated allowance and our portfolio credit quality, underwriting standards, and risk grade

- Our assessment of economic conditions and trends and credit cycles and their impact on our business

- The seasonal nature of our business

- The impact of changes in interest rates and our strategy to manage our interest rate risk profile
- Loan portfolio composition and risk grade trends, expected charge offs, delinquency rates and our underwriting standards
- Our deposit base including renewal of time deposits
- The impact on our net interest income and net interest margin from the current low-interest rate environment
- The Company does not anticipate any significant increase or decrease in unrecognized tax benefits
- Our pension and retirement plan costs
- Our liquidity position
- Critical accounting policies and estimates, the impact or anticipated impact of recent accounting pronouncements or change in accounting principles
- Expected rates of return, yields and projected results

There are numerous risks and uncertainties that could and will cause actual results to differ materially from those discussed in our forward-looking statements. Many of these factors are beyond our ability to control or predict and could have a material adverse effect on our financial condition and results of operations or prospects. Such risks and uncertainties include, but are not limited to those listed in Item 1A "Risk Factors" of Part II, Item 2 "Management's Discussion and Analysis of Financial Condition and Results of Operations" of Part I of this Form 10-Q and "Supervision and Regulation" of our 2012 Annual Report on Form 10-K.

INTRODUCTION

This overview of Management's Discussion and Analysis highlights selected information in this report and may not contain all of the information that is important to you. For a more complete understanding of trends, events, commitments, uncertainties, liquidity, capital resources and critical accounting estimates, you should carefully read this entire report, together with our Consolidated Financial Statements and the Notes to Consolidated Financial Statements included in our Annual Report on Form 10-K for the year ended December 31, 2012.

Our subsidiary, First Northern Bank of Dixon (the "Bank"), is a California state-chartered bank that derives most of its revenues from lending and deposit taking in the Sacramento Valley region of Northern California. Interest rates, business conditions and customer confidence all affect our ability to generate revenues. In addition, the regulatory environment and competition can present challenges to our ability to generate those revenues.

Significant results and developments during the first quarter of 2013 include:

• Net income of $1.4 million for the three months ended March 31, 2013, up 27.3% from the $1.1 million for the same fiscal period last year.

• Net income available to common stockholders of $1.2 million for the three months ended March 31, 2013, up 50.0% from the $0.8 million for the same fiscal period last year.

• Diluted income per share for the three-month period ended March 31, 2013 was $0.12, up 33.3% from the diluted income per share of $0.09 reported in the same period last year.

• Net interest income increased in the three months ended March 31, 2013 by $142,000, or 2.2%, to $6.535 million from $6.393 million in the same period last year. The increase in net interest income was primarily attributable to a decrease in interest costs, partially offset by a decrease in interest yields. The decrease in interest costs is primarily attributable to a decrease in the Company's average cost of funds, partially offset by an increase in average loans. Net interest margin decreased from 3.51% for the three-month period ending March 31, 2013 to 3.36% for the same period ending March 31, 2013.

• Provision for loan losses of $0.40 million for the three-month period ended March 31, 2013 compared to a provision for loan losses of $0.55 million for the same period in 2012.

• Total assets at March 31, 2013 were $852.6 million, an increase of $21.1 million, or 2.5%, from levels at December 31, 2012.

• Total net loans at March 31, 2013 (including loans held-for-sale) decreased $1.5 million, or 0.4%, to $443.5 million compared to December 31, 2012.

• Total investment securities at March 31, 2013 increased $17.4 million, or 9.4%, to $201.9 million compared to December 31, 2012.

• Total deposits of $761.7 million at March 31, 2013, represented an increase of $30.9 million, or 4.2%, compared to December 31, 2012.

SUMMARY

The Company recorded net income of $1,363,000 for the three-month period ended March 31, 2013, representing an increase of $271,000 from net income of $1,092,000 for the same period in 2012.

The following tables present a summary of the results for the three-month periods ended March 31, 2013 and 2012, and a summary of financial condition at March 31, 2013 and December 31, 2012.

	Three months ended March 31, 2013	Three months ended March 31, 2012
(in thousands except for per share amounts)		
For the Period:		
Net Income	$1,363	$1,092
Basic Earnings Per Common Share	$0.12	$0.09
Diluted Earnings Per Common Share	$0.12	$0.09

	March 31, 2013	December 31, 2012
(in thousands except for ratios)		
At Period End:		
Total Assets	$852,560	$831,483
Total Loans, Net (including loans held-for-sale)	$443,466	$445,008
Total Investment Securities	$201,861	$184,491
Total Deposits	$761,710	$730,811
Loan-To-Deposit Ratio	58.2 %	60.9 %

FIRST NORTHERN COMMUNITY BANCORP

Distribution of Average Statements of Condition and Analysis of Net Interest Income
(in thousands, except percentage amounts)

	Three months ended March 31, 2013				Three months ended March 31, 2012			
	Average Balance	Interest	Yield/ Rate		Average Balance	Interest	Yield/ Rate	
Assets								
Interest-earning assets:								
Loans (1)	$437,855	$5,971	5.53	%	$421,994	$5,990	5.69	%
Interest bearing due from banks	153,600	105	0.28	%	130,984	79	0.24	%
Investment securities, taxable	182,970	693	1.54	%	164,131	780	1.91	%
Investment securities, non-taxable (2)	10,180	100	3.98	%	10,518	104	3.97	%
Other interest earning assets	3,607	—	—	%	3,075	4	0.52	%
Total average interest-earning assets	788,212	6,869	3.53	%	730,702	6,957	3.82	%
Non-interest-earning assets:								
Cash and due from banks	16,573				16,454			
Premises and equipment, net	7,799				8,084			
Other real estate owned	1,062				1,345			
Interest receivable and other assets	28,593				32,045			
Total average assets	842,239				788,630			
Liabilities and Stockholders' Equity:								
Interest-bearing liabilities:								
Interest-bearing transaction deposits	189,271	64	0.14	%	161,173	90	0.22	%
Savings and MMDA's	226,320	158	0.28	%	218,090	195	0.36	%
Time, under $100,000	35,323	39	0.45	%	38,045	54	0.57	%
Time, $100,000 and over	55,858	73	0.53	%	67,692	153	0.91	%
FHLB advances and other borrowings	—	—	—	%	7,000	72	4.13	%
Total average interest-bearing liabilities	506,772	334	0.27	%	492,000	564	0.46	%
Non-interest-bearing liabilities:								
Non-interest-bearing demand deposits	240,129				200,854			
Interest payable and other liabilities	7,757				6,947			
Total liabilities	754,658				699,801			
Total average stockholders' equity	87,581				88,829			
Total average liabilities and stockholders' equity	$842,239				$788,630			
		$6,535	3.36	%		$6,393	3.51	%

Net interest income and net
interest margin (3)

1. Average balances for loans include loans held-for-sale and non-accrual loans and are net of the allowance for loan losses, but non-accrued interest thereon is excluded. Loan interest income includes loan fees of approxiamtely $278 and $197 for the three months ended March 31, 2013 and 2012, respectively.
2. Interest income and yields on tax-exempt securities are not presented on a taxable equivalent basis.
3. Net interest margin is computed by dividing net interest income by total average interest-earning assets.

CHANGES IN FINANCIAL CONDITION

The assets of the Company set forth in the Unaudited Condensed Consolidated Balance Sheets reflect a $4,755,000 increase in cash and cash equivalents, a $17,370,000 increase in investment securities available-for-sale, an $814,000 decrease in net loans held-for-investment, a $728,000 decrease in loans held-for-sale, and a $591,000 increase in interest receivable and other assets from December 31, 2012 to March 31, 2013. The increase in cash and cash equivalents was due to an increase in interest bearing due from bank accounts and non-interest bearing due from bank accounts. The increase in investment securities available-for-sale was primarily the result of purchases of municipal bonds, agency bonds, and mortgage backed securities, partially offset by calls of agency and municipal bonds and amortization on mortgage backed securities. The decrease in loans held-for-investment was due to decreases in the following loan categories as a result of decreased loan demand: agricultural; true equipment leases; consumer; home equity lines. The decrease in loans held-for-investment was partially offset by increases in the following loan categories: commercial and industrial; equipment; financed equipment leases; real estate; real estate commercial and construction. The decrease in loans held-for-sale was due to timing of sales of loans held-for-sale. The increase in interest receivable and other assets was mainly due to increases in accrued income on securities, accrued income on loans, prepaid expenses, cash surrender value of bank owned life insurance, unamortized loan costs and mortgage servicing asset, which was partially offset by decreases in income taxes receivable, housing tax credits, sold loan settlement and suspense & holdovers.

The liabilities of the Company set forth in the Unaudited Condensed Consolidated Balance Sheets reflect an increase in total deposits of $30,899,000 from December 31, 2012 to March 31, 2013. The increase in deposits was due to increases in demand deposits, interest-bearing transaction deposits, and savings accounts, which was partially offset by decreases in money market accounts and time deposits.

CHANGES IN RESULTS OF OPERATIONS

Interest Income

The Federal Open Market Committee made no changes to the Federal Funds rate during the twelve-month period ended March 31, 2013.

Interest income on loans for the three-month period ended March 31, 2013 was down 0.3% from the same period in 2012, decreasing from $5,990,000 to $5,971,000. The decrease in interest income on loans for the three-month period ended March 31, 2013 as compared to the same period a year ago was primarily due to a 16 basis point decrease in loan yields, partially offset by an increase in average loans. The decrease in loan yields was primarily due to repricing of loans at lower rates.

Interest income on investment securities available-for-sale for the three-month period ended March 31, 2013 was down 10.3% from the same period in 2012, decreasing from $884,000 to $793,000. The decrease in interest income on investment securities for the three-month period ended March 31, 2013 as compared to the same period a year ago was primarily due to a 38 basis point decrease in investment securities yields, partially offset by an increase in average investment securities. The decrease in investment securities yields was primarily due to reinvestment of maturing securities at lower rates and purchases of securities at lower rates.

Interest income on interest-bearing due from banks for the three-month period ended March 31, 2013 was up 32.9% from the same period in 2012, increasing from $79,000 to $105,000. The increase in interest income on interest-bearing due from banks for the three-month period ended March 31, 2013 as compared to the same period a year ago was primarily due to a 4 basis point increase in interest bearing due from banks yield combined with an increase in average interest-bearing due from banks.

The Company had no Federal Funds sold balances during the three-month periods ended March 31, 2013 and March 31, 2012.

Interest Expense

The sustained low interest rate environment decreased the Company’s cost of funds in the first three months of 2013 compared to the same period a year ago.

Interest expense on deposits and other borrowings for the three-month period ended March 31, 2013 was down 40.8% from the same period in 2012, decreasing from $564,000 to $334,000. The decrease in interest expense during the three-month period ended March 31, 2013 was due to a 19 basis point decrease in the Company’s average cost of funds, which was partially offset by an increase in average interest-bearing liabilities. The Company had no FHLB advances and related interest expense during the three-month period ended March 31, 2013. Included in interest expense on deposits and other borrowings for the three-month period ended March 31, 2012 is $72,000 in expense on FHLB advances of $7,000,000. The decrease in average cost of funds for the three-month period ended March 31, 2013 is primarily due to the maturing and repricing of time deposits and a change in the mix of interest-bearing liabilities, which resulted in an increase in lower cost deposits.

Provision for Loan Losses

There was a provision for loan losses of $400,000 for the three-month period ended March 31, 2013 compared to a provision for loan losses of $550,000 for the same period in 2012. The allowance for loan losses was approximately $8,846,000, or 1.98% of total loans, at March 31, 2013 compared to $8,554,000, or 1.91% of total loans, at December 31, 2012. The allowance for loan losses is maintained at a level considered adequate by management to provide for probable loan losses inherent in the loan portfolio.

The decrease in the provision for loan losses during the three-month period in 2013 was primarily due to decreased net charge-offs, partially offset by increased loan volumes compared to the three-month period in 2012.

Provision for Unfunded Lending Commitment Losses

There was no provision for unfunded lending commitment losses for the three-month periods ended March 31, 2013 and March 31, 2012.

The provision for unfunded lending commitment losses is included in non-interest expense.

Other Operating Income

Other operating income was up 23.3% for the three-month period ended March 31, 2013 from the same period in 2012, increasing from $2,125,000 to $2,621,000.

This increase was primarily due to increases in gains on sales of loans held-for-sale, investment and brokerage services income, loan servicing income, fiduciary activities income, and signature based transaction fees, which was partially offset by a decrease in ATM fees. The increase in gains on sales of loans held-for-sale was due to increased sales volume of loans held-for-sale. The increase in in investment and brokerage services income and fiduciary activities income was primarily due to an increase in the demand for those services. The increase in loan servicing income was primarily due to an increase in mortgage servicing assets booked and the reversal of mortgage servicing impairment expense. The increase in signature based transaction fees was primarily due to an increase in the volume of transactions. The decrease in ATM fees was primarily due to a decrease in the volume of transactions.

Other Operating Expenses

Total other operating expenses were up 4.0% for the three-month period ended March 31, 2013 from the same period in 2012, increasing from $6,492,000 to $6,754,000.

The increase was primarily due to increases in salaries and employee benefits, occupancy and equipment expense, and data processing, which was partially offset by decreases in advertising, other real estate owned expense and impairment, and other expenses. The increase in salaries and employee benefits was primarily due to increases in commissions, contingent compensation, and profit sharing expense, which was partially offset by a decrease in regular salaries. The increase in occupancy and equipment expense was primarily due to increases in building maintenance and service contracts. The increase in data processing was primarily due to increases in contract pricing. The decrease in advertising was due to decreases in printed materials and related costs. The decrease in other real estate owned expense and impairment was due to a decrease in write-downs and maintenance expense. The decrease in other expenses is primarily due to decreases in FDIC assessments, legal fees, telephone expense, loan origination expense, loan collection expense and sundry losses, which was partially offset by an increase in consulting fees.

The following table sets forth other miscellaneous operating expenses by category for the three-month periods ended March 31, 2013 and 2012.

	(in thousands)	
	Three months ended March 31, 2013	Three months ended March 31, 2012
Other miscellaneous operating expenses		
FDIC assessments	$149	$181
Contributions	18	20
Legal fees	25	80
Accounting and audit fees	78	65
Consulting fees	234	88
Postage expense	80	69
Telephone expense	29	57
Public relations	38	43
Training expense	39	25
Loan origination expense	111	161
Computer software depreciation	33	39
Sundry (reversals) losses	(9)	17
Loan collection expense	16	57
Other miscellaneous expense	346	355
Total other miscellaneous operating expenses	$1,187	$1,257

Income Taxes

The Company's tax rate, the Company's income or loss before taxes and the amount of tax relief provided by non-taxable earnings primarily affect the Company's provision for income taxes.

In the three months ended March 31, 2013, the Company's expense for income taxes increased $255,000 from the same period last year, from $384,000 to $639,000.

The increase in expense for income taxes for the period presented is primarily attributable to the respective level of earnings combined with the interim effective tax rate and the incidence of allowable deductions, in particular non-taxable municipal bond income, tax credits generated from low-income housing investments, solar tax credits, excludable interest income and, for California franchise taxes, higher excludable interest income on loans within designated enterprise zones.

Off-Balance Sheet Commitments

The following table shows the distribution of the Company's undisbursed loan commitments at the dates indicated.

	(in thousands)	
	March 31, 2013	December 31, 2012
Undisbursed loan commitments	$168,107	$159,329
Standby letters of credit	2,441	2,376
Commitments to sell loans	2,450	7,480
	$172,998	$169,185

The reserve for unfunded lending commitments amounted to $793,000 at March 31, 2013 and December 31, 2012, respectively. The reserve for unfunded lending commitments is included in other liabilities.

Asset Quality

The Company manages asset quality and credit risk by maintaining diversification in its loan portfolio and through review processes that include analysis of credit requests and ongoing examination of outstanding loans and delinquencies, with particular attention to portfolio dynamics and loan mix. The Company strives to identify loans experiencing difficulty early enough to correct the problems, to record charge-offs promptly based on realistic assessments of collectability and current collateral values and to maintain an adequate allowance for loan losses at all times. Asset quality reviews of loans and other non-performing assets are administered using credit risk rating standards and criteria similar to those employed by state and federal banking regulatory agencies. The federal bank and thrift regulatory agencies utilize the following definitions for assets adversely classified for supervisory purposes:

- Substandard Assets – A substandard asset is inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. Assets so classified must have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected.
- Doubtful Assets – An asset classified doubtful has all the weaknesses inherent in one classified substandard 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.

Other Real Estate Owned and loans rated Substandard and Doubtful are deemed "classified assets". This category, which includes both performing and non-performing assets, receives an elevated level of attention regarding collection.

The following tables summarize the Company's non-accrual loans net of guarantees of the State of California and U.S. Government by loan category at March 31, 2013 and December 31, 2012.

	At March 31, 2013			At December 31, 2012		
	Gross	Guaranteed	Net	Gross	Guaranteed	Net
(dollars in thousands)						
Residential mortgage	$1,940	$—	$1,940	$2,095	$—	$2,095
Residential construction	—	—	—	—	—	—
Commercial real estate	1,840	—	1,840	1,879	—	1,879
Agriculture	—	—	—	—	—	—
Commercial	2,747	46	2,701	2,853	73	2,780
Consumer	282	46	236	441	50	391
Total non-accrual loans	$6,809	$92	$6,717	$7,268	$123	$7,145

It is generally the Company's policy to discontinue interest accruals once a loan is past due for a period of 90 days as to interest or principal payments. When a loan is placed on non-accrual, interest accruals cease and uncollected accrued interest is reversed and charged against current income. Payments received on non-accrual loans are applied against principal. A loan may only be restored to an accruing basis when it again becomes well secured and in the process of collection or all past due amounts have been collected.

Non-accrual loans amounted to $6,809,000 at March 31, 2013 and were comprised of seven residential mortgage loans totaling $1,940,000, four commercial real estate loans totaling $1,840,000, nine commercial loans totaling $2,747,000 and five consumer loans totaling $282,000. Non-accrual loans amounted to $7,268,000 at December 31, 2012 and were comprised of seven residential mortgage loans totaling $2,095,000, five commercial real estate loans totaling $1,879,000, eleven commercial loans totaling $2,853,000 and seven consumer loans totaling $441,000. It is

generally the Company's policy to charge-off the portion of any non-accrual loan that the Company does not expect to collect by writing the loan down to the estimated net realizable value of the underlying collateral.

The five largest non-accrual loans as of March 31, 2013, totaled approximately $4,787,000 or 70% of total non-accrual loans and consisted of two commercial real estate loans totaling $1,645,000, supported by commercial properties located within the Company's market area, two residential mortgage loans totaling $1,428,000, supported by residential properties located within the Company's market area and one commercial and industrial loan totaling $1,714,000, supported by the business assets of the borrower. The collateral securing these loans is generally appraised every six months.

In comparison, the five largest non-accrual loans as of December 31, 2012, totaled approximately $4,889,000 or 67% of total non-accrual loans and consisted of two residential mortgage loan totaling $1,466,000, supported by residential property located within the Company's market area, two commercial real estate loans totaling $1,665,000, supported by commercial properties located within the Company's market area and one commercial and industrial loan totaling $1,758,000, supported by the business assets of the borrower.

Loans for which it is probable that payment of interest and principal will not be made in accordance with the contractual terms of the loan agreement are considered impaired. Non-performing impaired loans are non-accrual loans and loans that are 90 days or more past due and still accruing. Total non-performing impaired loans at March 31, 2013 and December 31, 2012 consisting of loans on non-accrual status totaled $6,809,000 and $7,268,000, respectively. A restructuring of a loan can constitute a troubled debt restructuring if the Company for economic or legal reasons related to the borrower's financial difficulties grants a concession to the borrower that it would not otherwise consider. A loan that is restructured in a troubled debt restructuring is considered an impaired loan. Performing impaired loans totaled $6,307,000 and $6,113,000 at March 31, 2013 and December 31, 2012, respectively. Performing impaired loans at March 31, 2013 consist of loans modified as troubled debt restructurings totaling $6,234,000 and other impaired loans totaling $73,000 which the Company expects to collect all principal and interest due and are performing satisfactorily. Additionally, these loans are not on non-accrual status. The majority of the non-performing impaired loans were in management's opinion adequately collateralized based on recently obtained appraised property values or guaranteed by a governmental entity. See "Allowance for Loan Losses" below for additional information. No assurance can be given that the existing or any additional collateral will be sufficient to secure full recovery of the obligations owed under these loans.

As the following table illustrates, total non-performing assets, net of guarantees of the State of California and U.S. Government, including its agencies and its government-sponsored agencies, decreased $428,000, or 5.2% to $7,779,000 during the first three months of 2013. Non-performing assets, net of guarantees, represent 0.9% of total assets at March 31, 2013.

	At March 31, 2013				At December 31, 2012			
(dollars in thousands)	Gross	Guaranteed	Net		Gross	Guaranteed	Net	
Non-accrual loans	$6,809	$92	$6,717		$7,268	$123	$7,145	
Loans 90 days past due and still accruing	—	—	—		—	—	—	
Total non-performing loans	6,809	92	6,717		7,268	123	7,145	
Other real estate owned	1,062	—	1,062		1,062	—	1,062	
Total non-performing assets	7,871	92	7,779		8,330	123	8,207	
Non-performing loans to total loans			1.5	%			1.6	%
Non-performing assets to total assets			0.9	%			1.0	%
Allowance for loan and lease losses to non-performing loans			131.7	%			119.7	%

The Company had no loans 90 days past due and still accruing at March 31, 2013 and December 31, 2012.

Other real estate owned (OREO) consists of property that the Company has acquired by deed in lieu of foreclosure or through foreclosure proceedings, and property that the Company does not hold title to but is in actual control of, known as in-substance foreclosure. The estimated fair value of the property is determined prior to transferring the balance to OREO. The balance transferred to OREO is the estimated fair value of the property less estimated cost to sell. Impairment may be deemed necessary to bring the book value of the loan equal to the appraised value. Appraisals or loan officer evaluations are then conducted periodically thereafter charging any additional impairment to the appropriate expense account.

OREO amounted to $1,062,000 as of March 31, 2013 and December 31, 2012, respectively.

Allowance for Loan Losses

The Company's Allowance for Loan Losses is maintained at a level believed by management to be adequate to provide for loan losses that can be reasonably anticipated. The allowance is increased by provisions charged to operating expense and reduced by net charge-offs. The Company contracts with vendors for credit reviews of the loan portfolio as well as considers current economic conditions, loan loss experience, and other factors in determining the adequacy of the reserve balance. The allowance for loan losses is based on estimates, and actual losses may vary from current estimates.

The following table summarizes the Allowance for Loan Losses of the Company during the three-month periods ended March 31, 2013 and 2012, and for the year ended December 31, 2012.

Analysis of the Allowance for Loan Losses
(Amounts in thousands, except percentage amounts)

	Three months ended March 31,		Year ended December 31,
	2013	2012	2012
Balance at beginning of period	$8,554	$10,408	$10,408
Provision for loan losses	400	550	3,276
Loans charged-off:			
Commercial	(111)	(542)	(3,498)
Commercial Real Estate	—	—	(375)
Agriculture	(1)	—	(116)
Residential mortgage	(78)	(31)	(864)
Residential construction	—	—	(167)
Consumer loans to individuals	(58)	(264)	(875)
Total charged-off	(248)	(837)	(5,895)
Recoveries:			
Commercial	75	206	306
Commercial Real Estate	1	—	—
Agriculture	3	2	4
Residential mortgage	—	—	—
Residential construction	41	1	341
Consumer loans to individuals	20	27	114
Total recoveries	140	236	765
Net charge-offs	(108)	(601)	(5,130)
Balance at end of period	$8,846	$10,357	$8,554
Ratio of net charge-offs to average loans outstanding during the period (annualized)	(0.10%)	(0.56%)	(1.18%)
Allowance for loan losses			

To total loans at the end of the period	1.98	%	2.43	%	1.91	%
To non-performing loans, net of guarantees at the end of the period	131.7	%	113.5	%	119.7	%

Deposits

Deposits are one of the Company's primary sources of funds. At March 31, 2013, the Company had the following deposit mix: 29.6% in savings and MMDA deposits, 12.0% in time deposits, 25.4% in interest-bearing transaction deposits and 33.0% in non-interest-bearing transaction deposits. At December 31, 2012, the Company had the following deposit mix: 30.5% in savings and MMDA deposits, 12.6% in time deposits, 25.3% in interest-bearing transaction deposits and 31.6% in non-interest-bearing transaction deposits. Non-interest-bearing transaction deposits increase the Company's net interest income by lowering its cost of funds.

The Company obtains deposits primarily from the communities it serves. The Company believes that no material portion of its deposits has been obtained from or is dependent on any one person or industry. The Company accepts deposits in excess of $100,000 from customers. These deposits are priced to remain competitive.

Maturities of time certificates of deposits of $100,000 or more outstanding at March 31, 2013 and December 31, 2012 are summarized as follows:

	(in thousands)	
	March 31, 2013	December 31, 2012
Three months or less	$17,656	$17,159
Over three to twelve months	27,737	30,361
Over twelve months	10,631	8,953
Total	$56,024	$56,473

The decrease in time certificates of deposit (CD's) of $100,000 or more is primarily attributable to the maturities of time deposits.

Liquidity and Capital Resources

In order to serve our market area, the Company must maintain adequate liquidity and adequate capital. Liquidity is measured by various ratios, in management's opinion, the most common being the ratio of net loans to deposits (including loans held-for-sale). This ratio was 58.2% on March 31, 2013. In addition, on March 31, 2013, the Company had the following short-term investments: $1,968,000 in securities due within one year or less; and $27,079,000 in securities due in one to five years.

To meet unanticipated funding requirements, the Company maintains short-term unsecured lines of credit with other banks totaling $37,000,000 at March 31, 2013; additionally, the Company has a line of credit with the Federal Home Loan Bank (the "FHLB"), with a borrowing capacity at March 31, 2013 of $145,683,000. The line of credit with FHLB is secured under terms of a blanket collateral agreement by a pledge of FHLB stock and certain other qualifying collateral such as commercial and mortgage loans.

The Company's primary source of liquidity on a stand-alone basis is dividends from the Bank. Dividends from the Bank are subject to regulatory restrictions.

As of March 31, 2013, the Bank's capital ratios exceeded applicable regulatory requirements. The following table presents the capital ratios for the Bank, compared to the regulatory standards for well-capitalized depository institutions, as of March 31, 2013.

	(amounts in thousands except percentage amounts)		
	Actual		Well Capitalized Ratio Requirement
	Capital	Ratio	
Leverage	$74,256	8.86 %	5.0 %
Tier 1 Risk-Based	$74,256	15.10 %	6.0 %
Total Risk-Based	$80,447	16.35 %	10.0 %

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ITEM 3. – QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company believes that there have been no material changes in the quantitative and qualitative disclosures about market risk as of March 31, 2013, from those presented in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2012, which are incorporated by reference herein.

ITEM 4. – CONTROLS AND PROCEDURES

(a) We maintain "disclosure controls and procedures," as such term is defined in Rule 13a-15(e) under the Securities Exchange Act of 1934 (the "Exchange Act"), that are designed to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in Securities and Exchange Commission rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating our disclosure controls and procedures, management recognized that disclosure controls and procedures, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the disclosure controls and procedures are met. Our disclosure controls and procedures have been designed to meet reasonable assurance standards. Additionally, in designing disclosure controls and procedures, our management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible disclosure controls and procedures. The design of any disclosure controls and procedures also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Our Chief Executive Officer (principal executive officer) and Chief Financial Officer (principal financial officer) have concluded that the design and operation of our disclosure controls and procedures are effective as of March 31, 2013. This conclusion is based on an evaluation conducted under the supervision and with the participation of management.

(b) During the quarter ended March 31, 2013, there were no changes in our internal controls over financial reporting that materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.

PART II – OTHER INFORMATION

ITEM 1. – LEGAL PROCEEDINGS

Neither the Company nor the Bank is a party to any material pending legal proceeding, nor is any of their property the subject of any material pending legal proceeding, except ordinary routine litigation arising in the ordinary course of the Bank's business and incidental to its business, none of which is expected to have a material adverse impact upon the Company's or the Bank's business, financial position or results of operations.

ITEM 1A. – RISK FACTORS

There are no material changes from the risk factors previously disclosed in our Annual Report on Form 10-K for the year ended December 31, 2012. See Part I, Item 1A in our Annual Report on Form 10-K for the year ended December 31, 2012, entitled “Risk Factors.”

ITEM 2. – UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

None.

ITEM 3. – DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. – MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5. – OTHER INFORMATION

None.

ITEM 6. – EXHIBITS

Exhibit Number	Description of Document
31.1	Rule 13a — 14(a) Certification of Chief Executive Officer
31.2	Rule 13a — 14(a) Certification of Chief Financial Officer
32.1*	Statement of the Chief Executive Officer under Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. Section 1350)
32.2*	Statement of the Chief Financial Officer under Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. Section 1350)
101**	Pursuant to Rule 405 of Regulation S-T, the following financial information from the Registrant's Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2013, is formatted in XBRL interactive data files: (i) Condensed Consolidated Balance Sheets; (ii) Condensed Consolidated Statements of Income; (iii) Condensed Consolidated Statement of Stockholders' Equity and Comprehensive Income; (iv) Condensed Consolidated Statements of Cash Flows; and (iv) Notes to Condensed Consolidated Financial Statements.

* In accordance with Item 601(b)(32)(ii) of Regulation S-K and SEC Release No. 34-47986, the certifications furnished in Exhibits 32.1 and 32.2 hereto are deemed to accompany this Form 10-Q and will not be deemed "filed" for purposes of Section 18 of the Exchange Act. Such certifications will not be deemed to be incorporated by reference into any filing under the Securities Act or the Exchange Act.

** In accordance with Rule 406T of Regulation S-T, the information furnished in these exhibits will not be deemed "filed" for purposes of Section 18 of the Exchange Act. Such exhibits will not be deemed to be incorporated by reference into any filing under the Securities Act or Exchange Act.

SIGNATURES

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

FIRST NORTHERN COMMUNITY BANCORP

Date: May 9, 2013 By:/s/ Jeremiah Z. Smith

Jeremiah Z. Smith, Executive Vice President / Chief Financial Officer
(Principal Financial Officer and Duly Authorized Officer)