UNION BANKSHARES INC
Form 10-Q/A
January 07, 2010

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q/A

Amendment No. 1

(X) QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)

OF THE SECURITIES EXCHANGE ACT OF 1934

OR

( ) TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)

OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended: September 30, 2009

Commission file number: 001-15985

UNION BANKSHARES, INC.

VERMONT 03-0283552

P.O. BOX 667

MAIN STREET

MORRISVILLE, VT 05661

Registrant s telephone number: 802-888-6600

Former name, former address and former fiscal year, if changed since last report: Not applicable

Securities registered pursuant to section 12(b) of the Act:

Common Stock, $2.00 par value	Nasdaq Stock Market
(Title of class)	**(Exchanges registered on)**

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes [X] No [ ]

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See 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 Act). Yes [ ] No [X]

Indicate the number of shares outstanding of each of the issuer s classes of common stock as of November 13, 2009:

Common Stock, $2 par value	4,461,208 shares

Explanatory Note: The September 30, 2009 Form 10-Q is being amended to correct the following two clerical errors in the Management s Discussion and Analysis of Financial Condition and Results of Operations (MD&A) in Part I, Item 2 of the report:

(1) In the MD&A section on Market Risk and Asset and Liability Management on page 42 of the original filing Projected Net Interest Income was understated by $380 thousand and should have been $13,279 thousand instead of $12,899 thousand. This correction reduces the percentage difference between projected and actual net interest income to 0.8% instead of 3.8% as previously reported. The corrected information appears on page 30 of this Amendment.

(2) In the MD&A section on Capital Resources on page 48 of the original filing the Total Capital to risk weighted assets for the Company was mistakenly reported as $42,231 thousand and the correct amount was $46,231 thousand. All the other amounts and ratios in the table are unchanged. The corrected information appears on page 36 of this Amendment.

A conforming change was made to the MD&A page number references in the Quantitative and Qualitative Disclosures About Market Risk (Part 1, Item 3).

UNION BANKSHARES, INC.

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Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations

MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

GENERAL

The following discussion and analysis by management focuses on those factors that had a material effect on Union Bankshares, Inc. s (Company) financial position as of September 30, 2009, and as of December 31, 2008, and its results of operations for the three and nine months ended September 30, 2009 and 2008. This discussion is being presented to provide a narrative explanation of the financial statements and should be read in conjunction with the consolidated financial statements and related notes and with other financial data appearing elsewhere in this filing and with the Company s Annual Report on Form 10-K for the year ended December 31, 2008. In the opinion of the Company s management, the interim unaudited data reflects all adjustments, consisting only of normal recurring adjustments, and disclosures necessary to fairly present the Company s consolidated financial position and results of operations for the interim period. Management is not aware of the occurrence of any events between September 30, 2009 and November 13, 2009 which would materially affect the information presented.

CAUTIONARY ADVICE ABOUT FORWARD LOOKING STATEMENTS

The Company may from time to time make written or oral statements that are considered forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements may include financial projections, statements of plans and objectives for future operations, estimates of future economic performance and assumptions relating thereto. The Company may include forward-looking statements in its filings with the Securities and Exchange Commission (SEC), in its reports to stockholders, including this Quarterly Report, in press releases, other written materials, and in statements made by senior management to analysts, rating agencies, institutional investors, representatives of the media and others.

Forward-looking statements reflect management s current expectations and are subject to uncertainties, both general and specific, and risk exists that those predictions, forecasts, projections and other estimates contained in forward-looking statements will not be achieved. When management uses any of the words believes, expects, anticipates, intends, plans, seeks, estimates , or similar expressions, they are making forward looking statement possible events or factors, including those beyond the control of management, could affect the future financial results and performance of the Company. This could cause results or performance to differ materially from those expressed in forward-looking statements. The possible events or factors that might affect the forward-looking statements include, but are not limited to, the listing in the Company s Annual Report on Form 10-K for the year ended December 31, 2008 and the items added below:

disruptions in U.S. and global financial and credit markets;

the implementation of international financial reporting standards (IFRS) for United States companies;

impact of governmental interposition in financial services or other industries;

adverse changes in the local real estate market, which negatively impact collateral values and the Company s ability to recoup loan losses through disposition of real estate collateral; and

further expansion of fair value accounting or disclosure.

When evaluating forward-looking statements to make decisions with respect to the Company, investors and others are cautioned to consider these and other risks and uncertainties, including the events and circumstances discussed under Recent Developments below, and are reminded not to place undue reliance on such statements. Forward-looking statements speak only as of the date they are made and the Company undertakes no obligation to update them to reflect new or changed information or events, except as may be required by federal securities laws.

RECENT DEVELOPMENTS

The U.S. and global economies have experienced significant stress and disruptions in the financial sector over the last twelve months but are showing signs of stabilization. Interest rates remain at historic lows, bank failures are higher than they have been in over 15 years and the amount of U.S. Government dollars pumped into the system is unprecedented. Dramatic slowdowns in certain sectors of the housing industry with falling home prices, continuing foreclosures and increasing unemployment have resulted in major issues for some financial institutions, including government-sponsored entities and investment banks. These issues have caused many financial institutions to seek additional capital, to merge with larger and stronger institutions and, in some cases, to fail. The economic instability progressed to many other business and government sectors and appears to be affecting the majority of consumers as well.

Despite the volatile economy, Vermont continues to have one of the lowest residential foreclosure rates in the country. Also, as northern New England did not experience the dramatic run up in housing prices that preceded the current economic downturn, likewise, we have not seen the values drop as far as other parts of the country.

In response to the financial crisis affecting the banking and financial markets, many new laws, regulations and programs have been promulgated. We will not attempt to discuss them all within this Form 10-Q but will mention the ones that continue or will have a known financial impact on the Company.

In October 2008, the Emergency Economic Stabilization Act of 2008 (the EESA) was signed into law. Pursuant to the EESA, the Federal Deposit Insurance Corporation temporarily increased the deposit insurance coverage limits to $250,000 per ownership category at each insured financial institution. That coverage has been extended until December 31, 2013.

After receiving a recommendation from the boards of the Federal Deposit Insurance Corporation (the FDIC) and the Federal Reserve System (the Federal Reserve), the Treasury signed the systemic risk exception to the FDIC Act, enabling the FDIC to temporarily provide a 100% guarantee on deposits in noninterest bearing transaction deposit accounts under a Temporary Liquidity Guarantee Program. Coverage under the Temporary Liquidity Guarantee Program was available for 30 days without charge and for calendar year 2009 at a cost of 10 basis points per annum for noninterest bearing transaction deposits in excess of the $250,000 insured deposit limit. The program has been extended until June 30, 2010 at a cost of 15 basis points per annum and the Company is continuing its participation in this program through that date.

The Company decided it was not in the best interest of the Company or its shareholders to participate in any of the other governmental programs available under the Troubled Asset Purchase Program given the strength of the Company s capital position, the nature of the government restrictions with the possibility of additional restrictions in the future, the fact that the Company did not target sub-prime borrowers and the fact that the Company is able to meet the lending and withdrawal needs of our customers with our available funding sources. (For additional information,

see Capital Resources on page 47.)

Union Bank is participating in the U.S. Small Business Administration s (SBA) temporary America s Recovery Capital (ARC) program which offers interest-free loans of up to $35,000 to viable small businesses, which carry a 100% guaranty from the SBA to the lender and require no fees paid to the SBA. The program pays participating lenders a market rate of interest while the ARC loans are outstanding.

In addition, as a result of the weakness of certain financial institutions, the FDIC is continuing to take action that will result in increased FDIC insurance assessments for United States FDIC-insured financial institutions, including Union. Under the deposit insurance restoration plan approved by the FDIC in October 2008, the FDIC Board set a rate schedule to raise the insurance reserve ratio to 1.15% within five years. On February 27, 2009, the FDIC announced that the restoration plan horizon has been extended to seven years in light of the current significant strains on banks and the financial system and the likelihood of a severe recession. In addition, the FDIC announced a special assessment of 5 basis points assessed on net assets at June 30, 2009 and collected on September 30, 2009. This special assessment totaled $191 thousand for the Company and we anticipate our total premium assessment for

2009 will be approximately $700 thousand compared to $87 thousand for 2008. In September 2009, the FDIC proposed that banks prepay three and one quarter years of regular assessments on December 30, 2009. The FDIC would maintain its current assessment rates through 2010 but effective January 1, 2011, the rate would increase by three basis points. Additionally, the agency s restoration plan would be extended from seven to eight years. If approved, the Company will book the prepayment as an asset and expense an appropriate amount monthly through the statement of income. The Company anticipates its Prepaid Assessment will be approximately $1.8 million.

It is not completely clear at this time what impact current or future government sponsored programs will have on the Company, its customers or the U.S. and global financial markets.

CRITICAL ACCOUNTING POLICIES

The Company has established various accounting policies which govern the application of accounting principles generally accepted in the United States of America (GAAP) in the preparation of the Company s financial statements. Certain accounting policies involve significant judgments and assumptions by management which have a material impact on the reported amount of assets, liabilities, capital, revenues and expenses and related disclosures of contingent assets and liabilities in the consolidated financial statements and accompanying notes. The SEC has defined a company s critical accounting policies as the ones that are most important to the portrayal of the company s financial condition and results of operations, and which require the company to make its most difficult and subjective judgments, often as a result of the need to make estimates of matters that are inherently uncertain. Based on this definition, the Company has identified the accounting policies and judgments most critical to the Company. The judgments and assumptions used by management are based on historical experience and other factors, which are believed to be reasonable under the circumstances. Because of the nature of the judgments and assumptions made by management, actual results could differ from estimates and have a material impact on the carrying value of assets, liabilities, capital, or the results of operations of the Company.

The Company believes the allowance for loan losses is a critical accounting policy that requires the most significant judgments and estimates used in the preparation of its consolidated financial statements. Adequacy of the allowance for loan losses is determined quarterly using a consistent, systematic methodology, which analyzes the risk inherent in the loan portfolio. In addition to evaluating the collectability of specific loans when determining the adequacy of the allowance, management also takes into consideration other factors such as changes in the mix and size of the loan portfolio, historical loss experience, the amount of delinquencies and loans adversely classified, industry trends, and the impact of the local and regional economy on the Company s borrowers. Changes in these factors may cause management s estimate of the allowance for loan losses to increase or decrease and result in adjustments to the Company s provision for loan losses in future periods. For additional information, see FINANCIAL CONDITION *Allowance for Loan Losses* below.

The decision to recognize other-than-temporary impairment on investment securities available-for-sale has become more difficult as complete information is not always available and market conditions and other relevant factors are subject to rapid changes. The other-than-temporary impairment decision has become a critical accounting policy for the Company. Accounting guidance requires companies to perform periodic reviews of individual securities in their

investment portfolios to determine whether a decline in the value of a security is other-than-temporary. A review of other-than-temporary impairment requires companies to make certain judgments regarding the cause and materiality of the decline, its effect on the financial statements and the probability, extent and timing of a valuation recovery, the company s intent and ability to continue to hold the security, and, with respect to debt securities, the likelihood that the Company will have to sell the security before its value recovers. Pursuant to these requirements, management assesses valuation declines to determine the extent to which such changes are attributable to (1) fundamental factors specific to the issuer, such as the nature of the issuer and its financial condition, business prospects or other factors or (2) market-related factors, such as interest rates or equity market declines. Declines in the fair value of securities below their costs that are deemed by management to be other-than-temporary are (1) if equity securities, recorded in earnings as realized losses and (2) if debt securities, recorded in earnings as realized losses to the extent they are deemed credit losses, with noncredit losses recorded in Other Comprehensive Income.

The Company s pension benefit obligations and net periodic benefit cost are actuarially determined based on the following assumptions: discount rate, current and estimated future return on plan assets, wage base rate, anticipated mortality rates, Consumer Price Index, and rate of increase in compensation levels. The annual determination of the pension benefit obligations and net periodic benefit cost is a critical accounting estimate as it requires the use of estimates and judgment related to the amount and timing of expected future cash outflows for benefit payments and cash inflows for maturities and returns on plan assets as well as Company contributions. Changes in estimates, assumptions and actual results could have a material impact on the Company s financial condition or results of operations.

The Company also has other key accounting policies, which involve the use of estimates, judgments and assumptions that are significant to understanding the Company s financial results including the valuation of deferred tax assets, and determination of the fair values of investment securities and other real estate owned. See FINANCIAL CONDITION *Allowance for Loan Losses and Investment Activities* below. Although management believes that its estimates, assumptions and judgments are reasonable, they are based upon information presently available and can be impacted by events outside the control of the Company. Actual results may differ significantly from these estimates under different assumptions, judgments or conditions.

OVERVIEW

The Company s net income was $1.45 million for the quarter ended September 30, 2009 and $1.17 million for the quarter ended September 30, 2008, an increase of $280 thousand, or 24.0%. These results reflected an increase in net interest income of $157 thousand, or 3.6%, and an increase of $671 thousand, or 80.1%, in noninterest income. The increase in noninterest income was mainly due to the increase in net gains on sales of loans held for sale from $74 thousand for the quarter ended September 30, 2008 to $314 thousand for the quarter ended September 30, 2009 and the third quarter 2008 write-down of $512 thousand on impaired investment securities available-for-sale. Salaries and wages were also lower by $73 thousand, or 4.5%, for the third quarter of 2009 compared to the same period last year due to the deferral of $30 thousand of loan origination costs for 2009 and increased operating efficiencies despite the addition of two full service branches in the third quarter of 2008. These positive changes were partially offset by a net increase in noninterest expense of $290 thousand between periods, which reflected an increase of $87 thousand in the FDIC insurance assessment due to higher rates and deposit growth and a $126 thousand increase, or 86.3%, in the defined benefit pension plan expense.

The Company continued to face a challenging interest rate environment as the prime rate has been reduced seven times since January 1, 2008 from 7.25% to 3.25% on September 30, 2009. Total interest income decreased by $356 thousand, or 5.7%, to $5.8 million in the third quarter of 2009 versus $6.2 million in the third quarter of 2008, but that decrease was more than offset by the decrease in interest expense from $1.8 million in 2008 to $1.3 million in 2009, a decrease of $513 thousand, or 28.7%, between periods. The result of the changes in interest income and interest expense was that net interest income for the third quarter of 2009 was $4.6 million, up $157 thousand, or 3.6%, from the third quarter of 2008 of $4.4 million. The increase in net interest income was more a function of the decrease in interest paid on interest bearing liabilities as this mitigated the decrease in interest income. During the third quarter of 2009, the Company s net interest margin decreased 17 basis points to 4.50%, from 4.67% for the third quarter of 2008. The Company s net interest spread declined 3 basis points to 4.22% for the third quarter of 2009, compared to 4.25% for the same period last year. The decline in the net interest spread was primarily the result of the decline in average

interest rates earned on loans as the 400 basis point drop in the prime rate between January 1, 2008 and September 30, 2009 had an effect on the repricing of adjustable rate loans and the volume of refinancings, as customers took advantage of the lower rates. Further drops in the prime rate and/or increases in competitors deposit rates could be problematic as individual instruments continue to reprice.

The Company s total assets increased from $440.1 million at December 31, 2008, to $443.9 million at September 30, 2009, an increase of $3.8 million, or 0.9%. Deposits increased from $364.4 million at December 31, 2008 to $369.4 million at September 30, 2009, an increase of $5.1 million, or 1.4%.

Borrowed funds decreased from $27.4 million at December 31, 2008 to $25.8 million at September 30, 2009, a decrease of $1.6 million, or 6.0%. Total loans, including loans held for sale, decreased $1.5 million, or 0.4%, from $353.4 million at December 31, 2008 to $351.9 million at September 30, 2009. Total loans at September 30, 2009 are net of $53.6 million in residential real estate loans sold during the first nine months of 2009. Despite a weakening economy and our conservative underwriting practices, loan demand during the first nine months of 2009 was strong due, in large part, to lower interest rates which have sparked both existing and new customers to refinance loans. The Company has also benefited from a changing competitive environment as some of our competitors have changed their lending and pricing practices.

The Company s asset quality has remained strong with September 30, 2009 total nonperforming assets at $6.3 million, or 1.42% of total assets, compared to $8.1 million, or 1.85% of total assets, at December 31, 2008 and $8.5 million, or 2.01% of total assets, at September 30, 2008.

The following unaudited per share information and key ratios depict several measurements of performance or financial condition for or at the three and nine months ended September 30, 2009 and 2008, respectively:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2009	2008	2009	2008
Return on average assets (ROA) (1)	1.31%	1.12%	1.22%	1.25%
Return on average equity (ROE) (1)	14.66%	11.27%	13.47%	12.04%
Net interest margin (1)(2)	4.50%	4.67%	4.55%	4.80%
Net interest spread (3)	4.22%	4.25%	4.24%	4.34%
Loan to deposit ratio	95.24%	98.50%	95.24%	98.50%
Net loan charge-offs to average loans not held for sale (1)	0.10%	0.03%	0.09%	0.05%
Allowance for loan losses to loans not held for sale	1.03%	1.01%	1.03%	1.01%
Nonperforming assets to total assets (4)	1.42%	2.01%	1.42%	2.01%
Equity to assets	9.07%	9.73%	9.07%	9.73%
Total capital to risk weighted assets	15.66%	15.89%	15.66%	15.89%
Book value per share	$9.02	$9.19	$9.02	$9.19
Earnings per share	$0.32	$0.26	$0.88	$0.84
Dividends paid per share	$0.25	$0.28	$0.78	$0.84
Dividend payout ratio (5)	78.13%	107.69%	88.64%	100.00%

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(1)

Annualized.

(2)

The ratio of tax equivalent net interest income to average earning assets. See page 21 for more information.

(3)

The difference between the average rate earned on assets minus the average rate paid on liabilities. See page 21 for more information.

(4)

Nonperforming assets are loans or investment securities that are in nonaccrual or 90 or more days past due as well as other real estate or assets owned.

(5)

Cash dividends declared and paid per share divided by consolidated net income per share.

RESULTS OF OPERATIONS

Net Interest Income. The largest component of the Company s operating income is net interest income, which is the difference between interest and dividend income received from interest-earning assets and the interest expense paid on interest-bearing liabilities. The Company s net interest income increased $157 thousand, or 3.6%, to $4.6 million for the three months ended September 30, 2009, from $4.4 million for the three months ended September 30, 2008. The net interest spread decreased 3 basis points

to 4.22% for the three months ended September 30, 2009, from 4.25% for the three months ended September 30, 2008. The decline in the net interest spread was primarily the result of the drop in average interest rates earned on loans from 6.85% for the quarter ended September 30, 2008 to 6.25% for the quarter ended September 30, 2009. The prime rate was 7.25% on January 1, 2008, 5.00% by September 30, 2008 and 3.25% throughout 2009, which affected the repricing of adjustable rate loans as well as the volume of new loans and refinancing activity during the last 21 months, as customers took advantage of the lower rates. The adverse effect of declining rates on the Company s net interest spread was mitigated by a 77 basis point decline in the average rate paid on interest bearing liabilities in the third quarter of 2009 versus the same period last year. The net interest margin for the third quarter of 2009 decreased 17 basis points to 4.50% from the 2008 comparison period at 4.67% reflecting the net effect of an increase in net interest income of $157 thousand and an increase of $29.2 million, or 7.6%, in average earning assets.

The trend of increasing pressure on the net interest spread and net interest margin were also reflected in the year-to-date results, with a decline of 10 basis points in the net interest spread from 4.34% for the nine months ended September 30, 2008 to 4.24% for the nine months ended September 30, 2009. The net interest margin declined 25 basis points from 4.80% to 4.55% over the same period. Further decrease in the prime rate would not necessarily be beneficial to the Company in the near term, especially if funding rates did not follow a similar downward trend. (See *Market Risk and Asset and Liability Management* on page 41.)

Yields Earned and Rates Paid. The following tables show, for the periods indicated, the total amount of income recorded from average interest-earning assets and the related average yields, the interest expense associated with average interest-bearing liabilities, the related average rates paid, and the relative net interest spread and net interest margin. Yield and rate information is calculated on an annualized tax equivalent basis. Yield and rate information for a period is average information for the period, and is calculated by dividing the annualized tax equivalent income or expense item for the period by the average balance of the appropriate balance sheet item during the period. Net interest margin is annualized tax equivalent net interest income divided by average interest-earning assets. Nonaccrual loans and investments are included in asset balances for the appropriate periods, but recognition of interest on such loans or investments is discontinued and any remaining accrued interest receivable is reversed in conformity with federal regulations.

Tax-exempt interest income amounted to $315 thousand and $284 thousand for the three months ended September 30, 2009 and 2008, respectively, and $955 thousand and $787 thousand for the nine months ended September 30, 2009 and 2008, respectively. The following table presents the effect of tax-exempt income on the calculation of the net interest margin, using a marginal tax rate of 34% for 2009 and 2008:

	For The Three Months ended, September 30,		**For The Nine Months ended, September 30,**	
	2009	**2008**	**2009**	**2008**
	(Dollars in thousands)			
Net interest income as presented	$4,571	$4,414	$13,388	$13,072
Effect of tax-exempt interest				
Securities available-for-sale	30	33	96	103

Loans	103	87	308	230
Net interest income, tax equivalent	$4,704	$4,534	$13,792	$13,405

	Three Months Ended September 30,					
	2009			2008		
	Average Balance	Interest Earned/ Paid	Average Yield/ Rate	Average Balance	Interest Earned/ Paid	Average Yield/ Rate
	(Dollars in thousands)					
Average Assets:						
Federal funds sold and overnight deposits	$ 21,886	$ 11	0.20%	$ 10,048	$ 46	1.83%
Interest bearing deposits in banks	16,011	115	2.84%	9,590	104	4.31%
Investment securities (1), (2)	21,404	245	5.15%	27,483	322	5.16%
Loans, net (1), (3)	354,316	5,477	6.25%	337,271	5,718	6.85%
FHLB of Boston stock (4)	1,922	-	0.00%	1,922	14	2.87%
Total interest earning assets (1)	415,539	5,848	5.71%	386,314	6,204	6.51%
Cash and due from banks	5,309			10,597		
Premises and equipment	7,545			7,276		
Other assets	11,568			10,685		
Total assets	$439,961			$414,872		
Average Liabilities and Stockholders Equity:						
NOW accounts	$ 60,149	$ 34	0.23%	$ 54,307	$ 71	0.52%
Savings/money market accounts	106,661	160	0.59%	93,911	314	1.33%
Time deposits	144,298	791	2.17%	138,267	1,101	3.17%
Borrowed funds	27,078	292	4.22%	27,782	304	4.30%
Total interest bearing liabilities	338,186	1,277	1.49%	314,267	1,790	2.26%
Noninterest bearing deposits	54,303			53,441		
Other liabilities	8,039			5,797		
Total liabilities	400,528			373,505		
Stockholders equity	39,433			41,367		
Total liabilities and stockholders equity	$439,961			$414,872		

Net interest income	$4,571	$4,414
Net interest spread (1)	4.22%	4.25%
Net interest margin (1)	4.50%	4.67%

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(1)

Average yields reported on a tax-equivalent basis using a marginal tax rate of 34%.

(2)

Average balances of investment securities are calculated on the amortized cost basis and include nonaccrual securities.

(3)

Includes loans held for sale as well as nonaccrual loans and is net of unearned income and allowance or loan losses.

(4)

Dividends on this stock were suspended effective during the fourth quarter of 2008.

	Nine Months Ended September 30,					
	2009			2008		
	Average Balance	Interest Earned/ Paid	Average Yield/ Rate	Average Balance	Interest Earned/ Paid	Average Yield/ Rate
	(Dollars in thousands)					
Average Assets:						
Federal funds sold and overnight deposits	$ 12,906	$ 16	0.17%	$ 6,703	$ 105	2.08%
Interest bearing deposits in banks	14,016	344	3.28%	9,512	335	4.69%
Investment securities (1), (2)	24,153	858	5.27%	30,038	1,075	5.22%
Loans, net (1), (3)	352,580	16,293	6.30%	324,106	16,997	7.08%
FHLB of Boston stock (4)	1,922	-	0.00%	1,795	51	3.74%
Total interest earning assets (1)	405,577	17,511	5.90%	372,154	18,563	6.77%
Cash and due from banks	5,355			10,129		
Premises and equipment	7,457			7,000		
Other assets	11,752			10,925		
Total assets	$430,141			$400,208		
Average Liabilities and Stockholders Equity:						
NOW accounts	$ 60,083	$ 116	0.26%	$ 53,550	$ 232	0.58%
Savings/money market accounts	105,072	510	0.65%	91,327	951	1.39%
Time deposits	137,837	2,610	2.53%	129,617	3,440	3.53%
Borrowed funds	27,841	887	4.20%	26,492	868	4.31%
Total interest bearing liabilities	330,833	4,123	1.66%	300,986	5,491	2.43%
Noninterest bearing deposits	51,925			51,257		
Other liabilities	8,311			6,314		
Total liabilities	391,069			358,557		
Stockholders equity	39,072			41,651		
Total liabilities and stockholders equity	$430,141			$400,208		

Net interest income	$13,388		$13,072	
Net interest spread (1)		4.24%		4.34%
Net interest margin (1)		4.55%		4.80%

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(1)

Average yields reported on a tax-equivalent basis using a marginal tax rate of 34%.

(2)

Average balances of investment securities are calculated on the amortized cost basis and include nonaccrual securities.

(3)

Includes loans held for sale as well as nonaccrual loans and is net of unearned income and allowance for loan losses.

(4)

Dividends on this stock were suspended effective during the fourth quarter of 2008.

Rate/Volume Analysis. The following table describes the extent to which changes in average interest rates (on a fully tax-equivalent basis) and changes in volume of average interest earning assets and interest bearing liabilities have affected the Company s interest income and interest expense during the period indicated. For each category of interest earning assets and interest bearing liabilities information is provided on changes attributable to:

changes in volume (change in volume multiplied by prior rate);

changes in rate (change in rate multiplied by prior volume); and

total change in rate and volume.

Changes attributable to both rate and volume have been allocated proportionately to the change due to volume and the change due to rate.

	Three Months Ended September 30, 2009 Compared to Three Months Ended September 30, 2008 Increase/(Decrease) Due to Change In		
	Volume	**Rate**	**Net**
	(Dollars in thousands)		
Interest earning assets:			
Federal funds sold and overnight deposits	$ 28	$ (63)	$ (35)
Interest bearing deposits in banks	55	(44)	11
Investment securities	(76)	(1)	(77)
Loans, net	286	(527)	(241)
FHLB of Boston stock	-	(14)	(14)
Total interest earning assets	293	(649)	(356)
Interest bearing liabilities:			
NOW accounts	$ 7	$ (44)	$(37)
Savings/money market accounts	38	(192)	(154)
Time deposits	46	(356)	(310)
Borrowed funds	(7)	(5)	(12)
Total interest bearing liabilities	84	(597)	(513)
Net change in net interest income	$ 209	$ (52)	$157