SALISBURY BANCORP INC
Form 10-Q
August 15, 2011

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2011

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

Commission file number 0-24751
SALISBURY BANCORP, INC.
(Exact name of registrant as specified in its charter)

Connecticut	06-1514263
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
5 Bissell Street, Lakeville, CT	06039
(Address of principal executive offices)	(Zip code)

(860) 435-9801
(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 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) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes_________ 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 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 o Accelerated filer o Non-accelerated filer o Smaller reporting company ý

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 August 1, 2011, is 1,688,731.

1

TABLE OF CONTENTS

		Page
	PART I FINANCIAL INFORMATION	
Item 1.	Financial Statements:	
	Consolidated Balance Sheets as of June 30, 2011 (unaudited) and December 31, 2010	3
	Consolidated Statements of Income for the three and six month periods ended June 30, 2011 and 2010 (unaudited)	4
	Consolidated Statements of Changes in Shareholders' Equity for the six month periods ended June 30, 2011 and 2010 (unaudited)	5
	Consolidated Statements of Cash Flows for the six month periods ended June 30, 2011 and 2010 (unaudited)	6
	Notes to Consolidated Financial Statements (unaudited)	7
Item 2.	Management's Discussion and Analysis of Financial Condition and Results of Operations	21
Item 3.	Quantitative and Qualitative Disclosures of Market Risk	39
Item 4.	Controls and Procedures	40
	PART II Other Information	
Item 1.	Legal Proceedings	40
Item 1A.	Risk Factors	41
Item 2.	Unregistered Sales of Equity Securities and Use of Proceeds	41
Item 3.	Defaults upon Senior Securities	41
Item 4.	Removed and Reserved	41
Item 5.	Other information	41
Item 6.	Exhibits	41

Table of Contents

PART I - FINANCIAL INFORMATION

Salisbury Bancorp, Inc. and Subsidiary
CONSOLIDATED BALANCE SHEETS

in thousands (except share data)	June 30, 2011 Unaudited	December 31, 2010
ASSETS		
Cash and due from banks	$7,570	$6,694
Interest bearing demand deposits with other banks	36,374	20,214
Total cash and cash equivalents	43,944	26,908
Interest bearing time deposits with other banks	-	5,000
Securities		
Available-for-sale at fair value	139,407	147,422
Held-to-maturity at amortized cost (fair value: $54 and $58)	53	56
Federal Home Loan Bank of Boston stock at cost	6,032	6,032
Loans held-for-sale	146	1,184
Loans receivable, net (allowance for loan losses: $3,979 and $3,920)	364,854	352,449
Investment in real estate	75	75
Other real estate owned	452	610
Bank premises and equipment, net	12,307	12,190
Goodwill	9,829	9,829
Intangible assets (net of accumulated amortization: $1,412 and $1,301)	1,131	1,242
Accrued interest receivable	2,086	2,132
Cash surrender value of life insurance policies	3,934	3,854
Deferred taxes	1,328	2,540
Other assets	2,737	3,947
Total Assets	$588,315	$575,470
LIABILITIES and SHAREHOLDERS' EQUITY		
Deposits		
Demand (non-interest bearing)	$78,985	$71,565
Demand (interest bearing)	63,651	63,258
Money market	113,316	77,089
Savings and other	93,341	93,324
Certificates of deposit	109,736	125,053
Total deposits	459,029	430,289
Repurchase agreements	12,359	13,190
Federal Home Loan Bank of Boston advances	55,460	72,812
Accrued interest and other liabilities	3,358	4,163
Total Liabilities	530,206	520,454
Commitments and contingencies	-	-
Shareholders' Equity		
Preferred stock - $.01 per share par value		
Authorized: 25,000; Shares issued: 8,816;		
Liquidation preference: $1,000 per share	8,749	8,738
Common stock - $.10 per share par value		
Authorized: 3,000,000;		
Issued: 1,688,731 and 1,687,661	169	168

Common stock warrants outstanding	112	112
Paid-in capital	13,227	13,200
Retained earnings	37,216	36,567
Accumulated other comprehensive loss, net	(1,364)	(3,769)
Total Shareholders' Equity	58,109	55,016
Total Liabilities and Shareholders' Equity	$588,315	$575,470

Table of Contents

Salisbury Bancorp, Inc. and Subsidiary
CONSOLIDATED STATEMENTS OF INCOME

Periods ended June 30, (in thousands except per share amounts) unaudited	Three months ended 2011	Three months ended 2010	Six months ended 2011	Six months ended 2010
Interest and dividend income				
Interest and fees on loans	$4,695	$4,601	$9,359	$9,088
Interest on debt securities				
Taxable	733	1,033	1,516	1,959
Tax exempt	554	559	1,108	1,119
Other interest and dividends	38	38	75	84
Total interest and dividend income	6,020	6,231	12,058	12,250
Interest expense				
Deposits	829	1,125	1,700	2,324
Repurchase agreements	12	19	27	46
Federal Home Loan Bank of Boston advances	562	761	1,207	1,518
Total interest expense	1,403	1,905	2,934	3,888
Net interest income	4,617	4,326	9,124	8,362
Provision for loan losses	350	260	680	440
Net interest and dividend income after provision for loan losses	4,267	4,066	8,444	7,922
Non-interest income				
Trust and wealth advisory	596	491	1,263	1,036
Service charges and fees	522	499	1,022	952
Gains on sales of mortgage loans, net	59	122	192	164
Mortgage servicing, net	(5)	27	26	60
Gains on securities, net	-	1	11	1
Other	58	89	117	146
Total non-interest income	1,230	1,229	2,631	2,359
Non-interest expense				
Salaries	1,657	1,668	3,386	3,239
Employee benefits	650	586	1,283	1,216
Premises and equipment	568	495	1,151	1,011
Data processing	285	363	662	772
Professional fees	300	455	577	857
Collections and OREO	243	21	367	43
FDIC insurance	182	182	405	354
Marketing and community support	92	59	160	121
Amortization of intangibles	56	56	111	111
Other	399	360	754	833
Total non-interest expense	4,432	4,245	8,856	8,557
Income before income taxes	1,065	1,050	2,219	1,724
Income tax provision	183	172	394	251
Net income	$882	$878	$1,825	$1,473
Net income available to common shareholders	$766	$763	$1,594	$1,243
Basic and diluted earnings per share	$0.45	$0.45	$0.94	$0.74
Common dividends per share	0.28	0.28	0.56	0.56

4

Table of Contents

Salisbury Bancorp, Inc. and Subsidiary
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

(dollars in thousands) unaudited	Common Stock Shares	Common Stock Amount	Preferred Stock	Warrants	Paid-in capital	Retained earnings	Accumulated other comprehensive loss	Total shareholders' equity
Balances at December 31, 2009	1,686,701	$ 168	$ 8,717	$ 112	$ 13,177	$ 35,259	$ (5,078)	$ 52,355
Net income for period	-	-	-	-	-	1,473	-	1,473
Other comprehensive income, net of tax	-	-	-	-	-	-	1,703	1,703
Total comprehensive income								3,176
Amortization (accretion) of preferred stock	-	-	10	-	-	(10)	-	-
Common stock dividends paid	-	-	-	-	-	(945)	-	(945)
Preferred stock dividends paid	-	-	-	-	-	(220)	-	(220)
Issuance of common stock for director fees	960	-	-	-	23	-	-	23
Balances at June 30, 2010	1,687,661	$ 168	$ 8,727	$ 112	$ 13,200	$ 35,557	$ (3,375)	$ 54,389
Balances at December 31, 2010	1,687,661	$ 168	$ 8,738	$ 112	$ 13,200	$ 36,567	$ (3,769)	$ 55,016
Net income for period	-	-	-	-	-	1,825	-	1,825
Other comprehensive income, net of tax	-	-	-	-	-	-	2,405	2,405
Total comprehensive income								4,230
Amortization (accretion) of preferred stock	-	-	11	-	-	(11)	-	-
Common stock dividends paid	-	-	-	-	-	(945)	-	(945)

Preferred stock dividends paid	-	-	-	-	-	(220)	-	(220)
Issuance of common stock for director fees	1,070	1	-	-	27	-	-	28
Balances June 30, 2011	1,688,731	$ 169	$ 8,749	$ 112	$ 13,227	$ 37,216	$ (1,364)	$ 58,109

Table of Contents

Salisbury Bancorp, Inc. and Subsidiary
CONSOLIDATED STATEMENTS OF CASH FLOWS

Six months ended June 30, (in thousands) unaudited	2011	2010
Operating Activities		
Net income	$1,825	$1,473
Adjustments to reconcile net income to net cash provided by operating activities:		
(Accretion), amortization and depreciation		
Securities	163	305
Bank premises and equipment	414	396
Core deposit intangible	111	111
Mortgage servicing rights	114	74
Fair value adjustment on loans	22	22
Gain of calls of securities available-for-sale	(11)	(1)
Write down of other real estate owned	163	-
Provision for loan losses	680	440
Decrease in loans held-for-sale	1,038	152
Increase in deferred loan origination fees and costs, net	(116)	(44)
Mortgage servicing rights originated	(106)	(112)
Decrease (increase) in mortgage servicing rights impairment reserve	15	(5)
Decrease (increase) in interest receivable	45	(74)
Deferred tax benefit	(27)	(42)
Decrease in prepaid expenses	391	415
Increase in cash surrender value of life insurance policies	(80)	(84)
Decrease (increase) in income tax receivable	715	(194)
Decrease in other assets	17	40
(Decrease) increase in accrued expenses	(29)	46
Decrease in interest payable	(128)	(85)
(Decrease) increase in other liabilities	(613)	130
Issuance of shares for directors' fee	27	23
Net cash provided by operating activities	4,631	2,986
Investing Activities		
Proceeds from maturities of interest-bearing time deposits	5,000	-
Purchases of securities available-for-sale	(15,034)	(37,987)
Proceeds from calls of securities available-for-sale	19,000	12,190
Proceeds from maturities of securities available-for-sale	7,507	17,645
Proceeds from maturities of securities held-to-maturity	3	3
Loan originations and principle collections, net	(13,326)	(15,029)
Recoveries of loans previously charged-off	22	14
Proceeds from sale of other real estate owned	308	-
Capital expenditures	(467)	(1,416)
Net cash provided (utilized) by investing activities	3,013	(24,580)
Financing Activities		
Increase in deposit transaction accounts, net	44,058	27,560
Decrease in time deposits, net	(15,318)	(21,772)
Decrease in securities sold under agreements to repurchase, net	(831)	(3,295)
Principal payments on Federal Home Loan Bank of Boston advances	(17,352)	(1,418)
Common stock dividends paid	(945)	(945)
Preferred stock dividends paid	(220)	(220)

Net cash provided (utilized) by financing activities	9,392	(90)
Net increase (decrease) in cash and cash equivalents	17,036	(21,684)
Cash and cash equivalents, beginning of period	26,908	43,298
Cash and cash equivalents, end of period	$43,944	$21,614
Cash paid during period		
Interest	$3,062	$3,973
Income taxes	449	79
Non-cash transfers		
Transfer from loans to other real estate owned	321	-

6

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

NOTE 1 - BASIS OF PRESENTATION

The interim (unaudited) consolidated financial statements of Salisbury Bancorp, Inc. ("Salisbury") include those of Salisbury and its wholly owned subsidiary, Salisbury Bank and Trust Company (the "Bank"). In the opinion of management, the interim unaudited consolidated financial statements include all adjustments (consisting of normal recurring adjustments) necessary to present fairly the financial position of Salisbury and the statements of income, shareholders' equity and cash flows for the interim periods presented.

The financial statements have been prepared in accordance with generally accepted accounting principles. In preparing the financial statements, management is required to make extensive use of estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the balance sheet, and revenues and expenses for the period. Actual results could differ significantly from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses and the valuation of real estate acquired in connection with foreclosures or in satisfaction of loans. In connection with the determination of the allowance for loan losses and valuation of real estate, management obtains independent appraisals for significant properties.

Certain financial information, which is normally included in financial statements prepared in accordance with generally accepted accounting principles, but which is not required for interim reporting purposes, has been condensed or omitted. Operating results for the interim period ended June 30, 2011 are not necessarily indicative of the results that may be expected for the year ending December 31, 2011. The accompanying condensed financial statements should be read in conjunction with the financial statements and notes thereto included in Salisbury's 2010 Annual Report on Form 10-K for the period ended December 31, 2010.

The allowance for loan losses is a significant accounting policy and is presented in the Notes to Consolidated Financial Statements and in Management's Discussion and Analysis, which provide information on how significant assets are valued in the financial statements and how those values are determined. Based on the valuation techniques used and the sensitivity of financial statement amounts to the methods, assumptions and estimates underlying those amounts, management has identified the determination of the allowance for loan losses to be the accounting area that requires the most subjective judgments, and as such could be most subject to revision as new information becomes available.

Impact of New Accounting Pronouncements Issued

In June 2011, the FASB issued ASU 2011-05, "Presentation of Comprehensive Income." The objective of this ASU is to improve the comparability, consistency, and transparency of financial reporting and to increase the prominence of items reported in other comprehensive income. Under this ASU, an entity has 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. 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. An entity is required to present on the face of the financial statements reclassification adjustments for items that are reclassified from other comprehensive income to net income in the statement(s) where the components of net income and the components of other comprehensive income are presented. The amendments in this ASU should be applied retrospectively. For public entities, the amendments are effective for fiscal years, and interim periods within

those years, beginning after December 15, 2011.

In May 2011, the FASB issued ASU 2011-04, “Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and International Financial Reporting Standards.” The amendments in this ASU explain how to measure fair value. They do not require additional fair value measurements and are not intended to establish valuation standards or affect valuation practices outside of financial reporting. The amendments in this ASU are to be applied prospectively. For public entities, the amendments are effective during interim and annual periods beginning after December 15, 2011.

In April 2011, the Financial Accounting Standards Board (“FASB”) issued ASU 2011-02, “A Creditor’s Determination of Whether a Restructuring Is a Troubled Debt Restructuring.” This ASU provides additional guidance or clarification to help creditors determine whether a restructuring constitutes a troubled debt restructuring. For public entities, the amendments in this ASU are effective for the first interim or annual period beginning on or after June 15, 2011, and should be applied retrospectively to the beginning of the annual period of adoption. As a result of applying these amendments, an entity may identify receivables that are newly considered impaired, and should measure impairment on those receivables prospectively for the first interim or annual period beginning on or after June 15, 2011. Additional disclosures are also required under this ASU. Salisbury does not expect this ASU to have a significant impact on its financial position or results of operations.

Table of Contents

In April 2011, the FASB issued ASU 2011-03, "Reconsideration of Effective Control for Repurchase Agreements." The objective of this ASU is to improve the accounting for repurchase agreements and other agreements that both entitle and obligate a transferor to repurchase or redeem financial assets before their maturity. This ASU prescribes when an entity may or may not recognize a sale upon the transfer of financial assets subject to repurchase agreements. The guidance in this ASU is effective for the first interim or annual period beginning on or after December 15, 2011. Early adoption is not permitted.

In December 2010, the FASB issued Accounting Standards Update ("ASU") 2010-28, "Intangibles - Goodwill and Other." This ASU addresses when to perform step 2 of the goodwill impairment test for reporting units with zero or negative carrying amounts. For public entities, the amendments in this ASU are effective for fiscal years and interim periods beginning after December 15, 2010.

In December 2010, the FASB issued ASU 2010-29, "Disclosure of Supplementary Pro Forma Information for Business Combinations." This ASU addresses diversity in practice about the interpretation of the pro forma revenue and earnings disclosure requirements for business combinations. This ASU is effective prospectively for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2010.

In July 2010, the FASB issued ASU 2010-20, "Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses." This ASU is created to provide financial statement users with greater transparency about an entity's allowance for credit losses and the credit quality of its financing receivables. This ASU is intended to provide additional information to assist financial statement users in assessing the entity's credit risk exposures and evaluating the adequacy of its allowance for credit losses. The amendments in this ASU are effective as of the end of a reporting period for interim and annual reporting periods ending on or after December 15, 2010. The disclosures about activity that occurs during a reporting period are effective for interim and annual reporting periods beginning on or after December 15, 2010.

In April 2010, the FASB issued ASU 2010-18, "Effect of a Loan Modification When the Loan is Part of a Pool That is Accounted for as a Single Asset." As a result of this ASU, modifications of loans that are accounted for within a pool under Subtopic 310-30 do not result in the removal of those loans from the pool even if the modification of those loans would otherwise be considered a troubled debt restructuring. An entity continues to be required to consider whether the pool of assets in which the loan is included is impaired if expected cash flows for the pool change. The amendments in this ASU are effective for modifications of loans accounted for within pools under Subtopic 310-30 occurring in the first interim or annual period ending on or after July 15, 2010, with the amendments to be applied prospectively. This ASU did not have a significant impact on Salisbury's financial position or results of operations.

In January 2010, the FASB issued ASU 2010-06, "Improving Disclosures about Fair Value Measurements." The ASU requires disclosing the amounts of significant transfers in and out of Level 1 and 2 of the fair value hierarchy and describing the reasons for the transfers. The disclosures are effective for reporting periods beginning after December 15, 2009. Salisbury adopted ASU 2010-06 as of January 1, 2010. The required disclosures are included in Note 10, "Fair Value Measurements," to the consolidated Financial Statements. Additionally, disclosures of the gross purchases, sales, issuances and settlements activity in the Level 3 of the fair value measurement hierarchy are effective for interim and annual reporting periods beginning after December 15, 2010.

In March 2010, the FASB issued ASU 2010-11, "Scope Exception Related to Embedded Credit Derivatives." The ASU clarifies that certain embedded derivatives, such as those contained in certain securitizations, CDOs and structured notes, should be considered embedded credit derivatives subject to potential bifurcation and separate fair value

accounting. The ASU allows any beneficial interest issued by a securitization vehicle to be accounted for under the fair value option at transition. The requirements are effective July 1, 2010. This standard did not have a significant impact on Salisbury's financial position or results of operations.

Table of Contents

NOTE 2 - SECURITIES

The composition of securities is as follows:

(in thousands)	Amortized cost (1)	Gross un-realized gains	Gross un-realized losses	Fair value
June 30, 2011				
Available-for-sale				
U.S. Treasury notes	$4,999	$373	$-	$5,372
U.S. Government Agency notes	22,573	422	-	22,995
Municipal bonds	51,388	459	(3,062)	48,785
Mortgage backed securities				
U.S. Government Agencies	30,895	938	(1)	31,832
Collateralized mortgage obligations				
U.S. Government Agencies	8,052	41	-	8,093
Non-agency	16,624	499	(282)	16,841
SBA bonds	4,062	80	-	4,142
Corporate bonds	1,095	28	-	1,123
Preferred Stock	20	204	-	224
Total securities available-for-sale	$139,708	$3,044	$(3,345)	$139,407
Held-to-maturity				
Mortgage backed security	$53	$1	$-	$54
Non-marketable securities				
Federal Home Loan Bank of Boston stock	$6,032	$-	$-	$6,032
December 31, 2010				
Available-for-sale				
U.S. Treasury notes	$4,999	$197	$-	$5,196
U.S. Government Agency notes	41,590	380	(92)	41,878
Municipal bonds	51,330	139	(5,371)	46,098
Mortgage backed securities				
U.S. Government Agencies	19,190	566	(20)	19,736
Collateralized mortgage obligations				
U.S. Government Agencies	9,283	29	(1)	9,311
Non-agency	19,002	714	(599)	19,117
SBA bonds	4,831	70	-	4,901
Corporate bonds	1,089	41	-	1,130
Preferred Stock	20	35	-	55
Total securities available-for-sale	$151,334	$2,171	$(6,083)	$147,422
Held-to-maturity				
Mortgage backed security	$56	$2	$-	$58
Non-marketable securities				
Federal Home Loan Bank of Boston stock	$6,032	$-	$-	$6,032

(1) Net of other-than-temporary impairment write-down recognized in earnings.

Salisbury did not sell any securities available-for-sale during the three month periods ended June 30, 2011 and 2010.

Included in non-agency Collateralized Mortgage Obligations ("CMOs") are eight securities issued by Wells Fargo with an aggregate amortized cost basis and fair value of $5,671,000 and $5,867,000, respectively, that exceeded 10% of shareholders' equity as of June 30, 2011.

Table of Contents

The following table summarizes, for all securities in an unrealized loss position, including debt securities for which a portion of other-than-temporary impairment has been recognized in other comprehensive income, the aggregate fair value and gross unrealized loss of securities that have been in a continuous unrealized loss position as of the date presented:

	Less than 12 Months		12 Months or Longer		Total	
(in thousands)	Fair value	Unrealized losses	Fair value	Unrealized losses	Fair value	Unrealized losses
June 30, 2011						
Available-for-sale						
U.S. Government Agency notes	$-	$-	$-	$-	$-	$-
Municipal Bonds	14,410	630	15,321	2,432	29,731	3,062
Mortgage backed securities	58	1	-	-	58	1
Collateralized mortgage obligations						
U.S. Government Agencies	-	-	-	-	-	-
Non-agency	1,004	15	2,068	151	3,072	166
Total temporarily impaired securities	15,472	646	17,389	2,583	32,861	3,229
Other-than-temporarily impaired securities						
Collateralized mortgage obligations						
Non-agency	3,186	71	750	45	3,936	116
Total temporarily impaired and other-than-temporarily impaired securities	$18,658	$717	$18,139	$2,628	$36,797	$3,345

Salisbury evaluates securities for Other Than Temporary Impairment ("OTTI") where the fair value of a security is less than its amortized cost basis at the balance sheet date. As part of this process, Salisbury considers its intent to sell each debt security and whether it is more likely than not that it will be required to sell the security before its anticipated recovery. If either of these conditions is met, Salisbury recognizes an OTTI charge to earnings equal to the entire difference between the security's amortized cost basis and its fair value at the balance sheet date. For securities that meet neither of these conditions, an analysis is performed to determine if any of these securities are at risk for OTTI.

The following summarizes, by security type, the basis for evaluating if the applicable securities were OTTI at June 30, 2011.

U.S Government Agency notes, U.S. Government Agency mortgage-backed securities and U.S. Government Agency CMOs: The contractual cash flows are guaranteed by U.S. government agencies and U.S. government-sponsored enterprises. Changes in fair values are a function of changes in investment spreads and interest rate movements and not changes in credit quality. Management expects to recover the entire amortized cost basis of these securities. Furthermore, Salisbury does not intend to sell these securities and it is not more likely than not that Salisbury will be required to sell these securities before recovery of their cost basis, which may be maturity. Therefore, management does not consider these securities to be OTTI at June 30, 2011.

Municipal bonds: Contractual cash flows are performing as expected. The decline in fair values at June 30, 2011 as compared with December 31, 2010, is primarily due to an increase in interest rates and risk premium spreads for

municipal bonds in 2011 compared to 2010. Late in 2010 and continuing into 2011 the municipal bond market experienced significant price declines as uncertainty about the health of local and state government finances caused investors to exit the market. Salisbury purchased substantially all of these securities during 2006-to-2008 as bank qualified, insured, AAA rated general obligation or revenue bonds. Salisbury's portfolio is mostly comprised of tax-exempt general obligation bonds or public-purpose revenue bonds for schools, municipal offices, sewer infrastructure and fire houses, for small towns and municipalities across the United States. In the wake of the financial crisis, most monoline bond insurers had their ratings downgraded or withdrawn because of excessive exposure to insurance for collateralized debt obligations. Salisbury has performed credit underwriting reviews of certain issuers, including those that have had their ratings withdrawn and those that are insured by insurers that have had their ratings withdrawn, to assess their default risk. For all completed reviews pass credit risk ratings have been assigned. Management believes that unrealized losses on its municipal bonds are a function of interest rate movements and changes in investor spreads for credit sensitive securities. Management expects to recover the entire amortized cost basis of these securities. Salisbury does not intend to sell these securities and it is not more likely than not that Salisbury will be required to sell these securities before recovery of their cost basis, which may be maturity. Management does not consider these securities to be OTTI at June 30, 2011.

Table of Contents

Non-agency CMOs: Salisbury performed a detailed cash flow analysis of its non-agency CMOs at June 30, 2011 to assess whether any of the securities were OTTI. Salisbury uses third party provided cash flow forecasts of each security based on a variety of market driven assumptions and securitization terms, including prepayment speed, default or delinquency rate, and default severity for losses including interest, legal fees, property repairs, expenses and realtor fees, that, together with the loan amount are subtracted from collateral sales proceeds to determine severity. In 2009 Salisbury determined that five non-agency CMO securities reflected OTTI and recognized losses for deterioration in credit quality of $1,128,000. Salisbury judged these five securities not to have additional OTTI and all other CMO securities not to be OTTI as of June 30, 2011. It is possible that future loss assumptions could change necessitating Salisbury to recognize future OTTI for further deterioration in credit quality. Salisbury does not intend to sell these securities and it is not more likely than not that Salisbury will be required to sell these securities before recovery of their cost basis.

The following table presents activity related to credit losses recognized into earnings on the non-agency CMOs held by Salisbury for which a portion of an OTTI charge was recognized in accumulated other comprehensive income:

Six months ended June 30 (in thousands)	2011	2010
Balance, beginning of period	$1,128	$1,128
Credit component on debt securities in which OTTI was not previously recognized	-	-
Balance, end of period	$1,128	$1,128

Federal Home Loan Bank of Boston (“FHLBB”): The Bank is a member of the FHLBB. The FHLBB is a cooperative that provides services, including funding in the form of advances, to its member banking institutions. As a requirement of membership, the Bank must own a minimum amount of FHLBB stock, calculated periodically based primarily on its level of borrowings from the FHLBB. No market exists for shares of the FHLBB and therefore, they are carried at par value. FHLBB stock may be redeemed at par value five years following termination of FHLBB membership, subject to limitations which may be imposed by the FHLBB or its regulator, the Federal Housing Finance Board, to maintain capital adequacy of the FHLBB. While the Bank currently has no intentions to terminate its FHLBB membership, the ability to redeem its investment in FHLBB stock would be subject to the conditions imposed by the FHLBB. In 2008, the FHLBB announced to its members that it is focusing on preserving capital in response to ongoing market volatility including the extension of a moratorium on excess stock repurchases and in 2009 announced the suspension of its quarterly dividends. On February 22, 2011, the FHLBB announced the resumption of modest quarterly cash dividends to its members through 2011 and on June 27, 2011 the FHLBB announced that its excess stock pool will be discontinued effective June 28, 2011, and designating December 28, 2011, as the required stock purchase date. Based on the capital adequacy and the liquidity position of the FHLBB, management believes there is no impairment related to the carrying amount of the Bank’s FHLBB stock as of June 30, 2011. Further deterioration of the FHLBB’s capital levels may require the Bank to deem its restricted investment in FHLBB stock to be OTTI. If evidence of impairment exists in the future, the FHLBB stock would reflect fair value using either observable or unobservable inputs. The Bank will continue to monitor its investment in FHLBB stock.

NOTE 3 - LOANS

The composition of loans receivable and loans held-for-sale is as follows:

(in thousands)	June 30, 2011	December 31, 2010
Residential 1-4 family	$182,764	$173,931
Residential 5+ multifamily	3,068	2,889
Construction of residential 1-4 family	8,046	8,949
Home equity credit	33,657	34,164

Residential real estate	227,535	219,933
Commercial	79,976	75,495
Construction of commercial	4,502	7,312
Commercial real estate	84,478	82,807
Farm land	5,767	5,690
Vacant land	12,687	12,979
Real estate secured	330,467	321,409
Commercial and industrial	30,060	25,123
Municipal	2,768	4,338
Consumer	4,599	4,677
Loans receivable, gross	367,894	355,547
Deferred loan origination fees and costs, net	939	822
Allowance for loan losses	(3,979)	(3,920)
Loans receivable, net	$364,854	$352,449
Loans held-for-sale		
Residential 1-4 family	$146	$1,184

Table of Contents

Concentrations of Credit Risk

Salisbury's loans consist primarily of residential and commercial real estate loans located principally in northwestern Connecticut and nearby New York and Massachusetts towns, which constitute Salisbury's service area. Salisbury offers a broad range of loan and credit facilities to borrowers in its service area, including residential mortgage loans, commercial real estate loans, construction loans, working capital loans, equipment loans, and a variety of consumer loans, including home equity lines of credit, and installment and collateral loans. All residential and commercial mortgage loans are collateralized by first or second mortgages on real estate. The ability of single family residential mortgage loan and consumer loan borrowers to honor their repayment commitments is generally dependent on the level of overall economic activity within the market area and real estate values. The ability of commercial borrowers to honor their repayment commitments is dependent on the general economy as well as the health of the real estate economic sector in Salisbury’s market area.

Credit Quality

The composition of loans receivable by risk rating grade is as follows:

June 30, 2011 (in thousands)	Pass	Special mention	Substandard	Doubtful	Loss	Total
Residential 1-4 family	$163,345	$13,210	$6,209	$-	$-	$182,764
Residential 5+ multifamily	2,538	530	-	-	-	3,068
Construction of residential 1-4 family	3,971	416	3,659	-	-	8,046
Home equity credit	30,960	1,465	1,232	-	-	33,657
Residential real estate	200,814	15,621	11,100	-	-	227,535
Commercial	60,896	6,101	12,979	-	-	79,976
Construction of commercial	3,840	191	471	-	-	4,502
Commercial real estate	64,736	6,292	13,450	-	-	84,478
Farm land	3,139	1,779	849	-	-	5,767
Vacant land	7,603	894	4,190	-	-	12,687
Real estate secured	276,292	24,586	29,589	-	-	330,467
Commercial and industrial	20,030	8,315	1,715	-	-	30,060
Municipal	2,768	-	-	-	-	2,768
Consumer	4,330	196	73	-	-	4,599
Loans receivable, gross	$303,420	$33,097	$31,377	$-	$-	$367,894

Credit quality segments of loans receivable by risk rating grade are as follows:

June 30, 2011 (in thousands)	Pass	Special mention	Substandard	Doubtful	Loss	Total
Performing loans	$303,151	$33,097	$-	$-	$-	$336,248
Potential problem loans	-	-	15,154	-	-	15,154
Troubled debt restructurings – accruing	269	-	1,661	-	-	1,930
Troubled debt restructuring - non-accrual	-	-	7,691	-	-	7,691
All other non-accrual loans	-	-	6,871	-	-	6,871
Impaired loans	269	-	16,223	-	-	16,492

Loans receivable, gross	$303,420	$33,097	$31,377	$-	$-	$367,894

Potential problem loans are performing loans risk rated substandard that are not classified as impaired. Impaired loans are loans for which it is probable that Salisbury will not be able to collect all principal and interest amounts due according to the contractual terms of the loan agreements.

The components of impaired loans are as follows:

(in thousands)	June 30, 2011	December 31, 2010
Troubled debt restructurings – accruing	$1,930	$5,330
Troubled debt restructuring - non-accrual	7,691	4,254
All other non-accrual loans	6,871	5,791
Impaired loans	$16,492	$15,375
Commitments to lend additional amounts to impaired borrowers	$-	$-

Table of Contents

The composition of loans receivable delinquency status by risk rating grade is as follows:

June 30, 2011 (in thousands)	Pass	Special mention	Substandard	Doubtful	Loss	Total
Current	$301,609	$30,228	$20,121	$-	$-	$351,958
Past due 001-029	1,726	1,950	3,571	-	-	7,247
Past due 030-059	69	731	376	-	-	1,176
Past due 060-089	16	188	925	-	-	1,129
Past due 090-179	-	-	1,038	-	-	1,038
Past due 180+	-	-	5,346	-	-	5,346
Loans receivable, gross	$303,420	$33,097	$31,377	$-	$-	$367,894

The composition of loans receivable by delinquency status is as follows:

		Past due							
June 30, 2011 (in thousands)	Current	1-29 days	30-59 days	60-89 days	90-179 days	180 days and over	30 days and over	Accruing 90 days and over	Non-accrual
Residential 1-4 family	$ 176,930	$ 3,748	$ 445	$ 303	$ 504	$ 834	$ 2,086	$ -	$ 6,288
Residential 5+ multifamily	2,794	-	274	-	-	-	274	-	-
Residential 1-4 family construction	8,046	-	-	-	-	-	-	-	-
Home equity credit	32,850	645	37	86	14	24	161	-	200
Residential real estate	220,620	4,393	756	389	518	858	2,521	-	6,488
Commercial	76,815	1,717	283	125	495	541	1,444	-	3,134
Construction of commercial	4,482	21	-	-	-	-	-	-	-
Commercial real estate	81,297	1,738	283	125	495	541	1,444	-	3,134
Farm land	5,334	433	-	-	-	-	-	-	-
Vacant land	8,645	16	64	565	-	3,397	4,026	-	3,933
Real estate secured	315,896	6,580	1,103	1,079	1,013	4,796	7,991	-	13,555
Commercial and industrial	28,842	590	20	34	25	550	629	-	1,008
Municipal	2,768	-	-	-	-	-	-	-	-
Consumer	4,452	77	53	16	-	-	69	-	-
Loans receivable, gross	$ 351,958	$ 7,247	$ 1,176	$ 1,129	$ 1,038	$ 5,346	$ 8,689	$ -	$ 14,563

Allowance for Loan Losses

Changes in the allowance for loan losses are as follows:

Three months ended June 30   Six months ended June 30

(in thousands)	Beginning balance	Provision	Charge-offs	Reco-veries	Ending balance	Beginning balance	Provision	Charge-offs	Reco-veries	Ending balance
2011 Periods										
Residential	$1,462	$ 139	$ (20)	$2	$ 1,583	$1,504	$ 197	$ (121)	$3	$ 1,583
Commercial	1,343	(9)	(96)	-	1,238	1,132	282	(175)	-	1,239
Land	296	(25)	-	-	271	392	(42)	(79)	-	271
Real estate	3,101	105	(116)	2	3,092	3,028	437	(375)	3	3,093
Commercial & industrial	531	79	(89)	-	521	541	69	(89)	-	521
Municipal	55	(27)	-	-	28	51	(23)	-	-	28
Consumer	167	70	(159)	13	91	164	86	(179)	19	92
Unallocated	124	123	-	-	247	136	111	-	-	245
Totals	$3,978	$ 350	$ (364)	$15	$ 3,979	$3,920	$ 680	$ (643)	$22	$ 3,979
2010 Periods										
Totals	$3,649	$ 260	$ (149)	$8	$ 3,768	$3,473	$ 440	$ (159)	$14	$ 3,768

Table of Contents

The composition of loans receivable and the allowance for loan losses is as follows:

June 30, 2011 (in thousands)	Collectively evaluated Loan balance	Collectively evaluated Allowance	Individually evaluated Loan balance	Individually evaluated Allowance	Total portfolio Loan Balance	Total portfolio Allowance
Residential 1-4 family	$177,466	$749	$5,299	$427	$182,764	$1,176
Residential 5+ multifamily	3,068	20	-	-	3,068	20
Construction of residential 1-4 family	4,387	16	3,659	-	8,046	16
Home equity credit	33,418	371	239	-	33,657	371
Residential real estate	218,339	1,156	9,197	427	227,535	1,583
Commercial	71,895	908	8,081	280	79,976	1,188
Construction of commercial	4,502	51	-	-	4,502	51
Commercial real estate	76,397	959	8,081	280	84,478	1,239
Farm land	5,767	56	-	-	5,767	56
Vacant land	8,599	101	4,088	114	12,687	215
Real estate secured	309,102	2,272	21,366	821	330,467	3,093
Commercial and industrial	28,623	390	1,437	131	30,060	521
Municipal	2,768	28	-	-	2,768	28
Consumer	4,476	46	122	46	4,599	92
Unallocated allowance	-	-	-	-	-	245
Totals	$344,969	$2,736	$22,925	$998	$367,894	$3,979

The credit quality segments of loans receivable and the allowance for loan losses are as follows:

June 30, 2011 (in thousands)	Collectively evaluated Loan balance	Collectively evaluated Allowance	Individually evaluated Loan balance	Individually evaluated Allowance	Total portfolio Loan Balance	Total portfolio Allowance
Performing loans	$335,708	$2,386	$540	$46	$336,247	$2,432
Potential problem loans	9,261	350	5,893	462	15,155	812
Impaired loans	-	-	16,492	490	16,492	490
Unallocated allowance	-	-	-	-	-	245
Totals	$344,969	$2,736	$22,925	$998	$367,894	$3,979

Certain data with respect to impaired loans individually evaluated is as follows:

June 30, 2011 (in thousands)	Impaired loans with specific allowance Loan balance Book	Note	Average	Specific Allowance	Income recognized	Impaired loans with no specific allowance Loan balance Book	Note	Average	Income recognized
Residential 1-4 family	$ 889	$ 922	$ 1,473	$ 142	$ 9	$ 5,400	$ 5,459	$ 4,453	$ 42
Home equity credit	-	-	-	-	-	200	203	265	1
Residential real estate	889	922	1,473	142	9	5,600	5,662	4,718	43
Commercial	2,671	2,790	2,657	154	61	2,123	2,581	2,137	14
Vacant land	669	774	735	64	-	3,263	3,627	3,215	-
Real estate secured	4,229	4,486	4,865	360	70	10,986	11,870	10,070	57

Commercial and industrial	154	155	333	130	2	1,123	1,744	778	1
Consumer	-	-	-	-	-	-	143	29	-
Totals	$ 4,383	$ 4,641	$ 5,198	$ 490	$ 72	$ 12,109	$ 13,757	$ 10,877	$ 58

Table of Contents

NOTE 4 - MORTGAGE SERVICING RIGHTS

Loans serviced for others are not included in the Consolidated Balance Sheets. The balance of loans serviced for others and the fair value of mortgage servicing rights are as follows:

June 30, (in thousands)	2011	2010
Residential mortgage loans serviced for others	$101,584	$78,119
Fair value of mortgage servicing rights	760	517

Changes in mortgage servicing rights are as follows:

	Three months		Six months	
Periods ended June 30, (in thousands)	2011	2010	2011	2010
Loan Servicing Rights				
Balance, beginning of period	$701	$424	$683	$427
Originated	29	84	105	112
Amortization (1)	(56)	(43)	(114)	(74)
Balance, end of period	674	465	674	465
Valuation Allowance				
Balance, beginning of period	(8)	(28)	(10)	(30)
(Increase) decrease in impairment reserve (1)	(17)	4	(15)	6
Balance, end of period	(25)	(24)	(25)	(24)
Loan servicing rights, net	$649	$441	$649	$441

(1) Amortization expense and changes in the impairment reserve are recorded in loan servicing fee income.

NOTE 5 - PLEDGED ASSETS

The following securities and loans were pledged to secure public and trust deposits, securities sold under agreements to repurchase, FHLBB advances and credit facilities available.

in thousands)	June 30, 2011	December 31, 2010
Securities available-for-sale (at fair value)	$61,388	$62,764
Loans receivable	118,290	114,424
Total pledged assets	$179,678	$177,188

At June 30, 2011, securities were pledged as follows: $46.2 million to secure public deposits and Treasury Tax and Loan deposits, $12.4 million to secure repurchase agreements and $2.8 million to secure FHLBB advances. Loans receivable were pledged to secure FHLBB advances and credit facilities.

NOTE 6 – EARNINGS PER SHARE

The calculation of earnings per share is as follows:

	Three months		Six months	
Periods ended June 30, (in thousands, except per share amounts)	2011	2010	2011	2010
Net income	$882	$878	$1,825	$1,473

Preferred stock net accretion	6	5	11	10
Preferred stock dividends paid	110	110	220	220
Net income available to common shareholders	$766	$763	$1,594	$1,243
Weighted average common stock outstanding – basic	1,689	1,687	1,688	1,687
Weighted average common and common equivalent stock outstanding- diluted	1,689	1,687	1,689	1,687
Earnings per common and common equivalent share				
Basic	$0.45	$0.45	$0.94	$0.74
Diluted	0.45	0.45	0.94	0.74

Table of Contents

NOTE 7 – SHAREHOLDERS' EQUITY

Capital Requirements

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

Quantitative measures established by regulation to ensure capital adequacy require Salisbury and the Bank to maintain minimum amounts and ratios (set forth in the table below) of Tier 1 capital (as defined) to average assets (as defined) and total and Tier 1 capital (as defined) to risk-weighted assets (as defined). Management believes, as of June 30, 2011, that Salisbury and the Bank meet all of their capital adequacy requirements.

The Bank was classified, as of its most recent notification, as "well capitalized". The Bank's actual regulatory capital position and minimum capital requirements as defined "To Be Well Capitalized Under Prompt Corrective Action Provisions" and "For Capital Adequacy Purposes" are as follows:

	Actual		For Capital Adequacy Purposes		To be Well Capitalized Under Prompt Corrective Action Provisions	
(dollars in thousands)	Amount	Ratio	Amount	Ratio	Amount	Ratio
June 30, 2011						
Total Capital (to risk-weighted assets)						
Salisbury	$52,605	13.93 %	$30,207	8.0 %	n/a	-
Bank	43,002	11.19	30,754	8.0	$38,443	10.0 %
Tier 1 Capital (to risk-weighted assets)						
Salisbury	48,513	12.85	15,104	4.0	n/a	-
Bank	38,910	10.12	15,377	4.0	23,066	6.0
Tier 1 Capital (to average assets)						
Salisbury	48,513	8.45	23,407	4.0	n/a	-
Bank	38,910	6.79	23,361	4.0	29,201	5.0
June 30, 2010						
Total Capital (to risk-weighted assets)						
Salisbury	$50,393	13.39 %	$30,108	8.0 %	n/a	-
Bank	40,817	10.88	30,042	8.0	$37,553	10.0 %
Tier 1 Capital (to risk-weighted assets)						
Salisbury	46,582	12.38	15,054	4.0	n/a	-
Bank	37,006	9.86	15,613	4.0	23,420	6.0

Tier 1 Capital (to average assets)						
Salisbury	46,582	8.35	22,318	4.0	n/a	-
Bank	37,006	6.63	22,318	4.0	27,898	5.0

Restrictions on Cash Dividends to Common Shareholders

Salisbury's ability to pay cash dividends is dependent on the Bank's ability to pay cash dividends to Salisbury. There are certain restrictions on the payment of cash dividends and other payments by the Bank to Salisbury. Under Connecticut law, the Bank cannot declare a cash dividend except from net profits, defined as the remainder of all earnings from current operations. The total of all cash dividends declared by the Bank in any calendar year shall not, unless specifically approved by the Banking Commissioner, exceed the total of its net profits of that year combined with its retained net profits of the preceding two years.

Federal Reserve Board (“FRB”) Supervisory Letter SR 09-4, February 24, 2009, revised March 27, 2009, notes that, as a general matter, the Board of Directors of a Bank Holding Company (“BHC”) should inform the Federal Reserve and should eliminate, defer, or significantly reduce dividends if (1) net income available to shareholders for the past four quarters, net of dividends previously paid during that period, is not sufficient to fully fund the dividends; (2) the prospective rate of earnings retention is not consistent with capital needs and overall current and prospective financial condition; or (3) the BHC will not meet, or is in danger of not meeting, its minimum regulatory capital adequacy ratios. Moreover, a BHC should inform the Federal Reserve reasonably in advance of declaring or paying a dividend that exceeds earnings for the period (e.g., quarter) for which the dividend is being paid or that could result in a material adverse change to the BHC capital structure.

Table of Contents

Further restrictions on cash dividends are imposed on Salisbury because of Salisbury's participation in the United States Treasury Department's ("Treasury") Troubled Asset Relief Program's Capital Purchase Program (the "CPP"). These preclude the payment of any common stock cash dividends if Salisbury is not paying the preferred stock dividend. Additionally, the common stock dividend may not be increased without prior approval from the Treasury for the first three years Salisbury is a CPP participant unless all CPP preferred shares are redeemed or transferred to third parties.

Preferred Stock

In March 2009, Salisbury issued to the Treasury $8,816,000 of Preferred Stock under the CPP.

The Preferred Stock qualifies as Tier 1 capital for regulatory purposes and ranks senior to the Common Stock. The Preferred Stock pays a cumulative dividend of 5 percent per annum for the first five years it is outstanding and thereafter at a rate of 9 percent per annum. The Preferred Stock is non-voting, other than voting rights on matters that could adversely affect the Preferred Stock. The Preferred Stock is redeemable at one hundred percent of the issue price plus any accrued and unpaid dividends.

As part of the CPP, Salisbury issued to the Treasury a 10-year Warrant to purchase 57,671 shares of Common Stock at an exercise price of $22.93 per share. If the Warrant were fully exercised, Salisbury estimates that the ownership percentage of the current shareholders would be diluted by approximately 3.3% percent.

NOTE 8 – PENSION AND OTHER BENEFITS

The components of net periodic cost for Salisbury's insured noncontributory defined benefit retirement plan were as follows:

	Three months		Six months	
Periods ended June 30, (in thousands)	2011	2010	2011	2010
Service cost	$95	$74	$191	$174
Interest cost on benefit obligation	93	89	187	180
Expected return on plan assets	(106)	(98)	(212)	(198)
Amortization of prior service cost	-	-	-	-
Amortization of net loss	17	16	33	34
Net periodic benefit cost	$99	$81	$199	$190

Salisbury's 401(k) Plan contribution expense was $96,000 and $41,000, respectively, for the three month periods ended June 30, 2011 and 2010. Other post-retirement benefit obligation expense for endorsement split-dollar life insurance arrangements was $12,000 and $12,000, respectively, for the three month periods ended June 30, 2011 and 2010.

NOTE 9 - COMPREHENSIVE INCOME

Comprehensive income includes net income and any changes in equity from non-owner sources that are not recorded in the income statement (such as changes in net unrealized gains (losses) on securities). The purpose of reporting comprehensive income is to report a measure of all changes in equity of an enterprise that result from recognized transactions and other economic events of the period other than transactions with owners in their capacity as owners.

17

Table of Contents

The components of comprehensive income are as follows:

	Three months		Six months	
Periods ended June 30, (in thousands)	2011	2010	2011	2010
Net income	$882	$878	$1,825	$1,473
Other comprehensive income				
Net unrealized gains on securities available-for-sale	2,762	1,570	3,600	2,545
Reclassification of net realized gains in net income	-	1	11	1
Unrealized gains on securities available-for-sale	2,762	1,571	3,611	2,546
Income tax expense	(939)	(534)	(1,228)	(866)
Unrealized gains on securities available-for-sale, net of tax	1,823	1,037	2,383	1,680
Pension plan income	17	17	33	35
Income tax expense	(6)	(6)	(11)	(12)
Pension plan income, net of tax	11	11	22	23
Other comprehensive income, net of tax	1,834	1,048	2,405	1,703
Comprehensive income	$2,716	$1,926	$4,230	$3,176

The components of accumulated other comprehensive losses are as follows:

June 30, (in thousands)	2011	2010
Unrealized losses on securities available-for-sale, net of tax	$(199)	$(2,151)
Unrecognized pension plan expense, net of tax	(1,165)	(1,224)
Accumulated other comprehensive loss, net	$(1,364)	$(3,375)

NOTE 10 – FAIR VALUE OF ASSETS AND LIABILITIES

Salisbury uses fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. Securities available-for-sale are recorded at fair value on a recurring basis. Additionally, from time to time, other assets are recorded at fair value on a nonrecurring basis, such as loans held for sale, collateral dependent impaired loans, property acquired through foreclosure or repossession and mortgage servicing rights. These nonrecurring fair value adjustments typically involve the application of lower-of-cost-or-market accounting or write-downs of individual assets.

Salisbury adopted ASC 820-10, “Fair Value Measurements and Disclosures,” which provides a framework for measuring fair value under generally accepted accounting principles, in 2008. This guidance permitted Salisbury the irrevocable option to elect fair value for the initial and subsequent measurement for certain financial assets and liabilities on a contract-by-contract basis. Salisbury did not elect fair value treatment for any financial assets or liabilities upon adoption.

In accordance with ASC 820-10, Salisbury groups its financial assets and financial liabilities measured 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.

GAAP specifies a hierarchy of valuation techniques based on whether the types of valuation information (“inputs”) are observable or unobservable. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect Salisbury’s market assumptions. These two types of inputs have created the following fair value hierarchy

- Level 1. Quoted prices in active markets for identical assets. Valuations for assets and liabilities traded in active exchange markets, such as the New York Stock Exchange. Level 1 also includes U.S. Treasury, other U.S. Government and agency mortgage-backed securities that are traded by dealers or brokers in active markets. Valuations are obtained from readily available pricing sources for market transactions involving identical assets or liabilities.

- Level 2. Significant other observable inputs. Valuations for assets and liabilities traded in less active dealer or broker markets. Valuations are obtained from third party pricing services for identical or comparable assets or liabilities.

- Level 3. Significant unobservable inputs. Valuations for assets and liabilities that are derived from other methodologies, including option pricing models, discounted cash flow models and similar techniques, and are not based on market exchange, dealer, or broker traded transactions. Level 3 valuations incorporate certain assumptions and projections in determining the fair value assigned to such assets and liabilities.

Table of Contents

A financial instrument's level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement.

The following is a description of valuation methodologies for assets recorded at fair value, including the general classification of such assets and liabilities pursuant to the valuation hierarchy.

- Securities available-for-sale. Securities available-for-sale are recorded at fair value on a recurring basis. Level 1 securities include exchange-traded equity securities. Level 2 securities include debt securities with quoted prices, which are traded less frequently than exchange-traded instruments, whose value is determined using matrix pricing with inputs that are observable in the market or can be derived principally from or corroborated by observable market data. This category generally includes obligations of the U.S. Treasury and U.S. government-sponsored enterprises, mortgage-backed securities, collateralized mortgage obligations, municipal bonds, SBA bonds, corporate bonds and certain preferred equities. Level 3 is for positions that are not traded in active markets or are subject to transfer restrictions, valuations are adjusted to reflect illiquidity and/or non-transferability, and such adjustments are generally based on available market evidence. In the absence of such evidence, management's best estimate is used. Subsequent to inception, management only changes level 3 inputs and assumptions when corroborated by evidence such as transactions in similar instruments, completed or pending third-party transactions in the underlying investment or comparable entities, subsequent rounds of financing, recapitalization and other transactions across the capital structure, offerings in the equity or debt markets, and changes in financial ratios or cash flows.

- Collateral dependent loans that are deemed to be impaired are valued based upon the fair value of the underlying collateral less costs to sell. Such collateral primarily consists of real estate and, to a lesser extent, other business assets. Management may adjust appraised values to reflect estimated market value declines or apply other discounts to appraised values resulting from its knowledge of the property. Internal valuations are utilized to determine the fair value of other business assets. Collateral dependent impaired loans are categorized as Level 3.

- Other real estate owned acquired through foreclosure or repossession is adjusted to fair value less costs to sell upon transfer out of loans. Subsequently, it is carried at the lower of carrying value or fair value less costs to sell. Fair value is generally based upon independent market prices or appraised values of the collateral. Management adjusts appraised values to reflect estimated market value declines or apply other discounts to appraised values for unobservable factors resulting from its knowledge of the property, and such property is categorized as Level 3.

Assets measured at fair value are as follows:

	Fair value measurements using			Assets at
(in thousands)	Level 1	Level 2	Level 3	fair value
June 30, 2011				
Assets at fair value on a recurring basis				
Securities available-for-sale	$224	$139,183	$-	$139,407
Assets at fair value on a non-recurring basis				
Collateral dependent impaired loans	-	-	3,894	3,894
Other real estate owned	-	-	400	400

Table of Contents

Changes in Level 3 assets measured at fair value are as follows:

(in thousands)	Securities available-for-sale	Collateral dependent impaired Loans	Other real estate owned	Level 3 assets at fair value
Balance, December 31, 2010	$ -	$4,768	$557	$5,325
Gains and losses (realized/unrealized)				
Included in earnings	-	-	-	-
Included in other comprehensive income	-	-	-	-
Principal pay-downs of securities, net of accretion	-	-	-	-
Write-down of other real estate owned			(157)	(157)
Transfers in and/or out of Level 3	-	(874)	-	(874)
Balance, June 30, 2011	$ -	$3,894	$400	$4,294
Amount of total gains or losses for the period attributable to the change in unrealized gains or losses				
Relating to assets still held at the reporting date	$ -	$-	$-	$-

Carrying values and estimated fair values of financial instruments are as follows:

	June 30, 2011		December 31, 2010	
(in thousands)	Carrying Value	Estimated fair value	Carrying Value	Estimated fair value
Financial Assets				
Cash and due from banks	$43,944	$43,944	$26,908	$26,908
Interest bearing time deposits with other banks	-	-	5,000	5,000
Securities available-for-sale	139,407	139,407	147,422	147,422
Security held-to-maturity	53	54	56	58
Federal Home Loan Bank stock	6,032	6,032	6,032	6,032
Loans held-for-sale	146	147	1,184	1,193
Loans receivable net	364,854	364,992	352,449	351,628
Accrued interest receivable	2,086	2,086	2,132	2,132
Financial Liabilities				
Demand (non-interest-bearing)	78,985	78,985	71,565	71,565
Demand (interest-bearing)	63,651	63,651	63,258	63,258
Money market	113,316	113,316	77,089	77,089
Savings and other	93,341	93,341	93,324	93,324
Certificates of deposit	109,736	109,750	125,053	125,172
Deposits	459,029	459,043	430,289	430,408
FHLBB advances	55,460	60,341	72,812	78,317
Repurchase agreements	12,359	12,359	13,190	13,190
Accrued interest payable	307	307	435	435

The carrying amounts of financial instruments shown in the above table are included in the consolidated balance sheets under the indicated captions.

Table of Contents

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 of Salisbury and its subsidiary should be read in conjunction with Salisbury's Annual Report on Form 10-K for the year ended December 31, 2010.

BUSINESS

Salisbury Bancorp, Inc. ("Salisbury"), a Connecticut corporation, formed in 1998, is a bank holding company for Salisbury Bank and Trust Company ("Bank"), a Connecticut-chartered and Federal Deposit Insurance Corporation (the "FDIC") insured commercial bank headquartered in Lakeville, Connecticut. Salisbury's principal business consists of the business of the Bank. The Bank, formed in 1848, is engaged in customary banking activities, including general deposit taking and lending activities to both retail and commercial markets, and trust and wealth advisory services. The Bank conducts its banking business from eight full-service offices in the towns of Canaan, Lakeville, Salisbury and Sharon, Connecticut, South Egremont and Sheffield, Massachusetts, Millerton and Dover Plains, New York, and its trust and wealth advisory services from offices in Lakeville, Connecticut.

Application of Critical Accounting Policies

Salisbury’s consolidated financial statements follow GAAP as applied to the banking industry in which it operates. Application of these principles requires management to make estimates, assumptions and judgments that affect the amounts reported in the financial statements. These estimates, assumptions and judgments are based on information available as of the date of the financial statements; accordingly, as this information changes, the financial statements could reflect different estimates, assumptions and judgments and as such have a greater possibility of producing results that could be materially different than originally reported. Estimates, assumptions and judgments are necessary when assets and liabilities are required to be recorded at fair value, when a decline in the value of an asset not carried at fair value warrants an impairment write-down or valuation reserve to be established, or when an asset or liability needs to be recorded contingent upon a future event.

Salisbury’s significant accounting policies are presented in Note 1 of Notes to Consolidated Financial Statements in Salisbury's 2010 Annual Report on Form 10-K for the period ended December 31, 2010 and, along with this Management’s Discussion and Analysis, provide information on how significant assets are valued in the financial statements and how those values are determined. Management believes that the following accounting estimates are the most critical to aid in fully understanding and evaluating Salisbury’s reported financial results, and they require management’s most difficult, subjective or complex judgments, resulting from the need to make estimates about the effect of matters that are inherently uncertain.

The allowance for loan losses represents management’s estimate of credit losses inherent in the loan portfolio. Determining the amount of the allowance for loan losses is considered a critical accounting estimate because it requires significant judgment and the use of estimates related to the amount and timing of expected future cash flows on impaired loans, estimated losses on pools of homogeneous loans based on historical loss experience, and consideration of current economic trends and conditions, all of which may be susceptible to significant change. The loan portfolio also represents the largest asset type on the balance sheet. Note 1 of Notes to Consolidated Financial Statements in Salisbury's 2010 Annual Report on Form 10-K for the period ended December 31, 2010 describes the methodology used to determine the allowance for loan losses. In addition, a discussion of the factors driving changes in the amount of the allowance for loan losses are included in the “Provision and Allowance for Loan Losses” section of Management’s Discussion and Analysis of this Quarterly Report.

Management evaluates goodwill and identifiable intangible assets for impairment annually using valuation techniques that involve estimates for discount rates, projected future cash flows and time period calculations, all of which are susceptible to change based on changes in economic conditions and other factors. Future events or changes in the estimates, which are used to determine the carrying value of goodwill and identifiable intangible assets or which otherwise adversely affects their value or estimated lives could have a material adverse impact on the results of operations.

Management evaluates securities for other-than-temporary impairment giving consideration to the extent to which the fair value has been less than cost, estimates of future cash flows, delinquencies and default severity, and the intent and ability of Salisbury to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value. The consideration of the above factors is subjective and involves estimates and assumptions about matters that are inherently uncertain. Should actual factors and conditions differ materially from those used by management, the actual realization of gains or losses on investment securities could differ materially from the amounts recorded in the financial statements.

Table of Contents

The determination of the obligation and expense for pension and other postretirement benefits is dependent on certain assumptions used in calculating such amounts. Key assumptions used in the actuarial valuations include the discount rate, expected long-term rate of return on plan assets and rates of increase in compensation and health care costs. Actual results could differ from the assumptions and market driven rates may fluctuate. Significant differences in actual experience or significant changes in the assumptions may materially affect the future pension and other postretirement obligations and expense.

RESULTS OF OPERATIONS

For the three month periods ended June 30, 2011 and 2010

Overview

Net income available to common shareholders was $766,000, or $0.45 per common share, for its second quarter ended June 30, 2011 (second quarter 2011), compared with $828,000, or $0.49 per common share, for the first quarter ended March 31, 2011 (first quarter 2011), and $763,000, or $0.45 per common share, for the second quarter ended June 30, 2010 (second quarter 2010).

Net income available to common shareholders for second quarter 2011 and 2010 is net of preferred stock dividends and accretion of $116,000 and $115,000, respectively.

- Earnings per common share decreased $0.04, or 8.2%, to $0.45 versus first quarter 2011, and were unchanged versus second quarter 2010.
  - Tax equivalent net interest income increased $110,000, or 2.3%, versus first quarter 2011, and increased $290,000, or 6.3%, versus second quarter 2010.
- Provision for loan losses was $350,000, versus $330,000 for first quarter 2011 and $260,000 for second quarter 2010. Net loan charge-offs were $349,000, versus $272,000 for first quarter 2011 and $141,000 for second quarter 2010.
- Non-interest income decreased $171,000, or 12.2%, versus first quarter 2011 and was relatively unchanged versus second quarter 2010.
- Non-interest expense increased $8,000, or 0.2%, versus first quarter 2011 and $187,000, or 4.4%, versus second quarter 2010.
- Non-performing assets increased $3.3 million to $15.0 million, or 2.55% of total assets, versus first quarter 2011 and $3.5 million versus second quarter 2010. Loans receivable 30 days or more past due decreased $3.4 million to $8.7 million, or 2.4% of gross loans, versus first quarter 2011 and increased $613,000 versus second quarter 2010.

Net Interest Income

Tax equivalent net interest income increased $290,000, or 6.3%, to $4.9 million for second quarter 2011 as compared with second quarter 2010, and the net interest margin increased 15 basis points to 3.56% from 3.41%, for the respective periods.

22

Table of Contents

The following table sets forth the components of Salisbury's tax-equivalent net interest income and yields on average interest-earning assets and interest-bearing funds.

Three months ended June 30, (dollars in thousands)	Average Balance 2011	Average Balance 2010	Income / Expense 2011	Income / Expense 2010	Average Yield / Rate 2011	Average Yield / Rate 2010
Loans (a)	$ 368,420	$ 338,175	$ 4,695	$ 4,601	5.10 %	5.44 %
Securities (c)(d)	138,950	166,413	1,544	1,852	4.44	4.45
FHLBB stock	6,032	6,032	6	-	0.42	-
Short term funds (b)	35,111	27,339	33	38	0.38	0.56
Total earning assets	548,513	537,959	6,278	6,491	4.58	4.83
Other assets	34,074	32,319				
Total assets	$ 582,587	$ 570,278				
Interest-bearing demand deposits	$ 62,468	$ 54,397	107	153	0.68	1.13
Money market accounts	108,975	75,002	159	105	0.58	0.56
Savings and other	96,739	89,168	97	142	0.40	0.64
Certificates of deposit	112,932	140,311	466	726	1.66	2.07
Total interest-bearing deposits	381,114	358,878	829	1,126	0.87	1.26
Repurchase agreements	9,466	9,730	12	19	0.50	0.78
FHLBB advances	55,605	75,087	562	761	4.00	4.01
Total interest-bearing liabilities	446,185	443,695	1,403	1,906	1.26	1.72
Demand deposits	75,703	68,907				
Other liabilities	3,734	3,662				
Shareholders' equity	56,965	54,014				
Total liabilities & shareholders' equity	$ 582,587	$ 570,278				
Net interest income			$ 4,875	$ 4,585		
Spread on interest-bearing funds					3.32	3.11
Net interest margin (e)					3.56	3.41

(a) Includes non-accrual loans.
(b) Includes interest-bearing deposits in other banks and federal funds sold.
(c) Average balances of securities are based on historical cost.
(d) Includes tax exempt income of $259,000 and $260,000, respectively for 2011 and 2010 on tax-exempt securities whose income and yields are calculated on a tax-equivalent basis.
(e) Net interest income divided by average interest-earning assets.

The following table sets forth the changes in FTE interest due to volume and rate.

Three months ended June 30, (in thousands)	2011 versus 2010		
Change in interest due to	Volume	Rate	Net
Interest-earning assets			
Loans	$398	$(304)	$94
Securities	(305)	(3)	(308)

FHLBB stock	-	6	6
Short term funds	9	(14)	(5)
Total	102	(315)	(213)
Interest-bearing liabilities			
Deposits	(50)	(247)	(297)
Repurchase agreements	-	(7)	(7)
FHLBB advances	(197)	(2)	(199)
Total	(247)	(256)	(503)
Net change in net interest income	$349	$(59)	$290

Interest Income

Tax equivalent interest income decreased $213,000, or 3.3%, to $6.3 million for second quarter 2011 as compared with second quarter 2010. Loan income increased $94,000, or 2.0%, primarily due to a $30.2 million, or 8.9%, increase in average loans offset by a 34 basis points decline in the average loan yield.

Tax equivalent securities income decreased $308,000, or 16.6%, for second quarter 2011 as compared with second quarter 2010, as a result of a $27.5 million, or 16.5%, decrease in average volume and a 1 basis points decline in the average yield. The decline in volume resulted from the redeployment of some of the cash flows from securities maturities, principal payments and calls, into new loans. Changes in securities yields resulted from the effect of changes in market interest rates on securities purchases, calls of agency bonds and prepayments of mortgage backed securities.

Table of Contents

Income from short term funds decreased $5,000 for second quarter 2011 as compared with second quarter 2010 as a result of an 18 basis points decline in the average yield offset in part by a $7.8 million increase in the average balance.

Interest Expense

Interest expense decreased $503,000, or 26.4%, to $1.4 million for second quarter 2011 as compared with second quarter 2010.

Interest on deposit accounts and retail repurchase agreements decreased $304,000, or 26.6%, as a result of a lower average rate, down 39 basis points to 0.86%, offset in part by a $21.9 million, or 6.0%, increase in the average balance. The lower average rate resulted from the effect of lower market interest rates on rates paid and changes in product mix. The higher average volume resulted from deposit growth.

Interest expense on FHLBB borrowings decreased $199,000 as a result of lower average borrowings, down $19.5 million, and average borrowing rate, down 1 basis point as compared with second quarter 2010. The decline in advances resulted from scheduled maturities that were not replaced with new advances.

Provision and Allowance for Loan Losses

The provision for loan losses was $350,000 for second quarter 2011, compared with $260,000 for second quarter 2010. Net loan charge-offs were $349,000 and $141,000, for the respective quarters. The following table sets forth changes in the allowance for loan losses and other selected statistics:

	Three months		Six months	
Periods ended June 30, (dollars in thousands)	2011	2010	2011	2010
Balance, beginning of period	$3,978	$3,649	$3,920	$3,473
Provision (benefit) or loan losses	350	260	680	440
Charge-offs				
Real estate mortgages	(116)	(135)	(375)	(135)
Commercial & industrial	(89)	-	(89)	-
Consumer	(159)	(14)	(179)	(24)
Total charge-offs	(364)	(149)	(643)	(159)
Recoveries				
Real estate mortgages	2	-	3	-
Commercial & industrial	-	-	-	-
Consumer	13	8	19	14
Total recoveries	15	8	22	14
Net (charge-offs) recoveries	(349)	(141)	(621)	(145)
Balance, end of period	$3,979	$3,768	$3,979	$3,768
Loans receivable, gross			$367,894	$345,205
Non-performing loans			14,563	11,520
Accruing loans past due 30-89 days			1,482	830
Ratio of allowance for loan losses:				
to loans receivable, gross			1.08%	1.09%
to non-performing loans			27.31	32.71
Ratio of non-performing loans to loans receivable, gross			3.96	3.33
Ratio of accruing loans past due 30-89 days to loans receivable, gross			0.40	0.24

Reserve coverage at June 30, 2011, as measured by the ratio of allowance for loan losses to gross loans, remained substantially unchanged at 1.08%, as compared with 1.09% at March 31, 2011, 1.10% at December 31, 2010 and 1.09% a year ago at June 30, 2010. During the first six months of 2011 non-performing loans (non-accrual loans and accruing loans past-due 90 days or more) increased $3.0 million to $14.6 million, or 3.96% of gross loans receivable, while accruing loans past due 30-89 days increased $652,000 to $1.5 million, or 0.40% of gross loans receivable. See “Financial Condition – Loan Credit Quality” for further discussion and analysis.

Table of Contents

The credit quality segments of loans receivable and the allowance for loan losses are as follows:

	June 30, 2011		December 31, 2010	
(in thousands)	Loan Balance	Allowance	Loan Balance	Allowance
Performing loans	$335,708	$2,386	$332,240	$2,500
Potential problem loans	9,261	350	5,744	169
Collectively evaluated	344,969	2,736	337,984	2,669
Performing loans	540	46	-	-
Potential problem loans	5,893	462	2,188	330
Impaired loans	16,492	490	15,375	785
Individually evaluated	22,925	998	17,563	1,115
Unallocated allowance	-	245	-	136
Totals	$367,894	$3,979	$355,547	$3,920

The allowance for loan losses represents management's estimate of the probable credit losses inherent in the loan portfolio as of the reporting date. The allowance is increased by provisions charged to earnings and by recoveries of amounts previously charged off, and is reduced by loan charge-offs. Loan charge-offs are recognized when management determines a loan or portion of a loan to be uncollectible. The allowance for loan losses is computed by segregating the portfolio into three components: (1) loans collectively evaluated for impairment: general loss allocation factors for non-impaired loans are segmented into pools of loans based on similar risk characteristics such as loan product, collateral type and loan-to-value, loan risk rating, historical loss experience, delinquency factors and other similar economic indicators, (2) loans individually evaluated for impairment: individual loss allocations for loans deemed to be impaired based on discounted cash flows or collateral value, and (3) unallocated: general loss allocations for other environmental factors.

Impaired loans and certain potential problem loans, where warranted, are individually evaluated for impairment. Impairment is measured for each individual loan, or for a borrower's aggregate loan exposure, using either the fair value of the collateral if the loan is collateral dependent or the present value of expected future cash flows discounted at the loan's effective interest rate. An allowance is established when the collateral value or discounted cash flows of the loan is lower than the carrying value of that loan.

The component of the allowance for loan losses for loans collectively evaluated for impairment is estimated by stratifying loans into segments and credit risk ratings and applying management's general loss allocation factors. The general loss allocation factors are based on expected loss experience adjusted for historical loss experience and other qualitative factors, including levels/trends in delinquencies; trends in volume and terms of loans; effects of changes in risk selection and underwriting standards and other changes in lending policies, procedures and practices; experience/ability/depth of lending management and staff; and national and local economic trends and conditions. The qualitative factors are determined based on the various risk characteristics of each loan segment. There were no significant changes in Salisbury's policies or methodology pertaining to the general component of the allowance for loan losses during the quarter ended June 30, 2011.

The unallocated component of the allowance is maintained to cover uncertainties that could affect management's estimate of probable losses. It reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating allocated and general reserves in the portfolio.

Determining the adequacy of the allowance at any given period is difficult, particularly during deteriorating or uncertain economic periods, and management must make estimates using assumptions and information that are often

subjective and changing rapidly. The review of the loan portfolio is a continuing event in light of a changing economy and the dynamics of the banking and regulatory environment. Should the economic climate deteriorate, borrowers could experience difficulty and the level of non-performing loans, charge-offs and delinquencies could rise and require increased provisions. In management's judgment, Salisbury remains adequately reserved both against total loans and non-performing loans at June 30, 2011.

Management’s loan risk rating assignments, loss percentages and specific reserves are subjected annually to an independent credit review by an external firm. In addition, the bank is examined annually on a rotational process by one of its two primary regulatory agencies, the FDIC and CTDOB. As an integral part of their examination process, the FDIC and CTDOB review the Bank's credit risk ratings and allowance for loan losses. The Bank was examined by the CTDOB April 2010 and by the FDIC in May 2011.

Table of Contents

Non-interest income

The following table details the principal categories of non-interest income.

Three months ended June 30, (dollars in thousands)	2011	2010	2011 vs. 2010	
Trust and wealth advisory fees	$596	$491	$105	21.38 %
Service charges and fees	522	499	23	4.61
Gains on sales of mortgage loans, net	59	122	(63)	(51.64)
Mortgage servicing, net	(5)	27	(32)	(118.52)
Gains on securities, net	-	1	(1)	(100.00)
Other	58	89	(31)	(34.83)
Total non-interest income	$1,230	$1,229	$1	(0.08)%

Non-interest income for second quarter 2011 decreased $171,000 versus first quarter 2011 and was substantially unchanged versus second quarter 2010. Trust and Wealth Advisory revenues decreased $71,000 versus first quarter 2011 and increased $105,000 versus second quarter 2010. First quarter 2011 included seasonal revenue related to annual income tax filings. The year-over-year revenue increase results from both growth in managed assets and higher asset valuations. Service charges and fees increased $23,000 versus first quarter 2011 and $23,000 versus second quarter 2010. Income from sales and servicing of mortgage loans decreased $111,000 versus first quarter 2011 and $95,000 versus second quarter 2010, due to a drop in fixed rate residential mortgage loan sales and a $16,000 mortgage servicing valuation impairment charge. Mortgage loans sales totaled $2.4 million for second quarter 2011, $6.1 million for first quarter 2011 and $5.2 million for second quarter 2010. The surge in residential mortgage loan refinancing precipitated by the decline in mortgage lending rates to historically low levels in mid-2010 has diminished. Gains on securities represent the accretion of discounts on called securities. Other income for second quarter 2010 included a gain from the sale of real estate.

Non-interest expense

The following table details the principal categories of non-interest expense.

Three months ended June 30, (dollars in thousands)	2011	2010	2011 vs. 2010	
Salaries	$1,657	$1,668	$(11)	(0.66)%
Employee benefits	650	586	64	10.92
Premises and equipment	568	495	73	14.75
Data processing	285	363	(78)	(21.49)
Professional fees	300	455	(155)	(34.07)
Collections and OREO	243	21	222	1057.14
FDIC insurance	182	182	-	-
Marketing and community contributions	92	59	33	55.93
Amortization of intangible assets	56	56	-	-
Other	399	360	39	10.83
Non-interest expense	$4,432	$4,245	$187	4.41 %

Non-interest expense for second quarter 2011 increased $8,000 versus first quarter 2011 and $187,000 versus second quarter 2010. Salaries decreased $11,000 versus second quarter 2010 due to changes in staffing levels and mix. Employee benefits increased $64,000 versus second quarter 2010 due to higher health benefits expense, caused by year over year premium increases and higher staff utilization, and higher 401K Plan expense due to the implementation of a Safe Harbor Plan, offset in part by lower pension plan expense. Premises and equipment

decreased $15,000 versus first quarter 2011 and increased $73,000 versus second quarter 2010. The year-over-year increase is due primarily to several facilities renovations, equipment replacement and the Sheffield branch relocation to a larger office in August 2010. Data processing decreased $92,000 versus first quarter 2011 and $78,000 versus second quarter 2010 due to a second quarter 2011 one-time vendor rebate. Professional fees increased $23,000 versus first quarter 2011 and decreased $155,000 versus second quarter 2010 due to reduced spending on audit, consulting, legal and investment management services. Collections and OREO increased $119,000 versus first quarter 2011 and $222,000 versus second quarter 2010. Second quarter 2011 included $105,000 of OREO write-downs. FDIC insurance decreased $41,000 versus first quarter 2011 and was unchanged versus second quarter 2010. Other operating expenses increased $44,000 and decreased $39,000, respectively, versus first quarter 2011 and second quarter 2010 due to increases in printing, telecommunications, consumable supplies and other administrative and operational expense categories.

Income taxes

The effective income tax rates for second quarter 2011, first quarter 2011 and second quarter 2010 were 17.18%, 18.27% and 16.38%, respectively. Fluctuations in the effective tax rate result from changes in the mix of taxable and tax exempt income. Salisbury's effective tax rate is generally less than the 34% federal statutory rate due to holdings of tax-exempt municipal bonds and bank owned life insurance.

Salisbury did not incur Connecticut income tax in 2011 or 2010, other than minimum state income tax, as a result of its utilization of Connecticut tax legislation that permits banks to shelter certain mortgage income from the Connecticut corporation business tax through the use of a special purpose entity called a Passive Investment Company ("PIC"). In accordance with this legislation, in 2004 the Bank formed a PIC, SBT Mortgage Service Corporation. Salisbury's income tax provision reflects the full impact of the Connecticut legislation. Salisbury does not expect to pay other than minimum state income tax in the foreseeable future unless there is a change in the State of Connecticut corporate tax law.

For the six month periods ended June 30, 2011 and 2010

Overview

Net income available to common shareholders was $1,594,000, or $0.94 per common share, for the six month period ended June 30, 2011 (year-to-date 2011) compared with $1,243,000, or $0.74 per common share, for the six month period ended June 30, 2010 (year-to-date 2010).

Net income available to common shareholders for year-to-date 2011 and year-to-date 2010 is net of preferred stock dividends and accretion of $231,000 and $230,000, respectively.

Net Interest Income

Tax equivalent net interest income increased $759,000, or 8.6%, to $9.6 million for year-to-date 2011 as compared with year-to-date 2010, and the net interest margin increased 23 basis points to 3.56% from 3.33%, for the respective periods.

The following table sets forth the components of Salisbury's tax-equivalent net interest income and yields on average interest-earning assets and interest-bearing funds.

Six months ended June 30,	Average Balance		Income / Expense		Average Yield / Rate	
(dollars in thousands)	2011	2010	2011	2010	2011	2010
Loans (a)	$365,445	$335,774	$9,360	$9,088	5.13 %	5.41 %
Securities (c)(d)	142,066	158,444	3,137	3,597	4.42	4.54
FHLBB stock	6,032	6,032	12	-	0.42	-
Short term funds (b)	29,463	34,006	64	84	0.45	0.49
Total earning assets	543,006	534,256	12,573	12,769	4.64	4.78
Other assets	33,756	32,590				
Total assets	$576,762	$566,846				
Interest-bearing demand deposits	$62,779	$51,792	223	301	0.71	1.16
Money market accounts	96,709	70,731	269	201	0.56	0.57
Savings and other	96,100	88,410	194	285	0.41	0.64

Certificates of deposit	116,788	144,602	1,014	1,538	1.75	2.13
Total interest-bearing deposits	372,376	355,535	1,700	2,325	0.92	1.31
Repurchase agreements	10,764	11,158	27	46	0.50	0.82
FHLBB advances	59,322	75,418	1,207	1,518	4.05	4.00
Total interest-bearing liabilities	442,462	442,111	2,934	3,889	1.33	1.76
Demand deposits	74,354	67,522				
Other liabilities	3,864	3,726				
Shareholders' equity	56,082	53,487				
Total liabilities & shareholders' equity	$576,762	$566,846				
Net interest income			$9,639	$8,880		
Spread on interest-bearing funds					3.31	3.02
Net interest margin (e)					3.56	3.33

(a) Includes non-accrual loans.
(b) Includes interest-bearing deposits in other banks and federal funds sold.
(c) Average balances of securities are based on historical cost.
(d) Includes tax exempt income of $517,000 and $519,000, respectively for the 2011 and 2010 periods on tax-exempt securities whose income and yields are calculated on a tax-equivalent basis.
(e) Net interest income divided by average interest-earning assets.

Table of Contents

The following table sets forth the changes in tax equivalent interest due to volume and rate.

Six months ended June 30, (in thousands)	2011 versus 2010		
Change in interest due to	Volume	Rate	Net
Interest-earning assets			
Loans	$782	$(510)	$272
Securities	(367)	(93)	(460)
FHLBB stock	-	12	12
Short term funds	(13)	(7)	(20)
Total	404	(598)	(194)
Interest-bearing liabilities			
Deposits	(125)	(500)	(625)
Repurchase agreements	(1)	(18)	(19)
FHLBB advances	(326)	15	(311)
Total	(452)	(503)	(955)
Net change in net interest income	$854	$(95)	$759

Interest Income

Tax equivalent interest income decreased $196,000, or 1.5%, to $12.6 million for year-to-date 2011 compared with year-to-date 2010. Loan income increased $272,000, or 3.0%, primarily due to a $29.7 million, or 8.8%, increase in average loans, offset by a lower average yield, down 28 basis points.

Tax equivalent securities income decreased $460,000, or 12.8%, for year-to-date 2011 compared with year-to-date 2010, as a result of a lower average yield, down 12 basis points, and a $16.4 million, or 10.3%, decrease in average securities. The decline in volume resulted from the redeployment of some of the cash flows from securities maturities, principal payments and calls, into new loans. Changes in securities yields resulted from the effect of changes in market interest rates on securities purchases, calls of agency bonds and prepayments of mortgage backed securities.

Income from short term funds decreased $20,000 for year-to-date 2011 as compared with year-to-date 2010 as a result of a $4.5 million decrease in average balance and a 4 basis points decrease in average yield.

Interest Expense

Interest expense decreased $955,000, or 24.6%, to $2.9 million for year-to-date 2011 as compared with year-to-date 2010.

Interest on deposit accounts and retail repurchase agreements decreased $644,000, or 27.2%, as a result of a lower average rate, down 39 basis points to 0.91%, offset in part by a $16.4 million, or 4.5%, increase in the average balance. The lower average rate was due to lower market interest rates on rates paid and changes in product mix. The higher average volume resulted from deposit growth.

Interest expense on FHLBB borrowings decreased $311,000 due to lower average borrowings, down $16.1 million, offset in part by a higher average borrowing rate, up 5 basis points, due to change in mix. The decline in advances resulted from scheduled maturities that were not replaced with new advances.

Provision and Allowance for Loan Losses

The provision for loan losses was $680,000 for year-to-date 2011, compared with $440,000 for year-to-date 2010. Net loan charge-offs were $621,000 and $145,000, for the respective periods. The increased provision for loan losses was necessitated by the increase in net charge-offs and increases in the level of impaired and potential problem loans.

Table of Contents

Non-interest income

The following table details the principal categories of non-interest income.

Six months ended June 30, (dollars in thousands)	2011	2010	2011 vs. 2010				
Trust and wealth advisory fees	$1,263	$1,036	$227		21.91	%
Service charges and fees	1,022	952	70		7.35	
Gains on sales of mortgage loans, net	192	164	28		17.07	
Mortgage servicing, net	26	60	(34	)	(56.67	)
Gains on securities, net	11	1	10		1000.00	
Other	117	146	(29	)	(19.86	)
Total non-interest income	$2,631	$2,359	$272		11.53	

Non-interest income for year-to-date 2011 increased $272,000 versus year-to-date 2010. Trust and Wealth Advisory revenues increased $227,000 versus year-to-date 2010 due to growth in managed assets and higher asset valuations. Service charges and fees increased $70,000 versus year-to-date 2010. Income from sales mortgage loans increased $28,000 versus year-to-date 2010 due to better pricing despite slightly fixed rate residential mortgage loan sales. Mortgage loans sales totaled $8.5 million for year-to-date 2011 versus $9.6 million for year-to-date 2010. Income from mortgage loan servicing of mortgage loans decreased $34,000 versus year-to-date 2010 due to a $16,000 2011 mortgage servicing valuation impairment charge and higher mortgage rights amortization expense, despite higher servicing fees. Gains on securities represent the accretion of discounts on called securities. Other income for year-to-date 2010 included a gain from the sale of real estate.

Non-interest expense

The following table details the principal categories of non-interest expense.

Six months ended June 30, (dollars in thousands)	2011	2010	2011 vs. 2010			
Salaries	$3,386	$3,239	$147		4.54	%
Employee benefits	1,283	1,216	67		5.51	
Premises and equipment	1,151	1,011	140		13.85	
Data processing	662	772	(110	)	(14.25	)
Professional fees	577	857	(280	)	(32.67	)
FDIC insurance	405	354	51		14.41	
Collections and OREO	367	43	324		753.49	
Marketing and community contributions	160	121	39		32.23	
Amortization of intangible assets	111	111	-		-	
Other	754	833	(79	)	(9.48	)
Non-interest expense	$8,856	$8,557	$299		3.49	%

Non-interest expense for year-to-date 2011 increased $299,000 versus year-to-date 2010. Salaries increased $147,000 versus year-to-date 2010 due to changes in staffing levels and mix. Employee benefits increased $67,000 versus year-to-date 2010 due to higher health benefits expense, caused by year over year premium increases and higher staff utilization, and higher 401K Plan expense due to the implementation of a Safe Harbor Plan, offset in part by lower pension plan expense. Premises and equipment increased $140,000 versus year-to-date 2010 due primarily to several facilities renovations, equipment replacement and the Sheffield branch relocation to a larger office in August 2010. Data processing decreased $110,000 versus year-to-date 2010 mostly due to a 2011 vendor rebate. Professional fees decreased $280,000 versus year-to-date 2010 due to reduced spending on audit, consulting, legal and investment

management services, and the reclassification of certain collection related legal expenses. Expenses related to collections and OREO increased $324,000 versus year-to-date 2010. Year-to-date 2011 included $163,000 of OREO write-downs, OREO carrying costs, and collection related legal and appraisal services. FDIC insurance increased $51,000 versus year-to-date 2010. Other operating expenses decreased $79,000 versus year-to-date 2010.

Income taxes

The effective income tax rate for year-to-date 2011 was 17.75%, compared with 14.56% for year-to-date 2010. Fluctuations in the effective tax rate result from changes in the mix of taxable and tax exempt income. Salisbury's effective tax rate is generally less than the 34% federal statutory rate due to holdings of tax-exempt municipal bonds and bank owned life insurance.

Table of Contents

FINANCIAL CONDITION

Overview

Total assets were $588 million at June 30, 2011, up $13 million from December 31, 2010. Loans receivable, net, were $365 million at June 30, 2011, up $13 million, or 3.7%, from December 31, 2010. Non-performing assets were $15.0 million at June 30, 2011, up $4.3 million from $10.7 million at December 31, 2010. Reserve coverage, as measured by the ratio of the allowance for loan losses to gross loans, was 1.08%, 1.10% and 1.09%, at June 30, 2011, December 31, 2010 and June 30, 2010, respectively. Deposits were $459 million, up $29 million from $430 million at December 31, 2010.

At June 30, 2011, book value and tangible book value per common share were $29.17 and $22.68, respectively. Salisbury's Tier 1 leverage and total risk-based capital ratios were 8.45% and 13.93%, respectively, and above the "well capitalized" limits as defined by the FRB.

Securities and Short Term Funds

During year-to-date 2011, securities decreased $8 million to $145 million, and FHLBB advances decreased $17 million, while cash and cash-equivalents (interest-bearing deposits with other banks, money market funds and federal funds sold) increased $12 million to $44 million as Salisbury increased its liquidity position in light of historically low interest rates and growth in volatile deposits.

Salisbury evaluates securities for OTTI where the fair value of a security is less than its amortized cost basis at the balance sheet date. As part of this process, Salisbury considers its intent to sell each debt security and whether it is more likely than not that it will be required to sell the security before its anticipated recovery. If either of these conditions is met, Salisbury recognizes an OTTI charge to earnings equal to the entire difference between the security's amortized cost basis and its fair value at the balance sheet date. For securities that meet neither of these conditions, an analysis is performed to determine if any of these securities are at risk for OTTI.

Salisbury does not intend to sell any of its securities and it is not more likely than not that Salisbury will be required to sell any of its securities before recovery of their cost basis, which may be maturity. Therefore, management does not consider any of its securities, other than the five non-agency CMO securities reflecting OTTI, to be OTTI at June 30, 2011.

In 2009 Salisbury determined that five non-agency CMO securities reflected OTTI and recognized losses for deterioration in credit quality of $1,128,000. Salisbury judged these five securities not to have additional OTTI and all other CMO securities not to be OTTI as of June 30, 2011. It is possible that future loss assumptions could change necessitating Salisbury to recognize future OTTI for further deterioration in credit quality. Salisbury does not intend to sell these securities and it is not more likely than not that Salisbury will be required to sell these securities before recovery of their cost basis.

Accumulated other comprehensive loss at June 30, 2011 included net unrealized holding losses, net of tax, of $199,000 that management deems as temporary impairment.

Loans

Net loans receivable increased $3.7 million during second quarter 2011 to $364.9 million at June 30, 2011, compared with $361.2 million at March 31, 2011, and increased $12.5 million for year-to-date 2011, compared with $352.4

million at December 31, 2010.

Table of Contents

The composition of loans receivable and loans held-for-sale is as follows:

(in thousands)	June 30, 2011	December 31, 2010
Residential 1-4 family	$182,764	$173,931
Residential 5+ multifamily	3,068	2,889
Construction of residential 1-4 family	8,046	8,949
Home equity credit	33,657	34,164
Residential real estate	227,535	219,933
Commercial	79,976	75,495
Construction of commercial	4,502	7,312
Commercial real estate	84,478	82,807
Farm land	5,767	5,690
Vacant land	12,687	12,979
Real estate secured	330,467	321,409
Commercial and industrial	30,060	25,123
Municipal	2,768	4,338
Consumer	4,599	4,677
Loans receivable, gross	367,894	355,547
Deferred loan origination fees and costs, net	939	822
Allowance for loan losses	(3,979)	(3,920)
Loans receivable, net	$364,854	$352,449
Loans held-for-sale		
Residential 1-4 family	$146	$1,184

Loan Credit Quality

The persistent weakness in the local and regional economies has continued to adversely impact the credit quality of Salisbury's loans receivable. Total impaired and potential problem loans increased $1.9 million during second quarter 2011 to $31.6 million, or 8.6% of gross loans receivable at June 30, 2011, from $29.7 million, or 8.1% of gross loans receivable at March 31, 2011, and increased $8.3 million for year-to-date 2011 from $23.3 million, or 6.6% of gross loans receivable at December 31, 2010.

The credit quality segments of loans receivable and their credit risk ratings are as follows:

(in thousands)	June 30, 2011	December 31, 2010
Pass	$303,151	$292,815
Special mention	33,097	39,415
Performing loans	336,248	332,230
Substandard	15,154	7,932
Doubtful	-	10
Potential problem loans	15,154	7,942
Pass		
Troubled debt restructured loans, accruing	269	-
Substandard		
Troubled debt restructured loans, accruing	1,661	5,330
Troubled debt restructured loans, non-accrual	7,691	4,254

All other non-accrual loans	6,871	5,791
Impaired loans	16,492	15,375
Loans receivable, gross	$367,894	$355,547

Table of Contents

Changes in impaired and potential problem loans are as follows:

	Three months ended June 30, 2011				Six months ended June 30, 2011			
	Impaired loans		Potential problem loans		Impaired loans		Potential problem loans	
(in thousands)	Non-accrual	Accruing		Total	Non-accrual	Accruing		Total
Loans placed on non-accrual status	$ 4,539	$ (2,960)	$ (1,035)	$ 544	$ 5,892	$ (2,960)	$ (2,268)	$ 664
Loan risk rating downgrades to substandard	-	-	3,632	3,632	-	-	10,763	10,763
Loan risk rating upgrades from substandard	-	-	(923)	(923)	-	-	(1,008)	(1,008)
Loan repayments	(355)	(15)	(140)	(510)	(456)	(22)	(266)	(744)
Loan charge-offs	(346)	-	-	(346)	(606)	-	-	(606)
Loans no longer classified as troubled debt restructurings	-	(417)	-	(417)	-	(417)	-	(417)
Real estate acquired in settlement of loans	-	-	-	-	(314)	-	-	(314)
Increase (decrease) in loans	$ 3,837	$ (3,392)	$ 1,534	$ 1,979	$ 4,516	$ (3,399)	$ 7,221	$ 8,338

During second quarter 2011 Salisbury downgraded the risk ratings of $3.6 million of loans to substandard, placed $4.5 million of loans on non-accrual status as a result of deteriorated payment and financial performance, charged-off $346,000 of losses resulting from collateral deficiencies. Loans placed on non-accrual status include a single $3 million construction loan for a completed residential property that is being actively marketed. Offsetting these deteriorations were loan risk rating upgrades resulting from improved performance, loan repayments and a loan restructured in 2010 whose designation as troubled debt restructured was removed due to satisfactory performance.

During the first six months of 2011 Salisbury downgraded the risk ratings of $10.8 million of loans to substandard, placed $5.9 million of loans on non-accrual status as a result of deteriorated payment and financial performance and charged-off $606,000 of losses primarily as a result of collateral deficiencies. Offsetting these deteriorations were loan risk rating upgrades resulting from improved performance, loan repayments, real estate acquired in settlement of a loan and a loan restructured in 2010 whose designation as troubled debt restructured was removed due to satisfactory performance.

Salisbury has cooperative relationships with the vast majority of its non-performing loan customers. Substantially all non-performing loans are collateralized with real estate and the repayment of such loans is largely dependent on the return of such loans to performing status or the liquidation of the underlying real estate collateral. Salisbury pursues the resolution of all non-performing loans through collections, restructures, voluntary liquidation of collateral by the borrower and, where necessary, legal action. When all attempts to work with a customer to return a loan to performing status, including restructuring the loan, are unsuccessful, Salisbury will initiate appropriate legal action seeking to acquire property by deed in lieu of foreclosure or through foreclosure, or to liquidate business assets.

Credit Quality Segments

Salisbury categorizes loans receivable into the following credit quality segments.

- Impaired loans consist of all non-accrual loans and troubled debt restructured loans, and represent loans for which it is probable that Salisbury will not be able to collect all principal and interest amounts due according to the contractual terms of the loan agreements.

- Non-accrual loans, a sub-set of impaired loans, are loans for which the accrual of interest has been discontinued because, in the opinion of management, full collection of principal or interest is unlikely.

    - Non-performing loans consist of non-accrual loans, and accruing loans past due 90 days and over that are well collateralized, in the process of collection and where full collection of principal and interest is assured. Non-performing assets consist of non-performing loans plus real estate acquired in settlement of loans.

- Troubled debt restructured loans are loans for which concessions such as reduction of interest rates, other than normal market rate adjustments, or deferral of principal or interest payments, extension of maturity dates, or reduction of principal balance or accrued interest, have been granted due to a borrower’s financial condition. Loan restructuring is employed when management believes the granting of a concession will increase the probability of the full or partial collection of principal and interest.

- Potential problem loans consist of performing loans that have been assigned a substandard credit risk rating and that are not classified as impaired.

Credit Risk Ratings

Salisbury assigns credit risk ratings to loans receivable in order to manage credit risk and to determine the allowance for loan losses. Credit risk ratings categorize loans by common financial and structural characteristics that measure the credit strength of a borrower. Salisbury's rating model has eight risk rating grades, with each grade corresponding to a progressively greater risk of default. Grades 1 through 4 are pass ratings and 5 through 8 are ratings (special mention, substandard, doubtful and loss) defined by the bank's regulatory agencies, the FDIC and CTDOB. Risk ratings are assigned to differentiate risk within the portfolio and are reviewed on an ongoing basis and revised, if needed, to reflect changes in the borrowers' current financial position and outlook, risk profiles and the related collateral and structural positions.

- Loans risk rated as "special mention" possess credit deficiencies or potential weaknesses deserving management's close attention that if left uncorrected may result in deterioration of the repayment prospects for the loans at some future date.

- Loans risk rated as "substandard" are loans where the Bank's position is clearly not protected adequately by borrower current net worth or payment capacity. These loans have well defined weaknesses based on objective evidence and include loans where future losses to the Bank may result if deficiencies are not corrected, and loans where the primary source of repayment such as income is diminished and the Bank must rely on sale of collateral or other secondary sources of collection.

- Loans risk rated as "doubtful" have the same weaknesses as substandard loans with the added characteristic that the weakness makes collection or liquidation in full, given current facts, conditions, and values, to be highly improbable. The possibility of loss is high, but due to certain important and reasonably specific pending factors, which may work to strengthen the loan, its reclassification as an estimated loss is deferred until its exact status can be determined.

- Loans risk rated as "loss" are considered uncollectible and of such little value, that continuance as Bank assets is unwarranted. This classification does not mean that the loan has absolutely no recovery or salvage value, but rather, it is not practical or desirable to defer writing off this basically worthless loan even though partial recovery may be made in the future.

Management actively reviews and tests its credit risk ratings against actual experience and engages an independent third-party to annually validate its assignment of credit risk ratings. In addition, the Bank's loan portfolio and risk ratings are examined annually on a rotating basis by its two primary regulatory agencies, the FDIC and CTDOB.

Impaired Loans

Impaired loans increased $445,000 during second quarter 2011 to $16.5 million, or 4.48% of gross loans receivable at June 30, 2011, from $16.0 million, or 4.40% of gross loans receivable at March 31, 2011, and increased $1.1 million for year-to-date 2011 from $15.4 million, or 4.32% of gross loans receivable at December 31, 2010. The components of impaired loans are as follows:

(in thousands)	June 30, 2011	December 31, 2010
Troubled debt restructurings, accruing	$1,930	$5,330
Troubled debt restructuring, non-accrual	7,691	4,254
All other non-accrual loans	6,871	5,791

Impaired loans	$16,492	$15,375

Non-Performing Assets

Non-performing assets increased $3.3 million during second quarter 2011 to $15.0 million, or 2.55% of assets at June 30, 2011, from $11.7 million, or 2.04% of assets at March 31, 2011, and increased $1.1 million for year-to-date 2011 from $10.8 million, or 1.87% of assets at December 31, 2010.

Table of Contents

The components of non-performing assets are as follows:

(in thousands)	June 30, 2011	December 31, 2010
Residential 1-4 family	$3,328	$2,534
Construction of residential 1-4 family	2,960	-
Home equity credit	200	362
Commercial	3,134	2,923
Vacant land	3,933	4,018
Real estate secured	13,555	9,837
Commercial and industrial	1,008	208
Consumer	-	-
Total non-accruing loans	14,563	10,045
Accruing loans past due 90 days and over	-	96
Total non-performing loans	14,563	10,141
Real estate acquired in settlement of loans	452	610
Total non-performing assets	$15,015	$10,751

The past due status of non-performing loans is as follows:

(in thousands)	June 30, 2011	December 31, 2010
Current	$6,410	$2,931
Past due 001-029 days	667	219
Past due 030-059 days	177	541
Past due 060-089 days	925	1,050
Past due 090-179 days	1,038	683
Past due 180 days and over	5,346	4,717
Total non-performing loans	$14,563	$10,141

At June 30, 2011, 44.0% of non-accrual loans were current with respect to loan payments, compared with 20.4% at March 31, 2011 and 28.9% at December 31, 2010. Loans past due 180 days include a $3.0 million loan secured by vacant land (residential building lots) where Salisbury has initiated a foreclosure action that is referred to in Item 1 of Part II, Legal Proceedings.

Troubled Debt Restructured Loans

Troubled debt restructured loans increased $654,000 during second quarter 2011 to $9.6 million, or 2.62% of gross loans receivable at June 30, 2011, from $9.0 million, or 2.46% of gross loans receivable at March 31, 2011, and increased $37,000 for year-to-date 2011 from $9.6 million, or 2.70% of gross loans receivable at December 31, 2010. The components of troubled debt restructured loans are as follows:

(in thousands)	June 30, 2011	December 31, 2010
Residential 1-4 family	$-	$3,377
Commercial	1,660	1,677
Real estate secured	1,660	5,054
Commercial and industrial	270	276

Accruing troubled debt restructured loans	1,930	5,330
Residential 1-4 family	4,383	552
Commercial	2,444	2,923
Vacant land	536	621
Real estate secured	7,363	4,096
Commercial and industrial	328	158
Non-accrual troubled debt restructured loans	7,691	4,254
Troubled debt restructured loans	$9,621	$9,584

Table of Contents

The past due status of troubled debt restructured loans is as follows:

(in thousands)	June 30, 2011	December 31, 2010
Current	$1,531	$4,798
Past due 001-029 days	399	375
Past due 030-059 days	-	157
Accruing troubled debt restructured loans	1,930	5,330
Current	5,966	2,585
Past due 001-029 days	667	169
Past due 030-059 days	177	378
Past due 060-089 days	536	-
Past due 090-179 days	345	346
Past due 180 days and over	-	776
Non-accrual troubled debt restructured loans	7,691	4,254
Total troubled debt restructured loans	$9,621	$9,584

At June 30, 2011, 77.9% of troubled debt restructured loans were current with respect to loan payments, as compared with 69.8% at March 31, 2011 and 77.0% at December 31, 2010.

Past Due Loans

Loans past due 30 days or more decreased $3.3 million during second quarter 2011 to $8.7 million, or 2.36% of gross loans receivable at June 30, 2011, compared with $12.0 million, or 3.31% of gross loans receivable at March 31, 2011, and have decreased $0.2 million for year-to-date 2011, compared with $8.9 million, or 2.51% of gross loans receivable at December 31, 2010.

The components of loans past due 30 days or greater are as follows:

(in thousands)	June 30, 2011	December 31, 2010
Past due 030-059 days	$999	$1,188
Past due 060-089 days	204	730
Past due 090-179 days	-	96
Accruing loans	1,203	2,014
Past due 030-059 days	177	541
Past due 060-089 days	925	1,050
Past due 090-179 days	1,038	587
Past due 180 days and over	5,346	4,716
Non-accrual loans	7,486	6,894
Total loans past due 30 days or greater	$8,689	$8,908

Potential Problem Loans

Potential problem loans increased $1.5 million during second quarter 2011 to $15.2 million, or 4.12% of gross loans receivable at June 30, 2011, compared with $13.6 million, or 3.74% of gross loans receivable at March 31, 2011, and increased $7.3 million for year-to-date 2011, compared with $7.9 million, or 2.23% of gross loans receivable at December 31, 2010.

35

Table of Contents

The components of potential problem loans are as follows:

(in thousands)	June 30, 2011	December 31, 2010
Residential 1-4 family	$3,580	$2,483
Residential 5+ multifamily	-	89
Construction of residential 1-4 family	-	75
Home equity credit	1,033	817
Residential real estate	4,613	3,464
Commercial	8,184	2,327
Construction of commercial	471	47
Commercial real estate	8,654	2,374
Farm land	849	881
Vacant land	257	249
Real estate secured	14,373	6,968
Commercial and industrial	708	897
Consumer	73	67
Potential problem loans	$15,154	$7,932

The past due status of potential problem loans is as follows:

(in thousands)	June 30, 2011	December 31, 2010
Current	$12,450	$5,757
Past due 001-029 days	2,505	1,233
Past due 030-059 days	199	357
Past due 060-089 days	-	534
Past due 090-179 days	-	51
Total potential problem loans	$15,154	$7,932

At June 30, 2011, 82.2% of potential problem loans were current with respect to loan payments, as compared with 84.4% at March 31, 2011 and 72.6% at December 31, 2010.

Management cannot predict the extent to which economic or other factors may impact such borrowers' future payment capacity, and there can be no assurance that such loans will not be placed on nonaccrual status, restructured, or require increased provision for loan losses.

Deposits and Borrowings

Deposits increased $6.6 million during second quarter 2011 to $459.0 million at June 30, 2011, compared with $452.4 million at March 31, 2011, and increased $28.7 million for year-to-date 2011 compared with $430.3 million at December 31, 2010. Retail repurchase agreements increased $4.2 million during second quarter 2011 to $12.4 million at June 30, 2011, compared with $8.2 million at March 31, 2011, and decreased $0.8 million for year-to-date 2011 compared with $13.2 million at December 31, 2010.

Federal Home Loan Bank of Boston (FHLBB) advances decreased $0.4 million during second quarter 2011 to $55.5 million at June 30, 2011, compared with $55.9 million at March 31, 2011, and decreased $17.3 million for year-to-date 2011 compared with $72.8 million at December 31, 2010. The decreases were due to amortizing advance

payments and to advance maturities that were not renewed.

Liquidity

Salisbury manages its liquidity position to ensure that there is sufficient funding availability at all times to meet both anticipated and unanticipated deposit withdrawals, loan originations and advances, securities purchases and other operating cash outflows. Salisbury's primary sources of liquidity are principal payments and maturities of securities and loans, short-term borrowings through repurchase agreements and Federal Home Loan Bank advances, net deposit growth and funds provided by operations. Liquidity can also be provided through sales of loans and available-for-sale securities.

Salisbury manages its liquidity in accordance with a liquidity funding policy, and also maintains a contingency funding plan that provide for the prompt and comprehensive response to unexpected demands for liquidity. At June 30, 2011, Salisbury's liquidity ratio, as represented by cash, short term available-for-sale securities and marketable assets to net deposits and short term unsecured liabilities, was 27.7%, down from 28.4% at December 31, 2010. Management believes Salisbury’s funding sources will meet anticipated funding needs.

Table of Contents

Operating activities for the six-month period ended June 30, 2011 provided net cash of $4.6 million. Investing activities provided net cash of $3.0 million, principally from $31.5 million in securities repayments, maturities and calls, offset by funding of $13.0 million of net loan advances and $15.0 million of securities purchases. Financing activities provided net cash of $9.3 million, principally for $28.7 million net increase in deposits, offset in part by $17.4 million of scheduled FHLB advance repayments, an $831,000 decrease in repurchase agreements and $1.2 million of cash dividends.

At June 30, 2011, Salisbury had outstanding commitments to fund new loan originations of $4.0 million and unused lines of credit of $55.5 million. Salisbury believes that these commitments can be met in the normal course of business. Salisbury believes that its liquidity sources will continue to provide funding sufficient to support operating activities, loan originations and commitments, and deposit withdrawals.

CAPITAL RESOURCES

Shareholders' equity was $58.1 million at June 30, 2011, up $3.1 million from December 31, 2010. Book value and tangible book value per common share were $29.17 and $22.68, respectively, compared with $27.37 and $20.81, respectively, at December 31, 2010. Contributing to the increase in shareholders' equity for year-to-date 2011 was net income of $1,825,000, other comprehensive income of $2,405,000 and the issuance of common stock for director fees of $28,000, less common and preferred stock dividends of $945,000 and $220,000, respectively. Other comprehensive income included unrealized gains on securities available-for-sale, net of tax, of $2,383,000 and pension plan income, net of tax, of $22,000.

Capital Requirements

Salisbury and the Bank are subject to various regulatory capital requirements administered by the federal banking agencies. Under current regulatory definitions, Salisbury and the Bank are considered to be "well capitalized" for capital adequacy purposes. As a result, the Bank pays lower federal deposit insurance premiums than banks that are not "well capitalized." Salisbury and the Bank's regulatory capital ratios are as follows:

	Well capitalized	June 30, 2011		December 31, 2010	
		Salisbury	Bank	Salisbury	Bank
Total Capital (to risk-weighted assets)	10.00 %	13.93 %	11.19 %	13.91 %	11.11 %
Tier 1 Capital (to risk-weighted assets)	6.00	12.85	10.12	12.84	10.06
Tier 1 Capital (to average assets)	5.00	8.45	6.79	8.39	6.72

A well-capitalized institution, which is the highest capital category for an institution as defined by the Prompt Corrective Action Regulations issued by the FDIC and the FRB, is one which maintains a Total Risk-Based ratio of 10% or above, a Tier 1 Risk-Based ratio of 6% or above and a Leverage ratio of 5% or above, and is not subject to any written order, written agreement, capital directive, or prompt corrective action directive to meet and maintain a specific capital level. Maintaining strong capital is essential to Salisbury's and the Bank's safety and soundness. However, the effective management of capital resources requires generating attractive returns on equity to build value for shareholders while maintaining appropriate levels of capital to fund growth, meet regulatory requirements and be consistent with prudent industry practices.

Dividends

During the six month period ended June 30, 2011 Salisbury paid $220,000 in preferred stock dividends to the U.S. Treasury's TARP CPP, and $945,000 in common stock dividends.

The Board of Directors of Salisbury declared a common stock dividend of $0.28 per common share payable on August 26, 2011 to shareholders of record on August 12, 2011. Common stock dividends, when declared, will generally be paid the last business day of February, May, August and November, although Salisbury is not obligated to pay dividends on those dates or at any other time.

Salisbury's ability to pay cash dividends is substantially dependent on the Bank's ability to pay cash dividends to Salisbury. There are certain restrictions on the payment of cash dividends and other payments by the Bank to Salisbury. Under Connecticut law the Bank cannot declare a cash dividend except from net profits, defined as the remainder of all earnings from current operations. The total of all cash dividends declared by the Bank in any calendar year shall not, unless specifically approved by the Commissioner of Banking, exceed the total of its net profits of that year combined with its retained net profits of the preceding two years.

Table of Contents

FRB Supervisory Letter SR 09-4, February 24, 2009, revised March 27, 2009, notes that, as a general matter, the board of directors of a bank holding company ("BHC") should inform the Federal Reserve and should eliminate, defer, or significantly reduce dividends if (1) net income available to shareholders for the past four quarters, net of dividends previously paid during that period, is not sufficient to fully fund the dividends; (2) the prospective rate of earnings retention is not consistent with capital needs and overall current and prospective financial condition; or (3) the BHC will not meet, or is in danger of not meeting, its minimum regulatory capital adequacy ratios. Moreover, a BHC should inform the FRB reasonably in advance of declaring or paying a dividend that exceeds earnings for the period (e.g., quarter) for which the dividend is being paid or that could result in a material adverse change to the BHC capital structure.

Further restrictions on cash dividends are imposed on Salisbury because of Salisbury's participation in the CPP. The terms upon which the preferred stock was issued to the Treasury preclude the payment of any common stock cash dividends if Salisbury is not paying the preferred stock dividend. Additionally, the common stock dividend may not be increased without prior approval from the Treasury for the second three years Salisbury is a CPP participant unless all CPP preferred shares are redeemed or transferred to third parties.

Salisbury believes that the payment of common stock cash dividends is appropriate, provided that such payment considers Salisbury's capital needs, asset quality, and overall financial condition and does not adversely affect the financial stability of Salisbury or the Bank. The continued payment of common stock cash dividends by Salisbury will be dependent on Salisbury's future core earnings, financial condition and capital needs, regulatory restrictions, and other factors deemed relevant by the Board of Directors of Salisbury.

IMPACT OF INFLATION AND CHANGING PRICES

Salisbury's consolidated financial statements are prepared in conformity with generally accepted accounting principles that require the measurement of financial condition and operating results in terms of historical dollars without considering changes in the relative purchasing power of money, over time, due to inflation. Unlike most industrial companies, virtually all of the assets and liabilities of Salisbury are monetary and as a result, interest rates have a greater impact on Salisbury's performance than do the effects of general levels of inflation, although interest rates do not necessarily move in the same direction or with the same magnitude as the prices of goods and services. Although not a material factor in recent years, inflation could impact earnings in future periods.

FORWARD-LOOKING STATEMENTS

This Form 10-Q and future filings made by Salisbury with the Securities and Exchange Commission, as well as other filings, reports and press releases made or issued by Salisbury and the Bank, and oral statements made by executive officers of Salisbury and the Bank, may include forward-looking statements relating to such matters as:

(a) assumptions concerning future economic and business conditions and their effect on the economy in general and on the markets in which Salisbury and the Bank do business; and

(b) expectations for revenues and earnings for Salisbury and the Bank.

Such forward-looking statements are based on assumptions rather than historical or current facts and, therefore, are inherently uncertain and subject to risk. For those statements, Salisbury claims the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Act of 1995.

Salisbury notes that a variety of factors could cause the actual results or experience to differ materially from the anticipated results or other expectations described or implied by such forward-looking statements. The risks and uncertainties that may effect the operation, performance, development and results of Salisbury's and the Bank's business include the following:

(a) the risk of adverse changes in business conditions in the banking industry generally and in the specific markets in which the Bank operates;

(b) changes in the legislative and regulatory environment that negatively impacts Salisbury and Bank through increased operating expenses;

(c) increased competition from other financial and non-financial institutions;

(d) the impact of technological advances; and

(e) other risks detailed from time to time in Salisbury's filings with the Securities and Exchange Commission.

Such developments could have an adverse impact on Salisbury's and the Bank's financial position and results of operations.

Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES OF MARKET RISK

Salisbury manages its exposure to interest rate risk through its Asset/Liability Management Committee ("ALCO") using risk limits and policy guidelines to manage assets and funding liabilities to produce financial results that are consistent with Salisbury's liquidity, capital adequacy, growth, risk and profitability targets. Interest rate risk is the risk of loss to future earnings due to changes in interest rates.

The ALCO manages interest rate risk using income simulation to measure interest rate risk inherent in Salisbury's financial instruments at a given point in time by showing the effect of interest rate shifts on net interest income over a 24-month horizon. In management's June 30, 2011 analysis, three of the simulations incorporate management's growth assumptions over the simulation horizons, with allowances made for loan, deposit and security product mix shifts in selected interest rate scenarios, such as movements between lower rate savings and money market deposit accounts and higher rate time deposits, and changes in the reinvestment of loan and securities cash flows. The fourth simulation incorporates management's balance sheet growth assumptions. Additionally, the simulations take into account the specific re-pricing, maturity and prepayment characteristics of differing financial instruments that may vary under different interest rate scenarios.

The ALCO reviews the simulation results to determine whether Salisbury's exposure to change in net interest income remains within established tolerance levels over the simulation horizons and to develop appropriate strategies to manage this exposure. Salisbury's tolerance levels for changes in net interest income in its income simulations varies depending on the magnitude of interest rate changes and level of risk-based capital. All changes are measured in comparison to the projected net interest income that would result from an "unchanged" rate scenario where interest rates remain stable over the forecast horizon. The ALCO also evaluates the directional trends of net interest income, net interest margin and other financial measures over the forecast horizon for consistency with its liquidity, capital adequacy, growth, risk and profitability targets.

The ALCO uses four interest rate scenarios to evaluate interest risk exposure and may vary these interest rate scenarios to show the effect of steepening or flattening changes in yield curves as well as parallel changes in interest rates. At June 30, 2011 the ALCO used the following interest rate scenarios: (1) unchanged interest rates; (2) immediately rising interest rates – immediate non-parallel upward shift in market interest rates ranging from 300 basis points for short term rates to 150 basis points for the 10-year Treasury; (3) immediately falling interest rates – immediate non-parallel downward shift in market interest rates ranging from 0 basis points for short term rates to 100 basis points for the 10-year Treasury; and (4) gradually rising interest rates – gradual non-parallel upward shift in market interest rates ranging from 400 basis points for short term rates to 185 basis points for the 10-year Treasury. Deposit rates are assumed to shift by lesser amounts due to their relative historical insensitivity to market interest rate movements. Further, deposits are assumed to have certain minimum rate levels below which they will not fall. Income simulations do not reflect adjustments in strategy that the ALCO could implement in response to rate shifts.

As of June 30, 2011 net interest income simulations indicated that the Bank's exposure to changing interest rates over the simulation horizons remained within its tolerance levels. The following table sets forth the estimated change in net interest income from an unchanged interest rate scenario over the periods indicated for changes in market interest rates using the Bank's financial instruments as of June 30, 2011:

As of June 30, 2011	Months 1-12	Months 13-24
Immediately rising interest rates (management's growth assumptions)	(12.62)%	(11.00)%
Immediately falling interest rates (management's growth assumptions)	0.40	(1.57)

Gradually rising interest rates (management's growth assumptions)	(0.25)	(2.91)

The negative exposure of net interest income to immediately and gradually rising rates as compared to the unchanged rate scenario results from a faster projected rise in the cost of funds versus income from earning assets, as relatively rate-sensitive money market and time deposits re-price faster than longer duration earning assets. The negative exposure of net interest income to immediately falling rates as compared to an unchanged rate scenario results from a greater decline in earning asset yields compared to rates paid on funding liabilities, as a result of faster prepayments on existing assets and lower reinvestment rates on future loans originated and securities purchased.

While the ALCO reviews simulation assumptions and back-tests simulation results to ensure that they are reasonable and current, income simulation may not always prove to be an accurate indicator of interest rate risk or future net interest margin. Over time, the re-pricing, maturity and prepayment characteristics of financial instruments and the composition of Salisbury's balance sheet may change to a different degree than estimated. Simulation modeling assumes Salisbury's expectation for future balance sheet growth, which is a

Table of Contents

function of the business environment and customer behavior. Another significant simulation assumption is the sensitivity of core savings deposits to fluctuations in interest rates. Income simulation results assume that changes in both core savings deposit rates and balances are related to changes in short-term interest rates. The assumed relationship between short-term interest rate changes and core deposit rate and balance changes used in income simulation may differ from the ALCO's estimates. Lastly, mortgage-backed securities and mortgage loans involve a level of risk that unforeseen changes in prepayment speeds may cause related cash flows to vary significantly in differing rate environments. Such changes could affect the level of reinvestment risk associated with cash flow from these instruments, as well as their market value. Changes in prepayment speeds could also increase or decrease the amortization of premium or accretion of discounts related to such instruments, thereby affecting interest income.

Salisbury also monitors the potential change in market value of its available-for-sale debt securities in changing interest rate environments. The purpose is to determine market value exposure that may not be captured by income simulation, but which might result in changes to Salisbury's capital and liquidity position. Results are calculated using industry-standard analytical techniques and securities data. Available-for-sale equity securities are excluded from this analysis because the market value of such securities cannot be directly correlated with changes in interest rates. The following table summarizes the potential change in market value of available-for-sale debt securities resulting from immediate parallel rate shifts:

As of June 30, 2011 (in thousands)	Rates up 100bp	Rates up 200bp
U.S. Treasury notes	$(257)	$(500)
U.S. Government agency notes	(560)	(1,301)
Municipal bonds	(3,781)	(7,522)
Mortgage backed securities	(1,019)	(2,232)
Collateralized mortgage obligations	(370)	(837)
SBA pools	(14)	(26)
Total available-for-sale debt securities	$(6,001)	$(12,418)

Item 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Salisbury's management, including its Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the design and operation of the disclosure controls and procedures as of June 30, 2011. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the disclosure controls and procedures are effective.

Disclosure controls and procedures are controls and other procedures that are designed to ensure that the information required to be disclosed in reports filed or submitted under the Securities Exchange Act of 1934 (the "Exchange Act") is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by us in our reports filed under the Exchange Act is accumulated and communicated to management, including the principle executive officer and principle financial officer, as appropriate to allow timely decisions regarding required disclosure.

In addition, based on an evaluation of its internal controls over financial reporting, no change in Salisbury's internal control over financial reporting occurred during the quarter ended June 30, 2011 that has materially affected, or is reasonably likely to materially affect, Salisbury's internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. LEGAL PROCEEDINGS

The Bank is involved in various claims and legal proceedings arising out of the ordinary course of business.

The Bank, individually and in its capacity as a former Co-Trustee of the Erling C. Christophersen Revocable Trust (the "Trust"), has been named as a defendant in litigation currently pending in the Connecticut Complex Litigation Docket in Stamford, captioned John Christophersen v. Erling Christophersen, et al., X05-CV-08-5009597S (the "First Action"). The Bank also is a counterclaim-defendant in a related mortgage foreclosure litigation also pending in the Connecticut Complex Litigation Docket in Stamford, captioned Salisbury Bank & Trust Company v. Erling C. Christophersen, et al., X05-CV-10-6005847-S (the "Foreclosure Action," together with the First Action, the "Actions"). The other parties to the Actions are John R. Christophersen; Erling C. Christophersen, individually and as Co-Trustee of the Trust; Bonnie Christophersen and Elena Dreiske, individually and as Co-Trustees of the Mildred B. Blount Testamentary Trust; People's United Bank; Law Offices of Gary Oberst, P.C.; Rhoda Rudnick; and Hinckley Allen & Snyder LLP.

Table of Contents

The Actions involve a dispute over title to certain real property located in Westport, Connecticut that was conveyed by Erling Christophersen, as grantor, to the Trust on or about August 8, 2007. Subsequent to this conveyance, the Bank loaned $3,386,609 to the Trust, which was secured by an open-end commercial mortgage in favor of the Bank on the Westport property. This mortgage is the subject of the Foreclosure Action brought by the Bank.

The gravamen of the plaintiff/counterclaim-plaintiff John Christophersen's claims in the Actions is that he has an interest in the Westport real property transferred to the Trust of which he was allegedly wrongfully divested on account of the actions of the defendants. In the Actions plaintiff seeks to quiet title to the property and to recover money damages from the defendants for the alleged wrongful divestiture of his claimed interest in the property.

In addition to the mortgage on the property, the Bank, at the time of the financing referenced above, acquired a lender's title insurance policy from the Chicago Title & Insurance Company, which is providing a defense to the Bank in the First Action under a reservation of rights. The Bank denies any wrongdoing, and is actively defending the case. The First Action presently is stayed, by Court order, pending resolution of a parallel action pending in New York Surrogate's Court to which the Bank is not a party. The Foreclosure Action remains in its early pleading stage. No discovery has been taken to date.

There are no other material pending legal proceedings, other than ordinary routine litigation incident to the registrant's business, to which Salisbury is a party or of which any of its property is subject.

Item 1A. RISK FACTORS

Not applicable.

Item 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

None

Item 3. DEFAULTS UPON SENIOR SECURITIES

None

Item 4. [REMOVED AND RESERVED]

Item 5. OTHER INFORMATION

None

Item 6. EXHIBITS

31.1	Rule 13a-14(a)/15d-14(a) Certification.
31.2	Rule 13a-14(a)/15d-14(a) Certification.
32	Section 1350 Certifications

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.

SALISBURY BANCORP, INC.

July 29, 2011	by /s/ Richard J. Cantele, Jr. Richard J. Cantele, Jr., Chief Executive Officer
July 29, 2011	by /s/ B. Ian McMahon B. Ian McMahon, Chief Financial Officer