BANCORP RHODE ISLAND INC
Form 10-Q
May 04, 2011

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**UNITED STATES**
**SECURITIES AND EXCHANGE COMMISSION**
**Washington, D.C. 20549**
**FORM 10-Q**

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

**For the quarterly period ended March 31, 2011**

**or**

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1937**

**For the transition period from __________ to __________**

**Commission File No. 001-16101**

**BANCORP RHODE ISLAND, INC.**

(Exact name of Registrant as specified in its charter)

| Rhode Island | 05-0509802 |
|---|---|
| (State or other jurisdiction of incorporation or organization) | (IRS Employer Identification No.) |

ONE TURKS HEAD PLACE, PROVIDENCE, RI 02903
(Address of principal executive offices)
(401) 456-5000
(Registrant s telephone number, including area code)
Not Applicable
(Former name, former address and former fiscal year, if changed since last report)

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 þ No o

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 during the preceding 12 months (or for such shorter period that the Registrant was required to submit and post files). Yes o No o

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.

| Large accelerated filer o | Accelerated filer þ | Non-accelerated filer o | Smaller reporting company o |
|---|---|---|---|

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes o No þ

Indicate the number of shares outstanding of each of the Issuer s classes of common stock, as of May 2, 2011:

| Common Stock Par Value $0.01 | 4,694,741 shares |
|---|---|
| (class) | (outstanding) |

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**BANCORP RHODE ISLAND, INC.**
**Quarterly Report on Form 10-Q**
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**Special Note Regarding Forward Looking Statements**

We make certain forward looking statements in this Quarterly Report on Form 10-Q and in other documents that we incorporate by reference into this report that are based upon our current expectations and projections about future events. We intend these forward looking statements to be covered by the safe harbor provisions for forward looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, and we are including this statement for purposes of these safe harbor provisions. You can identify these statements by reference to a future period or periods by our use of the words estimate, project, may, believe, intend, anticipate, plan, seek, expect and similar terms or variations Actual results may differ materially from those set forth in forward looking statements as a result of risks and uncertainties, including those detailed from time to time in our filings with the Federal Deposit Insurance Corporation ( FDIC ) and the Securities and Exchange Commission ( SEC ). Our forward looking statements do not reflect the potential impact of any future acquisitions, mergers, dispositions, joint ventures or investments we may make. We do not assume any obligation to update any forward looking statements.

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**BANCORP RHODE ISLAND, INC.**
**Consolidated Balance Sheets (unaudited)**

| | March 31, 2011 | December 31, 2010 |
|---|---|---|
| | *(In thousands)* | |
| **ASSETS:** | | |
| Cash and due from banks | $ 16,573 | $ 14,384 |
| Overnight investments | 551 | 395 |
| **Total cash and cash equivalents** | **17,124** | **14,779** |
| Available for sale securities (amortized cost of $359,299 and $357,402, respectively) | 361,579 | 360,025 |
| Stock in Federal Home Loan Bank of Boston | 16,274 | 16,274 |
| Loans and leases receivable: | | |
| Commercial loans and leases | 783,696 | 780,264 |
| Residential mortgage loans | 160,658 | 164,877 |
| Consumer and other loans | 210,094 | 210,348 |
| **Total loans and leases receivable** | **1,154,448** | **1,155,489** |
| Allowance for loan and lease losses | (18,222) | (18,654) |
| **Net loans and leases receivable** | **1,136,226** | **1,136,835** |
| Premises and equipment, net | 11,677 | 11,889 |
| Goodwill, net | 12,262 | 12,262 |
| Accrued interest receivable | 4,411 | 4,842 |
| Investment in bank-owned life insurance | 31,580 | 31,277 |
| Prepaid expenses and other assets | 15,375 | 15,576 |
| **Total assets** | **$ 1,606,508** | **$ 1,603,759** |
| **LIABILITIES:** | | |
| Deposits: | | |
| Demand deposit accounts | $ 254,291 | $ 264,274 |
| NOW accounts | 65,127 | 70,327 |
| Money market accounts | 113,126 | 96,285 |
| Savings accounts | 343,286 | 341,667 |
| Certificate of deposit accounts | 325,831 | 347,613 |
| **Total deposits** | **1,101,661** | **1,120,166** |
| Overnight and short-term borrowings | 36,068 | 40,997 |
| Wholesale repurchase agreements | 19,801 | 20,000 |
| Federal Home Loan Bank of Boston borrowings | 273,582 | 260,889 |
| Subordinated deferrable interest debentures | 13,403 | 13,403 |
| Other liabilities | 31,801 | 19,626 |
| **Total liabilities** | **1,476,316** | **1,475,081** |

| | | |
|---|---|---|
| **SHAREHOLDERS EQUITY:** | | |
| Common stock, par value $0.01 per share, authorized 11,000,000 shares: | | |
| Issued: 5,074,192 and 5,047,942 shares, respectively | 50 | 50 |
| Additional paid-in capital | 74,556 | 73,866 |
| Treasury stock, at cost: 385,950 and 373,850 shares, respectively | (12,897) | (12,527) |
| Retained earnings | 67,001 | 65,584 |
| Accumulated other comprehensive income, net | 1,482 | 1,705 |
| **Total shareholders equity** | **130,192** | **128,678** |
| **Total liabilities and shareholders equity** | $ **1,606,508** | $ **1,603,759** |

*See accompanying notes to unaudited consolidated financial statements*

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**BANCORP RHODE ISLAND, INC.**
**Consolidated Statements of Operations (unaudited)**

| | Three Months Ended March 31, | |
|---|---|---|
| | **2011** | **2010** |
| | *(In thousands, except per share data)* | |
| Interest and dividend income: | | |
| Overnight investments | $ | $ 5 |
| Mortgage-backed securities | 2,625 | 3,229 |
| Investment securities | 397 | 550 |
| Federal Home Loan Bank of Boston stock dividends | 12 | |
| Loans and leases | 14,550 | 14,568 |
| **Total interest and dividend income** | **17,584** | **18,352** |
| Interest expense: | | |
| Deposits | 1,459 | 2,278 |
| Overnight and short-term borrowings | 10 | 18 |
| Wholesale repurchase agreements | 139 | 139 |
| Federal Home Loan Bank of Boston borrowings | 2,296 | 2,665 |
| Subordinated deferrable interest debentures | 165 | 164 |
| **Total interest expense** | **4,069** | **5,264** |
| **Net interest income** | **13,515** | **13,088** |
| Provision for loan and lease losses | 1,125 | 1,600 |
| **Net interest income after provision for loan and lease losses** | **12,390** | **11,488** |
| Noninterest income: | | |
| Total other-than-temporary impairment losses on available for sale securities | | (1,592) |
| Non-credit component of other-than-temporary losses recognized in other comprehensive income | | 1,021 |
| Credit component of other-than-temporary impairment losses on available for sale securities | | (571) |
| Service charges on deposit accounts | 1,140 | 1,264 |
| Income from bank-owned life insurance | 303 | 315 |
| Loan related fees | 220 | 189 |
| Gain on sale of available for sale securities | 212 | 475 |
| Commissions on nondeposit investment products | 194 | 237 |
| Net (loss) gain on lease sales and commissions on loans originated for others | (4) | 36 |
| Other income | 267 | 370 |
| **Total noninterest income** | **2,332** | **2,315** |
| Noninterest expense: | | |

| | | | | |
|---|---|---|---|---|
| Salaries and employee benefits | | 5,934 | | 5,843 |
| Occupancy | | 907 | | 861 |
| Data processing | | 681 | | 654 |
| Professional services | | 606 | | 632 |
| FDIC insurance | | 477 | | 475 |
| Operating | | 454 | | 462 |
| Marketing | | 353 | | 258 |
| Equipment | | 276 | | 255 |
| Loan workout and other real estate owned | | 206 | | 336 |
| Loan servicing | | 144 | | 176 |
| Other expenses | | 1,231 | | 536 |
| **Total noninterest expense** | | **11,269** | | **10,488** |
| **Income before income taxes** | | **3,453** | | **3,315** |
| Income tax expense | | 1,146 | | 1,096 |
| **Net income** | $ | **2,307** | $ | **2,219** |
| **Per share data:** | | | | |
| Basic earnings per common share | $ | 0.49 | $ | 0.48 |
| Diluted earnings per common share | $ | 0.49 | $ | 0.48 |
| Cash dividends declared per common share | $ | 0.19 | $ | 0.17 |
| Weighted average common shares outstanding basic | | 4,683 | | 4,622 |
| Weighted average common shares outstanding diluted | | 4,715 | | 4,650 |

*See accompanying notes to unaudited consolidated financial statements*

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**BANCORP RHODE ISLAND, INC.**
**Consolidated Statements of Changes in Shareholders Equity (unaudited)**

| Three months ended March 31, | Common Stock | Additional Paid-in Capital | Treasury Stock | Retained Earnings | Accumulated Other Compre-hensive Income (Loss) | Total |
|---|---|---|---|---|---|---|
| | *(In thousands, expect per share data)* | | | | | |
| **2010** | | | | | | |
| Balance at December 31, 2009 | $ 50 | $ 72,783 | $ (12,309) | $ 59,012 | $ 1,125 | $ 120,661 |
| Net income | | | | 2,219 | | 2,219 |
| Other comprehensive income: | | | | | | |
| Unrealized holding gains on securities available for sale, net of taxes of ($1,213) | | | | | 2,252 | 2,252 |
| Reclassification adjustment for net gains included in net income, net of taxes of $166 | | | | | (309) | (309) |
| Non-credit portion OTTI, net of taxes of $358 | | | | | (663) | (663) |
| Total comprehensive income | | | | | | 3,499 |
| Exercise of stock options | | 220 | | | | 220 |
| Macrolease acquisition | | 211 | | | | 211 |
| Share repurchases | | | (218) | | | (218) |
| Share-based compensation | | 92 | | | | 92 |
| Dividends on common stock ($0.17 per common share) | | | | (786) | | (786) |
| Balance at March 31, 2010 | $ 50 | $ 73,306 | $ (12,527) | $ 60,445 | $ 2,405 | $ 123,679 |
| **2011** | | | | | | |
| Balance at December 31, 2010 | $ 50 | $ 73,866 | $ (12,527) | $ 65,584 | $ 1,705 | $ 128,678 |
| Net income | | | | 2,307 | | 2,307 |
| Other comprehensive income: | | | | | | |
| Unrealized holding gains on securities available for sale, net of taxes of $46 | | | | | (85) | (85) |
| Reclassification adjustment for net gains included in net income, net of taxes of $74 | | | | | (138) | (138) |
| Total comprehensive income | | | | | | 2,084 |
| Exercise of stock options | | 397 | | | | 397 |
| Share repurchases | | | (370) | | | (370) |

| | | | | | |
|---|---|---|---|---|---|
| Share-based compensation | | 153 | | | | 153 |
| Tax benefit from exercise of stock options | | 140 | | | | 140 |
| Dividends on common stock ($0.19 per common share) | | | | (890) | | (890) |
| Balance at March 31, 2011 | $ 50 | $ 74,556 | $ (12,897) | $ 67,001 | $ 1,482 | $ 130,192 |

*See accompanying notes to unaudited consolidated financial statements*

**BANCORP RHODE ISLAND, INC.**
**Consolidated Statements of Cash Flows (unaudited)**

| | Three Months Ended March 31, 2011 | 2010 |
|---|---|---|
| | (In thousands) | |
| Cash flows from operating activities: | | |
| Net income | $ 2,307 | $ 2,219 |
| Adjustments to reconcile net income to net cash provided by (used in) operating activities: | | |
| Depreciation, amortization and accretion, net | (276) | (1,444) |
| Provision for loan and lease losses | 1,125 | 1,600 |
| Income from bank-owned life insurance | (303) | (315) |
| Share-based compensation expense | 153 | 92 |
| Net loss (gain) on lease sales | 14 | (17) |
| Gain on sale of available for sale securities | (212) | (475) |
| Credit component of other-than-temporary impairment losses on available for sale securities | | 571 |
| Loss on sale of other real estate owned | | 56 |
| Proceeds from sales of leases | 5 | 907 |
| Leases originated for sale | (19) | (890) |
| Decrease in accrued interest receivable | 431 | 101 |
| Decrease in prepaid expenses and other assets | 766 | 146 |
| Decrease in other liabilities | (2,879) | (5,372) |
| Net cash provided by (used in) operating activities | 1,112 | (2,821) |
| Cash flows from investing activities: | | |
| Available for sale securities: | | |
| Purchases | (30,085) | (31,313) |
| Maturities and principal repayments | 39,128 | 41,081 |
| Proceeds from sales | 4,176 | 3,311 |
| Net increase in loans and leases | (180) | (12,368) |
| Capital expenditures for premises and equipment | (143) | (210) |
| Proceeds from sale of other real estate owned | | 345 |
| Net cash provided by investing activities | 12,896 | 846 |
| Cash flows from financing activities: | | |
| Net (decrease) increase in deposits | (18,505) | 8,787 |
| Net decrease in overnight and short-term borrowings | (5,128) | (2,320) |
| Proceeds from long-term borrowings | 89,500 | 33,700 |
| Repayment of long-term borrowings | (76,807) | (40,793) |
| Exercise of stock options | 27 | 2 |
| Tax benefit from exercise of stock options | 140 | |
| Dividends on common stock | (890) | (786) |

| | | | | |
|---|---|---|---|---|
| Net cash used in financing activities | | (11,663) | | (1,410) |
| Net increase (decrease) in cash and cash equivalents | | 2,345 | | (3,385) |
| Cash and cash equivalents at beginning of period | | 14,779 | | 20,830 |
| Cash and cash equivalents at end of period | $ | 17,124 | $ | 17,445 |
| Supplementary Disclosures: | | | | |
| Cash paid for interest | $ | 4,441 | $ | 5,749 |
| Cash paid for income taxes | | 519 | | 43 |
| Non-cash investing and financing transactions: | | | | |
| Change in accumulated other comprehensive income, net of taxes | | (223) | | 1,943 |
| Goodwill increase related to Macrolease acquisition | | | | 23 |
| Treasury stock acquisitions from shares tendered in stock option exercises | | 370 | | 218 |
| Transfer of loans to other real estate owned | | 445 | | 724 |
| Non-credit component of other-than-temporary impairment, net of taxes | | | | 663 |
| (Purchase) sale of available for sale securities not yet settled | | (15,054) | | 5,467 |

*See accompanying notes to unaudited consolidated financial statements*

**BANCORP RHODE ISLAND, INC.**
**Notes to Consolidated Financial Statements (unaudited)**

**(1) Basis of Presentation**

Bancorp Rhode Island, Inc. (the Company ), a Rhode Island corporation, is the holding company for Bank Rhode Island (the Bank ). The Company has no significant assets other than the common stock of the Bank. For this reason, substantially all of the discussion in this Quarterly Report on Form 10-Q relates to the operations of the Bank and its subsidiaries.

In preparing the consolidated financial statements, management is required to make 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. These estimates and assumptions are based on management s estimates and judgment and are evaluated on an ongoing basis using historical experiences and other factors, including the current economic environment. Estimates and assumptions are adjusted when facts and circumstances dictate. A recessionary environment, illiquid credit markets and declines in consumer spending have combined to increase the uncertainty inherent in management s estimates and assumptions. As future events cannot be determined with precision, actual results could differ significantly from management s estimates. Material estimates that are particularly susceptible to change relate to the determination of the allowance for loan and lease losses, evaluation of investments for other-than-temporary impairment, review of goodwill for impairment and income taxes.

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary, Bank Rhode Island, along with the Bank s wholly-owned subsidiaries, BRI Investment Corp. (a Rhode Island passive investment company), Macrolease Corporation (an equipment financing company), Acorn Insurance Agency, Inc. (a licensed insurance agency) and BRI Realty Corp. (a real estate holding company). All significant intercompany accounts and transactions have been eliminated in consolidation.

The unaudited interim consolidated financial statements of the Company conform to accounting principles generally accepted in the United States ( U.S. GAAP ) and prevailing practices within the banking industry and include all necessary adjustments (consisting of only normal recurring adjustments) that, in the opinion of management, are required for a fair presentation of the results and financial condition of the Company. Prior period amounts are reclassified whenever necessary to conform to the current year classifications.

The Company considers events or transactions that occur after the balance sheet date but before the consolidated financial statements are issued to provide additional evidence relative to certain estimates or to identify matters that require additional disclosure. Subsequent events have been evaluated through the date of the issuance of these consolidated financial statements.

The unaudited interim results of consolidated operations are not necessarily indicative of the results for any future interim period or for the entire year. These interim consolidated financial statements do not include all disclosures associated with annual financial statements and, accordingly, should be read in conjunction with the annual consolidated financial statements and accompanying notes included in the Company s 2010 Annual Report on Form 10-K filed with the Securities and Exchange Commission ( SEC ).

**(2) Earnings per Share**

Basic earnings per share ( EPS ) exclude dilution and are computed by dividing net income by the weighted average number of common shares and participating securities outstanding during the period. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of additional common stock that then share in the earnings of the Company.

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The following sets forth a reconciliation of basic EPS and diluted EPS:

| | Three Months Ended | |
|---|---|---|
| | March 31, 2011 | March 31, 2010 |
| | (In thousands, except per share data) | |
| Basic EPS Computation: | | |
| Numerator: | | |
| Net income | $ 2,307 | $ 2,219 |
| Denominator: | | |
| Weighted average shares outstanding | 4,683 | 4,622 |
| Basic EPS | $ 0.49 | $ 0.48 |
| Diluted EPS Computation: | | |
| Numerator: | | |
| Net income | $ 2,307 | $ 2,219 |
| Denominator: | | |
| Weighted average shares outstanding | 4,683 | 4,622 |
| Dilutive effect of stock options | 31 | 28 |
| Dilutive effect of contingent shares | 1 | |
| Diluted weighted average shares outstanding | 4,715 | 4,650 |
| Diluted EPS | $ 0.49 | $ 0.48 |

For the three months ended March 31, 2011 and 2010, average options to purchase 220,750 and 231,950 shares of common stock, respectively, were outstanding but excluded from the computation of diluted EPS because they were anti-dilutive.

**(3) Recently Adopted Accounting Pronouncements**

In January 2010, the FASB issued Accounting Standards Update ( ASU ) No. 2010-06, *Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Instruments*. ASU No. 2010-06 amends ASC 820 to require additional disclosures regarding fair value measurements. Specifically, the ASU requires entities to disclose the amounts and reasons for significant transfers between Level 1 and Level 2 of the fair value hierarchy, to disclose reasons for any transfers in or out of Level 3 and to separately disclose information in the reconciliation of recurring Level 3 measurements about purchases, sales, issuances and settlements. In addition, the ASU also amends ASC 820 to clarify certain existing disclosure requirements. Except for the requirement to disclose information about purchases, sales, issuances and settlements in the reconciliation of recurring Level 3 measurements separately, the amendments to ASC 820 made by ASU No. 2010-06 are effective for interim and annual reporting periods beginning after December 15, 2009. The adoption of these provisions of ASU No. 2010-06 on January 1, 2010 did not have a material impact on the Company s consolidated financial statements. The requirement to separately disclose purchases, sales, issuances and settlements of recurring Level 3 measurements is effective for interim and annual reporting periods beginning after December 15, 2010. The adoption of the remaining provisions of this ASU on January 1, 2011 did not have a material impact on the Company s consolidated financial statements.

In July 2010, the FASB issued ASU No. 2010-20, *Receivables (Topic 310): Disclosures About the Credit Quality of Financing Receivables and the Allowance for Credit Losses*. ASU No. 2010-20 amends ASC 310, *Receivables,* by requiring more robust and disaggregated disclosures about the credit quality of an entity s financing receivables and its allowance for credit losses. An entity is required to disclose the nature of credit risk associated with its financing receivables and the assessment of that risk in estimating its allowance for credit losses, as well as changes in the

allowance and the reason for those changes. The new and amended disclosures required under ASC 2010-20 that relate to information as of the end of a reporting period are effective for public entities with fiscal years and interim reporting periods ending on or after December 15, 2010. The Company adopted these provisions of the ASU on October 1, 2010. The disclosures that include information for activity that occurs during a reporting period are effective for public companies with the fiscal years or the first interim period beginning after December 15, 2010. The Company adopted these provisions of the ASU on January 1, 2011. The adoption of ASU No. 2010-20 required significant expansion to the Company s disclosures surrounding loans and leases receivable and the allowance for loan and lease losses. See *Note 6 - Credit Quality of Loans and Leases and Allowance for Loans and Leases.*

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In January 2011, the FASB issued ASU No. 2011-01, *Receivables (Topic 310): Deferral of the Effective Date of Disclosures about Troubled Debt Restructurings in Update No. 2010-20.* ASU No. 2011-01 deferred the effective date for the troubled debt restructuring ( TDR ) disclosures that are required by ASU No. 2010-20. The TDR disclosures are to be required when the FASB completes its separate project on identifying TDRs (see *Note 4 Recently Issued Accounting Pronouncements*).

**(4) Recently Issued Accounting Pronouncements**

In April 2011, the FASB issued ASU No. 2011-02, *Receivables (Topic 310): A Creditor s Determination of Whether a Restructuring is a Troubled Debt Restructuring.* ASU No. 2011-02 provides additional guidance clarifying when the restructure of a receivable should be considered a TDR. Specifically, the ASU provides guidance in determining whether the creditor has granted a concession and whether the debtor is experiencing financial difficulty. Public entities are required to adopt ASU No. 2011-02 for interim and annual periods beginning on or after June 15, 2011 with early adoption permitted. For purposes of TDR disclosures, this ASU applies retrospectively to restructurings occurring on or after the beginning of the annual period of adoption. However, any changes in the method used to measure impairment apply prospectively. Beginning in the period ASU No. 2011-02 is adopted, public entities will also be subject to the requirements to disclose the activity-based information about TDRs under ASU No. 2010-20 that was previously deferred. The Company does not expect the adoption of this ASU to have a material impact on the Company s consolidated financial statements.

**(5) Available for Sale Securities**

The Company categorizes available for sale securities by major category, including government-sponsored enterprise ( GSE ) obligations, trust preferred collateralized debt obligations ( CDOs ), collateralized mortgage obligations and GSE mortgage-backed securities. Major categories are determined by the nature and risks of the securities and consider, among other things, the issuing entity, type of investment and underlying collateral. The Company categorizes obligations and/or securities issued by the Federal Home Loan Bank, Federal Home Loan Mortgage Corporation, Federal National Mortgage Association and Federal Farm Credit Banks Funding Corporation as GSE obligations and/or securities.

A summary of available for sale securities by major categories follows:

| | Amortized Cost (1) | Unrealized Gains | Unrealized Losses | Fair Value |
|---|---|---|---|---|
| | | *(In thousands)* | | |
| At March 31, 2011: | | | | |
| GSE obligations | $ 80,984 | $ 332 | $ (397) | $ 80,919 |
| Trust preferred CDOs | 1,518 | | (917) | 601 |
| Collateralized mortgage obligations | 24,595 | 419 | (136) | 24,878 |
| GSE mortgage-backed securities | 252,202 | 5,227 | (2,248) | 255,181 |
| Total | $ 359,299 | $ 5,978 | $ (3,698) | $ 361,579 |
| At December 31, 2010: | | | | |
| GSE obligations | $ 80,992 | $ 436 | $ (394) | $ 81,034 |
| Trust preferred CDOs | 1,518 | | (956) | 562 |
| Collateralized mortgage obligations | 28,885 | 517 | (1,234) | 28,168 |
| GSE mortgage-backed securities | 246,007 | 6,076 | (1,822) | 250,261 |
| Total | $ 357,402 | $ 7,029 | $ (4,406) | $ 360,025 |

(1) Amortized cost is net of write-downs as a result of other-than-temporary impairment.

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The Company sells available for sale securities to capitalize on fluctuations in the market. During the quarter ended March 31, 2011, $4.2 million of available for sale securities were sold, generating $212,000 of gains compared to $8.8 million of available for sale securities sold, generating $475,000 of gains during the same quarter of 2010. The cost of securities used in calculating gains on the sale of available for sale securities is determined using the specific identification method.

The following table sets forth certain information regarding temporarily impaired available for sale securities:

| | Number of Holdings | Less than One Year Fair Value | Less than One Year Unrealized Losses | One Year or Longer Fair Value | One Year or Longer Unrealized Losses | Total Fair Value | Total Unrealized Losses |
|---|---|---|---|---|---|---|---|
| | | | (Dollars in thousands) | | | | |
| At March 31, 2011: | | | | | | | |
| GSE obligations | 7 | $ 34,597 | $ (397) | $ | $ | $ 34,597 | $ (397) |
| Trust preferred CDOs | 2 | | | 601 | (917) | 601 | (917) |
| Collateralized mortgage obligations | 2 | 213 | | 6,436 | (136) | 6,649 | (136) |
| GSE mortgage-backed securities | 23 | 93,396 | (2,248) | | | 93,396 | (2,248) |
| Total | 34 | $ 128,206 | $ (2,645) | $ 7,037 | $ (1,053) | $ 135,243 | $ (3,698) |
| At December 31, 2010: | | | | | | | |
| GSE obligations | 7 | $ 39,599 | $ (394) | $ | $ | $ 39,599 | $ (394) |
| Trust preferred CDOs | 2 | | | 562 | (956) | 562 | (956) |
| Collateralized mortgage obligations | 3 | 1,912 | (12) | 7,896 | (1,222) | 9,808 | (1,234) |
| GSE mortgage-backed securities | 15 | 60,592 | (1,822) | | | 60,592 | (1,822) |
| Total | 27 | $ 102,103 | $ (2,228) | $ 8,458 | $ (2,178) | $ 110,561 | $ (4,406) |

The following table sets forth the maturities of available for sale securities:

| | Within One Year Amortized Cost | Within One Year Fair Value | After One, But Within Five Years Amortized Cost | After One, But Within Five Years Fair Value | After Five, But Within Ten Years Amortized Cost | After Five, But Within Ten Years Fair Value | After Ten Years Amortized Cost | After Ten Years Fair Value |
|---|---|---|---|---|---|---|---|---|
| | | | | (In thousands) | | | | |
| At March 31, 2011: | | | | | | | | |
| GSE obligations | $ 16,000 | $ 16,222 | $ 64,984 | $ 64,697 | $ | $ | $ | $ |
| Trust preferred CDOs | | | | | | | 1,518 | 601 |
| Collateralized mortgage obligations | | | | | 13,189 | 13,522 | 11,406 | 11,356 |
| GSE mortgage-backed securities | | | 1,988 | 2,067 | 9,577 | 10,194 | 240,637 | 242,920 |
| Total | $ 16,000 | $ 16,222 | $ 66,972 | $ 66,764 | $ 22,766 | $ 23,716 | $ 253,561 | $ 254,877 |
| At December 31, 2010: | | | | | | | | |
| GSE obligations | $ | $ | $ 70,997 | $ 71,076 | $ 9,995 | $ 9,957 | $ | $ |
| Trust preferred CDOs | | | | | | | 1,518 | 562 |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Collateralized mortgage obligations | | | | | 15,059 | 15,426 | 13,827 | 12,743 |
| GSE mortgage-backed securities | | | 2,220 | 2,315 | 10,396 | 11,055 | 233,390 | 236,891 |
| Total | $ | $ | $ 73,217 | $ 73,391 | $ 35,450 | $ 36,438 | $ 248,735 | $ 250,196 |

At March 31, 2011 and December 31, 2010, respectively, $253.2 million and $245.8 million of available for sale securities were pledged as collateral for repurchase agreements, municipal deposits, treasury, tax and loan deposits, swap agreements, current and future Federal Home Loan Bank of Boston ( FHLB ) borrowings and future Federal Reserve discount window borrowings.

The Company performs regular analysis on the available for sale securities portfolio to determine whether a decline in fair value indicates that an investment is other-than-temporarily impaired. In making these other-than-temporary determinations, management considers, among other factors, the length of time and extent to which the fair value has been less than amortized cost, projected future cash flows, credit subordination and the creditworthiness, capital adequacy and near-term prospects of the issuers. Management also considers the Company s capital adequacy, interest rate risk, liquidity and business plans in assessing whether it is more likely than not that the Company will sell or be required to sell the securities before recovery.

If the Company determines that a decline in fair value is other-than-temporary and that it is more likely than not that the Company will not sell or be required to sell the security before recovery of its amortized cost, the credit portion of the impairment loss is recognized in earnings and the noncredit portion is recognized in accumulated other comprehensive income. The credit portion of the other-than-temporary impairment represents the difference between the amortized cost and the present value of the expected future cash flows of the security. If the Company determines that a decline in fair value is other-than-temporary and it will more likely than not sell or be required to sell the security before recovery of its amortized cost, the entire difference between the amortized cost and the fair value of the security will be recognized in earnings.

In performing the analysis for the two collateralized debt obligations ( CDO A and CDO B ) held by the Company, which are backed by pools of trust preferred securities, future cash flow scenarios for each security were estimated based on varying levels of severity for assumptions of future delinquencies, recoveries and prepayments. These estimated cash flow scenarios were used to determine whether the Company expects to recover the amortized cost basis of the securities. Projected credit losses were compared to the current level of credit enhancement to assess whether the security is expected to incur losses in any future period and therefore become other-than-temporarily impaired.

CDO A has experienced $99.0 million, or 42.8%, in deferrals/defaults of the security s underlying collateral to date, including an additional $5.0 million during the first quarter of 2011. Projected credit loss severity assumptions were increased in estimated future cash flow scenarios and it was determined that management expects to recover the security s amortized cost. At March 31, 2011, credit related other-than-temporary impairment losses on this security since its purchase totaled $484,000.

CDO B has experienced $176.5 million, or 30.6%, in deferrals/defaults of the security s underlying collateral to date. The Company has not received its scheduled quarterly interest payments since June 30, 2009 because the security is adding interest to the principal rather than paying out. Projected credit loss severity assumptions were increased in estimated future cash flow scenarios and it was determined that management expects to recover the security s amortized cost. At March 31, 2011, credit related other-than-temporary impairment losses on this security since its purchase totaled $932,000.

The following table provides a reconciliation of the beginning and ending balances for credit losses on debt securities for which a portion of an other-than-temporary impairment was recognized in other comprehensive income:

| | **Credit Component of Other-Than-Temporary Impairment Losses For Which a Portion Was Recognized in Other Comprehensive Income** | |
|---|---|---|
| | **2011** | **2010** |
| | ***(In thousands)*** | |
| Balance, January 1 | $ (1,416) | $ (384) |
| Credit losses for which an other-than-temporary impairment was previously recognized | | (571) |
| Balance, March 31 | $ (1,416) | $ (955) |

The decline in fair value of the remaining available for sale securities in an unrealized loss position is due to general market concerns of the liquidity and creditworthiness of the issuers of the securities. Management believes that it will recover the amortized cost basis of the securities and that it is more likely than not that it will not sell the securities before recovery. As such, management has determined that the securities are not other-than-temporarily impaired as of March 31, 2011. If market conditions for securities worsen or the creditworthiness of the underlying issuers deteriorates, it is possible that the Company may recognize additional other-than-temporary impairments in future

periods.

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**(6) Credit Quality of Loans and Leases and Allowance for Loan and Lease Losses**

At March 31, 2011, there were $15.3 million of nonaccrual loans and leases in the portfolio. There were $3.2 million of loans past due 60 to 89 days at March 31, 2011. At March 31, 2011, the Bank had no commitments to lend additional funds to borrowers whose loans were on nonaccrual. This compares to $16.5 million of nonaccrual loans and $2.4 million of loans past due 60 to 89 days as of December 31, 2010. There were $9.6 million of impaired loans with $651,000 of specific impairment reserves at March 31, 2011, while included in nonaccrual loans as of December 31, 2010 were impaired loans of $10.8 million with specific reserves of $1.5 million.

The following table sets forth information pertaining to the Company s recorded investment of loans and leases accounted for on a nonaccrual basis and past due 90 days or more, but still accruing.

| | March 31, 2011 | | | December 31, 2010 | | |
|---|---|---|---|---|---|---|
| | Nonaccrual | 90+ Days, Still Accruing | Total | Nonaccrual | 90+ Days, Still Accruing | Total |
| | *(In thousands)* | | | | | |
| Commercial loans and leases: | | | | | | |
| Commercial real estate owner occupied | $ 4,342 | $ 450 | $ 4,792 | $ 5,272 | $ | $ 5,272 |
| Commercial and industrial | 2,138 | 117 | 2,255 | 2,462 | | 2,462 |
| Multifamily | 1,050 | | 1,050 | 717 | | 717 |
| Small business | 981 | 78 | 1,059 | 1,090 | | 1,090 |
| Construction | 232 | | 232 | 470 | | 470 |
| Leases and other | 591 | | 591 | 581 | | 581 |
| Total commercial loans and leases | 9,334 | 645 | 9,979 | 10,592 | | 10,592 |
| Residential mortgage loans: | | | | | | |
| One- to four-family adjustable rate | 3,972 | | 3,972 | 4,089 | | 4,089 |
| One- to four-family fixed rate | 954 | | 954 | 956 | | 956 |
| Total residential mortgage loans | 4,926 | | 4,926 | 5,045 | | 5,045 |
| Consumer and other loans: | | | | | | |
| Home equity term loans | 919 | | 919 | 826 | | 826 |
| Home equity lines of credit | 74 | | 74 | 50 | | 50 |
| Total consumer and other loans | 993 | | 993 | 876 | | 876 |
| Total nonperforming loans and leases | $ 15,253 | $ 645 | $ 15,898 | $ 16,513 | $ | $ 16,513 |

The following table sets forth information pertaining to the Company s recorded investment of past due loans and leases.

| | March 31, 2011 | | | |
|---|---|---|---|---|
| | 30-59 Days Past Due | 60-89 Days Past Due | 90+ Days Past Due (1) | Total |
| | (In thousands) | | | |
| Commercial loans and leases: | | | | |
| Commercial real estate nonowner occupied | $ 380 | $ | $ | $ 380 |
| Commercial real estate owner occupied | 2,633 | | 450 | 3,083 |
| Commercial and industrial | 783 | 1,167 | 117 | 2,067 |
| Multifamily | 401 | | | 401 |
| Small business | 738 | 504 | 78 | 1,320 |
| Leases and other | 1,348 | 524 | | 1,872 |
| Total past due commercial loans and leases | 6,283 | 2,195 | 645 | 9,123 |
| Residential mortgage loans: | | | | |
| One- to four-family adjustable | 2,115 | 979 | | 3,094 |
| One- to four family fixed rate | | | | |
| Total past due residential mortgage loans | 2,115 | 979 | | 3,094 |
| Consumer and other loans: | | | | |
| Home equity term loans | 816 | | | 816 |
| Home equity lines of credit | 386 | | | 386 |
| Unsecured and other | | 5 | | 5 |
| Total past due consumer and other loans | 1,202 | 5 | | 1,207 |
| Total past due loans and leases | $ 9,600 | $ 3,179 | $ 645 | $ 13,424 |

| | December 31, 2010 | | | |
|---|---|---|---|---|
| | 30-59 Days Past Due | 60-89 Days Past Due | 90+ Days Past Due (1) | Total |
| | (In thousands) | | | |
| Commercial loans and leases: | | | | |
| Commercial real estate nonowner occupied | $ 282 | $ 143 | $ | $ 425 |
| Commercial real estate owner occupied | 832 | | | 832 |
| Commercial and industrial | 346 | 204 | | 550 |
| Multifamily | 299 | 661 | | 960 |
| Small business | 812 | 180 | | 992 |
| Leases and other | 1,053 | 711 | | 1,764 |

| | | | | |
|---|---|---|---|---|
| Total past due commercial loans and leases | 3,624 | 1,899 | | 5,523 |
| Residential mortgage loans: | | | | |
| One- to four-family adjustable | 2,005 | 415 | | 2,420 |
| One- to four family fixed rate | 142 | | | 142 |
| Total past due residential mortgage loans | 2,147 | 415 | | 2,562 |
| Consumer and other loans: | | | | |
| Home equity term loans | 398 | 115 | | 513 |
| Home equity lines of credit | 299 | | | 299 |
| Unsecured and other | 7 | | | 7 |
| Total past due consumer and other loans | 704 | 115 | | 819 |
| Total past due loans and leases | $ 6,475 | $ 2,429 | $ | $ 8,904 |

(1) 90+ Days Past Due includes only those loans and leases that are still accruing. All other loans and leases 90 days or more are included as a component of nonaccrual loans and leases.

The Company maintains an allowance for loan and lease losses sufficient to absorb probable losses in its loan and lease portfolios. Arriving at an appropriate level of allowance for loan and lease losses requires the creation and maintenance of a risk rating system that accurately classifies all loans and leases by category and further by degree of credit risk. A specified level of allowance is established within each classification and is based upon statistical analysis of loss trends, historical migration and delinquency patterns, anticipated trends in the loan and lease portfolios and industry standards and trends. The levels of allowance within each classification are subject to periodic reviews and, therefore, are subject to change.

Generally, commercial loans and leases are individually risk rated on a scale of 1 through 7. Ratings 1 through 5 are considered pass, or satisfactory credit exposures. Ratings 6, or special mention, and 7, or substandard, are negative ratings and loans and leases with these ratings are considered watch list assets. Loans and leases categorized as special mention have potential weaknesses that deserve management s close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects of the loan or lease at some future date. Loans and leases categorized as substandard are inadequately protected by the payment capacity of the obligor or by the collateral pledged, if any. Substandard loans and leases have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt and are characterized by the distinct possibility that the Company will sustain some loss if the deficiencies are not corrected.

A reserve percentage is assigned to each risk rating category based on the perceived risk of default and loss in conjunction with the Company s historical loss experience. At March 31, 2011 and December 31, 2010, the reserve percentages ranged from and 0.00% to 1.50% for pass-rated loans and leases. Special mention and substandard loans and leases were assigned reserve percentages of 5.00% and 15.00%, respectively. Macrolease-generated loans and leases and small business loans are excluded from the aforementioned commercial risk rating scale and are reserved at 1.00% and 2.00%, respectively, at March 31, 2011 and December 31, 2010. These portfolios are much smaller and historical evidence has shown that these portfolios experience fairly moderate losses.

Risk classifications for residential mortgage loans are stratified initially by type of loan. At March 31, 2011 and December 31, 2010, current fixed rate loans were reserved at 0.40%, while current adjustable rate mortgage ( ARM ) loans were reserved at 1.00%. Additionally, these loans are classified by delinquency, ranging from one payment delinquent to four or more payments delinquent. The reserve percentages for delinquent residential mortgage loans ranged from 2.00% to 25.00% at March 31, 2011 and December 31, 2010.

Consumer and other loans are also classified by type of loan. At March 31, 2011 and December 31, 2010, home equity term loans in which the Bank has a subordinated interest and home equity lines of credit were reserved at 0.90%. Home equity term loans in which the Bank has a first position interest are reserved for based on delinquency status, ranging from 0.40% for current loans to 25.00% for loans that are over 90 days delinquent at March 31, 2011 and December 31, 2010. Unsecured and other consumer loans are reserved at 7.00% at March 31, 2011 and December 31, 2010. Loans that are fully secured by depository accounts at the Bank are not reserved for.

Nonperforming commercial loans and leases in excess of $100,000 are deemed to be impaired. In addition, loans that have been modified as troubled debt restructurings, including residential mortgage and consumer loans regardless of dollar amount, are deemed to be impaired loans. Loans and leases deemed to be impaired are individually reviewed and a specific reserve is established rather than collectively reserved for based on risk rating profile. The reserves for impaired loans and leases are determined by reviewing the fair values of the collateral (if collateral-dependent), observable market prices of the loans and leases or the present value of expected future cash flows.

The management portion of the reserve is the most difficult to quantify. It is maintained to protect against probable, yet unexpected losses, which may include a larger loss or allocation on a loan or lease than is covered by the normal reserve percentage for that asset. It is not practical to quantify a specific amount for this portion of the allowance for loan and lease losses. Rather, an acceptable range is sought. Factors that bring a level of uncertainty to probable losses in the Bank s portfolio include, but are not limited to, economic and interest rate uncertainty, real estate market uncertainty, large relationship exposures and industry concentrations. A management reserve range of 0.08% to 0.20% of loans and leases is supported by these factors.

Early identification and reclassification of deteriorating credits is a critical component of the Company s ongoing evaluation process and includes a formal analysis of the allowance each quarter, which considers, among other factors, the character and size of the loan and lease portfolio, charge-off experience, delinquency and nonperforming loan and lease patterns, business and economic conditions and other asset quality factors. These factors are based on observable information as well as subjective assessment and interpretation. Besides numerous subjective judgments as to the number of categories, appropriate level of allowance with respect to each category and judgments as to categorization of any individual loan or lease, additional subjective judgments are involved when ascertaining the probability, as well as, the extent of any probable losses.

While management evaluates currently available information in establishing the allowance for loan and lease losses, future additions to the allowance may be necessary if conditions differ substantially from the assumptions used in making evaluations. In addition, various regulatory agencies, as an integral part of their examination process, periodically review a financial institution s allowance for loan and lease losses and carrying amounts of other real estate owned. Such agencies may require the financial institution to recognize adjustments to the allowance based on their judgments about information available to them at the time of their examination.

Loans deemed uncollectible are charged against the allowance for loan and lease losses, while recoveries of amounts previously charged-off are added to the allowance for loan and lease losses. Generally, amounts are charged-off once the probability of loss has been established, with consideration given to such factors as the customer s financial condition, underlying collateral and guarantees, and general and industry economic conditions. Additionally, in accordance with certain regulatory guidance, residential mortgage and home equity loans are charged-off after 120 days of cumulative delinquency. Home equity lines of credit are charged-off after 180 days of cumulative delinquency.

An analysis of the activity in the allowance for loan and lease losses is as follows:

| | Three Months Ended March 31, | |
|---|---|---|
| | 2011 | 2010 |
| | (In thousands) | |
| Balance at beginning of period | $ 18,654 | $ 16,536 |
| Loans and leases charged-off: | | |
| Commercial loans and leases | (1,288) | (1,163) |
| Residential mortgage loans | (379) | (347) |
| Consumer and other loans | (19) | (102) |
| Total loans and leases charged-off | (1,686) | (1,612) |
| Recoveries of loans and leases previously charged-off: | | |
| Commercial loans and leases | 122 | 97 |
| Residential mortgage loans | | |
| Consumer and other loans | 7 | 4 |
| Total recoveries of loans and leases previously charged-off | 129 | 101 |
| Net charge-offs | (1,557) | (1,511) |
| Provision for loan and lease losses charged against income | | |
| Commercial loans and leases | 923 | 857 |
| Residential mortgage loans | (74) | 78 |
| Consumer and other loans | 276 | 665 |
| Total provision for loan and lease losses charged against income | 1,125 | 1,600 |

| | | | | |
|---|---|---|---|---|
| Balance at end of period | $ | 18,222 | $ | 16,625 |

At March 31, 2011 and December 31, 2010, there were no significant purchases or sales of loans and/or leases. In addition, there were no reclassifications of loans and/or leases to held for sale.

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The following tables set forth information pertaining to the recorded investment of loans and leases that are collectively and individually evaluated for impairment and the related balance in the allowance for loan and lease losses.

| | Individually Evaluated for Impairment | | Collectively Evaluated for Impairment | |
|---|---|---|---|---|
| | Recorded Investment | Allowance for Loan and Lease Losses | Recorded Investment | Allowance for Loan and Lease Losses |
| | *(In thousands)* | | | |
| At March 31, 2011: | | | | |
| Commercial loans and leases: | | | | |
| Commercial real estate nonowner occupied | $ | $ | $ 196,353 | $ 2,654 |
| Commercial real estate owner occupied | 4,342 | 93 | 178,769 | 3,618 |
| Commercial and industrial | 2,126 | 260 | 158,878 | 2,487 |
| Multifamily | 955 | 85 | 83,817 | 1,452 |
| Small business | 361 | 86 | 61,872 | 1,239 |
| Construction | 232 | | 28,041 | 431 |
| Leases and other | 125 | 108 | 66,069 | 475 |
| Total commercial loans and leases | 8,141 | 632 | 773,799 | 12,356 |
| Residential mortgage loans: | | | | |
| One- to four-family adjustable rate | 545 | 7 | 100,431 | 1,420 |
| One- to four-family fixed rate | | | 59,106 | 232 |
| Total residential mortgage loans | 545 | 7 | 159,537 | 1,652 |
| Consumer and other loans: | | | | |
| Home equity term loans | 895 | 12 | 124,744 | 715 |
| Home equity lines of credit | | | 82,038 | 738 |
| Unsecured and other | | | 1,489 | 113 |
| Total consumer and other loans | 895 | 12 | 208,271 | 1,566 |
| Premium on loans acquired | | | 576 | |
| Net deferred loan origination costs | | | 2,684 | |
| Total loans and leases | $ 9,581 | $ 651 | $ 1,144,867 | $ 15,574 |
| At December 31, 2010: | | | | |
| Commercial loans and leases: | | | | |
| Commercial real estate nonowner occupied | $ | $ | $ 200,809 | $ 2,700 |
| Commercial real estate owner occupied | 5,272 | 392 | 174,494 | 3,462 |
| Commercial and industrial | 2,288 | 287 | 155,591 | 2,323 |
| Multifamily | 717 | 108 | 79,217 | 1,387 |
| Small business | 462 | 141 | 62,379 | 1,318 |
| Construction | 470 | 220 | 29,879 | 452 |
| Leases and other | 125 | 108 | 66,770 | 472 |

| | | | | |
|---|---|---|---|---|
| Total commercial loans and leases | 9,334 | 1,256 | 769,139 | 12,114 |
| Residential mortgage loans: | | | | |
| One- to four-family adjustable rate | 549 | 7 | 105,792 | 1,313 |
| One- to four-family fixed rate | | | 57,948 | 460 |
| Total residential mortgage loans | 549 | 7 | 163,740 | 1,773 |
| Consumer and other loans: | | | | |
| Home equity term loans | 906 | 101 | 124,208 | 721 |
| Home equity lines of credit | | | 82,778 | 745 |
| Unsecured and other | | | 1,511 | 114 |
| Total consumer and other loans | 906 | 101 | 208,497 | 1,580 |
| Premium on loans acquired | | | 598 | |
| Net deferred loan origination costs | | | 2,726 | |
| Total loans and leases | $ 10,789 | $ 1,364 | $ 1,144,700 | $ 15,467 |

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The following tables set forth information pertaining to the unpaid principal and the recorded investment for impaired loans and leases both requiring a specific reserve and not requiring a specific reserve.

| | **March 31, 2011** | | | |
|---|---|---|---|---|
| | Requiring a Specific Reserve | Not Requiring a Specific Reserve | Total Impaired Loans and Leases | Unpaid Principal |
| | *(In thousands)* | | | |
| Commercial loans and leases: | | | | |
| Commercial real estate owner occupied | $ 2,553 | $ 1,789 | $ 4,342 | $ 5,068 |
| Commercial and industrial | 1,865 | 261 | 2,126 | 3,581 |
| Multifamily | 707 | 248 | 955 | 1,272 |
| Small business | 148 | 213 | 361 | 366 |
| Construction | | 232 | 232 | 469 |
| Leases and other | 125 | | 125 | 125 |
| Total impaired commercial loans and leases | 5,398 | 2,743 | 8,141 | 10,881 |
| Residential mortgage loans: | | | | |
| One- to four-family adjustable rate | 258 | 287 | 545 | 545 |
| Total impaired residential mortgage loans | 258 | 287 | 545 | 545 |
| Consumer and other loans: | | | | |
| Home equity term loans | 736 | 159 | 895 | 895 |
| Total impaired consumer and other loans | 736 | 159 | 895 | 895 |
| Total impaired loans and leases | $ 6,392 | $ 3,189 | $ 9,581 | $ 12,321 |

| | **December 31, 2010** | | | |
|---|---|---|---|---|
| | Requiring a Specific Reserve | Not Requiring a Specific Reserve | Total Impaired Loans and Leases | Unpaid Principal |
| | *(In thousands)* | | | |
| Commercial loans and leases: | | | | |
| Commercial real estate owner occupied | $ 3,483 | $ 1,789 | $ 5,272 | $ 5,998 |
| Commercial and industrial | 2,008 | 280 | 2,288 | 3,743 |
| Multifamily | 717 | | 717 | 717 |
| Small business | 312 | 150 | 462 | 538 |
| Construction | 470 | | 470 | 470 |
| Leases and other | 125 | | 125 | 125 |
| Total impaired commercial loans and leases | 7,115 | 2,219 | 9,334 | 11,591 |
| Residential mortgage loans: | | | | |
| One- to four-family adjustable rate | 259 | 290 | 549 | 731 |

| | | | | |
|---|---|---|---|---|
| Total impaired residential mortgage loans | 259 | 290 | 549 | 731 |
| Consumer and other loans: | | | | |
| Home equity term loans | 745 | 161 | 906 | 906 |
| Total impaired consumer and other loans | 745 | 161 | 906 | 906 |
| Total impaired loans and leases | $ 8,119 | $ 2,670 | $ 10,789 | $ 13,228 |

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The following tables set forth information pertaining to the average recorded investment of impaired loans and leases, total interest income recognized and interest income recognized using the cash-basis method of accounting during the periods that the loans and leases were impaired for the years shown.

| | Three Months Ended | | | | | |
|---|---|---|---|---|---|---|
| | March 31, 2011 | | | March 31, 2010 | | |
| | Average Recorded Investment | Total Interest Income Recognized | Interest Income Recognized Using Cash-Basis | Average Recorded Investment | Interest Income Recognized | Interest Income Recognized Using Cash-Basis |
| | (In thousands) | | | | | |
| Commercial loans and leases: | | | | | | |
| Commercial real estate nonowner occupied | $ | $ | $ | $ 1,067 | $ | $ |
| Commercial real estate owner occupied | 4,772 | 76 | | 4,742 | | |
| Commercial and industrial | 2,265 | 23 | | 1,807 | | |
| Multifamily | 1,057 | 1 | | 154 | | |
| Small business | 422 | | | 761 | 1 | |
| Construction | 351 | | | 529 | | |
| Leases and other | 125 | 2 | | 889 | 2 | |
| Total impaired commercial loans and leases | 8,992 | 102 | | 9,949 | 3 | |
| Residential mortgage loans: | | | | | | |
| One- to four-family adjustable rate | 547 | | | 266 | | |
| One- to four-family fixed rate | | | | | | |
| Total impaired residential mortgage loans | 547 | | | 266 | | |
| Consumer and other loans: | | | | | | |
| Home equity term loans | 901 | | | 177 | | |
| Home equity lines of credit | | | | 49 | | |
| Total impaired consumer and other loans | 901 | | | 226 | | |
| Total impaired loans and leases | $ 10,440 | $ 102 | $ | $ 10,441 | $ 3 | $ |

Management believes that the Company s internal risk rating system for commercial loans and credit scores obtained from credit reporting agencies for residential mortgage and consumer loans are meaningful credit quality indicators. Risk ratings are evaluated and credit scores are obtained at least quarterly. The following table sets forth information pertaining to the recorded investment in loans and leases by credit quality indicator.

| | March 31, 2011 | December 31, 2010 |
|---|---|---|
| | *(In thousands)* | |
| Commercial loans and leases (risk rating): | | |
| Pass-rated | $ 741,575 | $ 735,869 |
| Special mention | 15,527 | 19,825 |
| Substandard | 24,838 | 22,779 |
| Total commercial loans and leases | 781,940 | 778,473 |
| Residential mortgage loans (credit score): | | |
| Greater than 750 | 85,280 | 84,695 |
| 725 750 | 14,598 | 18,930 |
| 680 724 | 18,933 | 19,310 |
| 650 679 | 8,348 | 6,558 |
| 620 649 | 3,934 | 6,278 |
| Less than 620 | 18,976 | 19,883 |
| Data not available | 10,013 | 8,635 |
| Total residential mortgage loans | 160,082 | 164,289 |
| Consumer and other loans (credit score): | | |
| Greater than 750 | 153,289 | 151,710 |
| 725 750 | 21,680 | 21,984 |
| 680 724 | 19,008 | 20,252 |
| 650 679 | 5,909 | 5,605 |
| 620 649 | 1,922 | 2,756 |
| Less than 620 | 6,153 | 6,006 |
| Data not available | 1,205 | 1,090 |
| Total consumer and other loans | 209,166 | 209,403 |
| Premium on loans acquired | 576 | 598 |
| Net deferred loan origination costs | 2,684 | 2,726 |
| Total loans and leases | $ 1,154,448 | $ 1,155,489 |

**(7) Derivatives**

All derivatives are recognized as either assets or liabilities on the balance sheet and are measured at fair value. The accounting for changes in the fair value of derivatives depends on the intended use of the derivative and resulting designation. Derivatives used to hedge the exposure to changes in fair value of an asset, liability or firm commitment attributable to a particular risk, such as interest rate risk, are considered fair value hedges. Derivatives used to hedge the exposure to variability in expected cash flows or other types of forecasted transactions are considered cash flow hedges. For derivatives designated as fair value hedges, changes in the fair value of the derivative are recognized in earnings together with the changes in the fair value of the related hedged item. The net amount, if any, representing hedge ineffectiveness, is reflected in earnings. For derivatives designated as cash flow hedges, the effective portion of

changes in the fair value of the derivative is recorded in other comprehensive income and recognized in earnings when the hedged transaction affects earnings. The ineffective portion of changes in the fair value of cash flow hedges is recognized directly in earnings. For derivatives not designated as hedges, changes in fair value are recognized in earnings, in noninterest income. The Company may use interest rate contracts (swaps, caps and floors) as part of interest rate risk management strategy. Interest rate swap, cap and floor agreements are entered into as hedges against future interest rate fluctuations on specifically identified assets or liabilities. The Company did not have derivative fair value or derivative cash flow hedges at March 31, 2011 or December 31, 2010.

Derivatives not designated as hedges are not speculative but rather result from a service the Company provides to certain customers for a fee. The Company executes interest rate swaps with commercial banking customers to aid them in managing their interest rate risk. The interest rate swap contracts allow the commercial banking customers to convert floating rate loan payments to fixed rate loan payments. The Company concurrently enters into mirroring swaps with a third party financial institution, effectively minimizing its net risk exposure resulting from such transactions. The third party financial institution exchanges the customer s fixed rate loan payments for floating rate loan payments.

As the interest rate swaps associated with this program do not meet hedge accounting requirements, changes in the fair value of both the customer swaps and the offsetting swaps are recognized directly in earnings. As of March 31, 2011, the Company had ten interest rate swaps with an aggregate notional amount of $34.6 million related to this program. During the three months ended March 31, 2011 and 2010, the Company recognized net gains of $8,000 and $32,000, respectively, related to changes in the fair value of these swaps.

The table below presents the fair value of the Company s derivative financial instruments as well as their classification on the consolidated balance sheets as of March 31, 2011 and December 31, 2010:

| | Asset Derivatives | |
|---|---|---|
| | **March 31, 2011** | **December 31, 2010** |
| | *(In thousands)* | |
| ***Other Assets*** | | |
| Derivatives **not** designated as hedging instruments | | |
| Interest rate products | $ 614 | $ 790 |
| Total derivatives **not** designated as hedging instruments | $ 614 | $ 790 |

| | Liability Derivatives | |
|---|---|---|
| | **March 31, 2011** | **December 31, 2010** |
| | *(In thousands)* | |
| ***Other Liabilities*** | | |
| Derivatives **not** designated as hedging instruments | | |
| Interest rate products | $ 648 | $ 832 |
| Total derivatives **not** designated as hedging instruments | $ 648 | $ 832 |

The table below presents the effect of the Company s derivative financial instruments on the consolidated income statements for the three months ended March 31, 2011 and 2010:

| **Derivatives Not Designated as Hedging Instruments** | **Location of Gain Recognized in Income on Derivative** | **Amount of Gain Recognized in Income on Derivative (1) Three Months Ended March 31,** | |
|---|---|---|---|
| | | **2011** | **2010** |
| | | *(In thousands)* | |
| Interest Rate Products | Loan related fees | $ 8 | $ 32 |

| | | | | |
|---|---|---|---|---|
| Total | $ | 8 | $ | 32 |

(1) The amount of gain recognized in income represents net fee income and changes related to the fair value of the interest rate products.

By using derivative financial instruments, the Company exposes itself to credit risk. Credit risk is the failure of the counterparty to perform under the terms of the derivative contract. When the fair value of a derivative contract is positive, the counterparty owes the Company, which creates credit risk for the Company. When the fair value of a derivative is negative, the Company owes the counterparty and, therefore, it does not possess credit risk. The credit risk in derivative instruments is mitigated by entering into transactions with highly-rated counterparties that management believes to be creditworthy and by limiting the amount of exposure to each counterparty.

Certain of the derivative agreements contain provisions that require the Company to post collateral if the derivative exposure exceeds a threshold amount. As of March 31, 2011, the Company has posted collateral of $724,000 in the normal course of business.

The Company has agreements with certain of its derivative counterparties that contain credit-risk-related contingent provisions. These provisions provide the counterparty with the right to terminate its derivative positions and require the Company to settle its obligations under the agreements if the Company defaults on certain of its indebtedness or if the Company fails to maintain its status as a well-capitalized institution. As of March 31, 2011, the Company had no derivative agreements in a net liability position, excluding fair value adjustments for credit risk.

**(8) Fair Value of Financial Instruments**

ASC 820, *Fair Value Measurements and Disclosures*, defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. A fair value measurement assumes that the transaction to sell the asset or transfer the liability occurs in the principal market for the asset or liability or, in the absence of a principal market, the most advantageous market for the asset or liability. The price in the principal (or most advantageous) market used to measure the fair value of the asset or liability is adjusted for transaction costs. An orderly transaction is a transaction that assumes exposure to the market for a period prior to the measurement date to allow for marketing activities that are usual and customary for transactions involving such assets and liabilities. Market participants are buyers and sellers in the principal market that are independent, knowledgeable, able to transact and willing to transact.

ASC 820 requires the use of valuation techniques that are consistent with the market approach, the income approach and/or the cost approach. The market approach uses prices and other relevant information generated by market transactions involving identical or comparable assets and liabilities. The income approach uses valuation techniques to convert future amounts, such as cash flows or earnings, to a single present amount on a discounted basis. The cost approach is based on the amount that currently would be required to replace the service capacity of an asset (replacement cost). Valuation techniques should be consistently applied. Inputs to valuation techniques refer to the assumptions that market participants would use in pricing the asset or liability. Inputs may be observable, meaning those that reflect the assumptions market participants would use in pricing the asset or liability developed based on market data obtained from independent sources, or unobservable, meaning those that reflect the reporting entity s own assumptions about what assumptions market participants would use in pricing the asset or liability developed based on the best information available in the circumstances. A fair value hierarchy for valuation inputs that gives the highest priority to quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs is included in ASC 820. The fair value hierarchy is as follows:

Level 1: Inputs are unadjusted quoted prices in active markets for assets or liabilities identical to those reported at fair value.

Level 2: Inputs other than quoted prices included within Level 1, Level 2 inputs are observable either directly or indirectly. These inputs might include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets in markets that are not active, inputs other than quoted prices that are observable for the asset or liability (such as interest rates, volatilities, prepayment speeds, credit risks, etc.) or inputs that are derived principally from or corroborated by market data by correlation or other means.

Level 3: Inputs are unobservable inputs for an asset or liability that reflect an entity s own assumptions about the assumptions that market participants would use in pricing the assets or liabilities. These inputs are used to determine fair value only when observable inputs are not available.

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Transfers between Level 1, Level 2 and Level 3 of the fair value hierarchy are recognized based on the valuation method used at the end of each reporting period. There were no transfers of financial assets or liabilities between Level 1, Level 2 or Level 3 during the three months ended March 31, 2011 or 2010.

The following tables summarize the financial assets and financial liabilities measured at fair value on a recurring basis as of March 31, 2011 and December 31, 2010, segregated by the level of valuation inputs within the fair value hierarchy utilized to measure fair value:

| | | Fair Value Measurements at March 31, 2011 Using | | |
|---|---|---|---|---|
| ***(In thousands)*** | **Total** | **Quoted Prices in Active Markets for Identical Assets (Level 1)** | **Significant Other Observable Inputs (Level 2)** | **Significant Other Unobservable Inputs (Level 3)** |
| GSE obligations | $ 80,919 | $ | $ 80,919 | $ |
| Trust preferred CDOs | 601 | | 601 | |
| Collateralized mortgage obligations | 24,878 | | 24,878 | |
| GSE mortgage-backed securities | 255,181 | | 255,181 | |
| Total available for sale securities | 361,579 | | 361,579 | |
| Interest rate swap assets | 614 | | 614 | |
| Interest rate swap liabilities | 648 | | 648 | |

| | | Fair Value Measurements at December 31, 2010 Using | | |
|---|---|---|---|---|
| ***(In thousands)*** | **Total** | **Quoted Prices in Active Markets for Identical Assets (Level 1)** | **Significant Other Observable Inputs (Level 2)** | **Significant Other Unobservable Inputs (Level 3)** |
| GSE obligations | $ 81,034 | $ | $ 81,034 | $ |
| Trust preferred CDOs | 562 | | 562 | |
| Collateralized mortgage obligations | 28,168 | | 28,168 | |

| | | |
|---|---|---|
| GSE mortgage-backed securities | 250,261 | 250,261 |
| Total available for sale securities | 360,025 | 360,025 |
| Interest rate swap assets | 790 | 790 |
| Interest rate swap liabilities | 832 | 832 |

A description of the valuation methodologies used for instruments measured at fair value, as well as the general classification of such instruments pursuant to the valuation hierarchy, is set forth below. In general, fair value is based upon quoted market prices, where available. If such quoted market prices are not available, fair value is based upon internally developed models that primarily use, as inputs, observable market-based parameters. Valuation adjustments may be made to ensure that financial instruments are recorded at fair value. These adjustments may include amounts to reflect counterparty credit quality and the Company s creditworthiness, among other things, as well as unobservable parameters. Any such valuation adjustments are applied consistently over time. The Company s valuation methodologies may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. While management believes the Company s valuation methodologies are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date.

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Financial assets and financial liabilities measured at fair value on a recurring basis include the following:
*Available for sale securities* Available for sale securities are reported at fair value primarily utilizing Level 2 inputs. The Company obtains fair value measurements from independent pricing sources, which base their fair value measurements upon observable inputs such as reported trades of comparable securities, broker quotes, the U.S. Treasury ( the Treasury ) yield curve, benchmark interest rates, market spread relationships, historic and consensus prepayment rates, credit information and the security s terms and conditions.
*Interest rate swaps* The fair values for the interest rate swap assets and liabilities represent a Level 2 valuation and are based on settlement values adjusted for credit risks associated with the counterparties and the Company. Credit risk adjustments consider factors such as the likelihood of default by the Company and its counterparties, its net exposures and remaining contractual life. To date, the Company has not realized any losses due to a counterparty s inability to pay any net uncollateralized position. The change in value of interest rate swap assets and liabilities attributable to credit risk was not significant during the reported periods. See also *Note 7 Derivatives.*
Certain financial assets and financial liabilities are measured at fair value on a nonrecurring basis; that is, the instruments are not measured at fair value on an ongoing basis, but are subject to fair value adjustments in certain circumstances (for example, when there is evidence of impairment).
The following tables summarize the financial assets and financial liabilities measured at fair value on a nonrecurring basis as of and for the three months ended March 31, 2011 and March 31, 2010, segregated by the level of valuation inputs within the fair value hierarchy utilized to measure fair value:

| | | Fair Value Measurements at March 31, 2011 Using | | |
|---|---|---|---|---|
| ***(In thousands)*** | **Total** | **Quoted Prices in Active Markets for Identical Assets (Level 1)** | **Significant Other Observable Inputs (Level 2)** | **Significant Other Unobservable Inputs (Level 3)** |
| Collateral-dependent loans and leases | $ 2,539 | $ | $ 2,539 | $ |
| Other real estate owned | 445 | | 445 | |

| | | Fair Value Measurements at March 31, 2010 Using | | |
|---|---|---|---|---|
| ***(In thousands)*** | **Total** | **Quoted Prices in Active Markets for Identical Assets (Level 1)** | **Significant Other Observable Inputs (Level 2)** | **Significant Other Unobservable Inputs (Level 3)** |
| Collateral-dependent loans and leases | $ 2,586 | $ | $ 2,586 | $ |
| Other real estate owned | 724 | | 724 | |

*Impaired loans* Impaired loans and leases were $9.6 million at March 31, 2011 and $10.8 million at December 31, 2010. Impaired loans and leases that are deemed collateral-dependent are valued based upon the fair value of the underlying collateral. The inputs used in the appraisal of the collateral are observable and, therefore, categorized as Level 2. The valuation allowance for collateral-dependent loans and leases was $423,000 at March 31, 2011 and $1.4 million at December 31, 2010.

*Other real estate owned and non-real estate foreclosed assets* Fair value estimates of other real estate owned ( OREO ) and non-real estate foreclosed assets are based on independent appraisals or brokers opinions of the value of the property or similar properties less estimated costs to sell at the date the loan is charged-off and the property is transferred into OREO and/or non-real estate foreclosed assets. A valuation allowance is maintained for declines in fair value and estimated selling costs. The inputs used to estimate the fair values are observable, and therefore, categorized as Level 2.

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The aggregate fair value of financial assets and financial liabilities presented does not represent the underlying value of the Company taken as a whole. The fair value estimates provided are made at a specific point in time, based on relevant market information and the characteristics of the financial instrument. The estimates do not provide for any premiums or discounts that could result from concentrations of ownership of a financial instrument. Because no active market exists for some of the Company s financial instruments, certain fair value estimates are based on subjective judgments regarding current economic conditions, risk characteristics of the financial instruments, future expected loss experience, prepayment assumptions and other factors. The resulting estimates involve uncertainties and therefore cannot be determined with precision. Changes made to any of the underlying assumptions could significantly affect the estimates. The estimated fair value approximates the carrying value for cash and cash equivalents, overnight investments and accrued interest receivable and payable. The methodologies for other financial assets and financial liabilities are discussed below:

*Loans and leases receivable* Fair value estimates are based on loans and leases with similar financial characteristics. Loans and leases have been segregated by homogenous groups into residential mortgage, commercial, and consumer and other loans. Fair values are estimated by discounting contractual cash flows, adjusted for prepayment estimates, using discount rates approximately equal to current market rates on loans with similar characteristics and maturities. The incremental credit risk for nonperforming loans has been considered in the determination of the fair value of loans.

*Stock in the Federal Home Loan Bank of Boston* The fair value of stock in the FHLB equals the carrying value reported in the balance sheet. This stock is redeemable at full par value only by the FHLB.

*Deposits* The fair values reported for demand deposit, NOW, money market, and savings accounts are equal to their respective book values reported on the balance sheet. The fair values disclosed are, by definition, equal to the amount payable on demand at the reporting date. The fair values reported for certificate of deposit accounts are based on the discounted value of contractual cash flows. The discount rates used are representative of approximate rates currently offered on certificate of deposit accounts with similar remaining maturities. The estimated fair value of deposits does not take into account the value of the Company s long-term relationships with depositors. Nonetheless, the Company would likely realize a core deposit premium if its deposit portfolio was sold in the principal market for such deposits.

*Wholesale repurchase agreements* The fair values reported for wholesale repurchase agreements are based on the discounted value of contractual cash flows. The discount rates used are representative of approximate rates currently offered on borrowings with similar characteristics and maturities.

*Federal Home Loan Bank of Boston borrowings* The fair values reported for FHLB borrowings are based on the discounted value of contractual cash flows. The discount rates used are representative of approximate rates currently offered on borrowings with similar characteristics and maturities.

*Subordinated deferrable interest debentures* The fair values reported for subordinated deferrable interest debentures are based on the discounted value of contractual cash flows. The discount rates used are representative of approximate rates currently offered on instruments with similar terms and maturities.

*Financial instruments with off-balance sheet risk* Since the Bank s commitments to originate or purchase loans, and for unused lines and outstanding letters of credit, are primarily at market interest rates, there is no significant fair value adjustment.

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The book values and estimated fair values for the Company s financial instruments are as follows:

| | March 31, 2011 | | December 31, 2010 | |
|---|---|---|---|---|
| | Book Value | Estimated Fair Value | Book Value | Estimated Fair Value |
| | (In thousands) | | | |
| Assets: | | | | |
| Cash and due from banks | $ 16,573 | $ 16,573 | $ 14,384 | $ 14,384 |
| Overnight investments | 551 | 551 | 395 | 395 |
| Available for sale securities | 361,579 | 361,579 | 360,025 | 360,025 |
| Stock in the FHLB | 16,274 | 16,274 | 16,274 | 16,274 |
| Loans and leases receivable, net of allowance for loan and lease losses: | | | | |
| Commercial loans and leases | 769,109 | 779,422 | 765,446 | 776,737 |
| Residential mortgage loans | 158,795 | 164,037 | 162,904 | 166,744 |
| Consumer and other loans | 208,322 | 201,776 | 208,485 | 203,545 |
| Interest rate swaps | 614 | 614 | 790 | 790 |
| Accrued interest receivable | 4,411 | 4,411 | 4,842 | 4,842 |
| Liabilities: | | | | |
| Deposits: | | | | |
| Demand deposit accounts | $ 254,291 | $ 254,291 | $ 264,274 | $ 264,274 |
| NOW accounts | 65,127 | 65,127 | 70,327 | 70,327 |
| Money market accounts | 113,126 | 113,126 | 96,285 | 96,285 |
| Savings accounts | 343,286 | 343,286 | 341,667 | 341,667 |
| Certificate of deposit accounts | 325,831 | 327,327 | 347,613 | 349,386 |
| Overnight and short-term borrowings | 36,068 | 36,068 | 40,997 | 40,997 |
| Wholesale repurchase agreements | 19,801 | 19,896 | 20,000 | 20,190 |
| FHLB borrowings | 273,582 | 298,895 | 260,889 | 285,819 |
| Subordinated deferrable interest debentures | 13,403 | 15,649 | 13,403 | 15,645 |
| Interest rate swaps | 649 | 649 | 832 | 832 |
| Accrued interest payable | 1,244 | 1,244 | 1,616 | 1,616 |

**(9) Contingent Liabilities**

In June 2009, the Bank received a Notice of Assessment from the Massachusetts Department of Revenue ( DOR ) challenging the 2002 to 2006 state income tax due from BRI Investment Corp., a Rhode Island passive investment company. The DOR seeks to collapse the income from BRI Investment Corp. into the Bank s income and assess state corporate excise tax on the resulting apportioned income. The passive investment company is not subject to corporate income tax in the State of Rhode Island. The Bank filed an Application for Abatement in September 2009 contesting the assessment and asserting its position. The Bank was notified in March 2010 that the application was denied and subsequently filed a petition with the Massachusetts Appellate Tax Board pursuing its position.

In June 2010, the DOR performed an audit of tax years 2007 and 2008, challenging the Bank s position of the tax treatment of BRI Investment Corp. under the same assertion. The Bank received a Notice of Assessment from the DOR in November 2010. The total estimated tax assessment, accrued interest and penalties for all years is $700,000. As a result of 2008 amendments to tax law, the Company filed the 2009 Massachusetts income tax return and will continue to file future Massachusetts income tax returns on a combined reporting basis. There are no further tax years available for audit under the statute of limitations. Management believes it more likely than not that the Bank will prevail in its tax position, and therefore has not recorded a contingent liability for this matter.

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On June 5, 2008, Empire Merchandising Corp. ( EMC ) and Joseph Pietrantonio (collectively, the Plaintiffs ) filed a complaint in the Providence County Superior Court against the Bank and EMC s outside accountants, Bernard Labush and Stevan H. Labush, alleging damages arising out of an embezzlement scheme perpetrated by EMC s bookkeeper beginning around January 2004 and continuing until September 2005. EMC had checking and payroll accounts and a $250,000 line of credit with the Bank. Mr. Pietrantonio personally guaranteed EMC s repayment obligations under the line of credit, which was secured by a first security interest in all of EMC s assets. The Plaintiffs allege that the Bank made unauthorized advances to EMC under the line of credit via online requests by the bookkeeper, failed to take reasonable and necessary measures to ensure authorized access to EMC s accounts and failed to notify Mr. Pietrantonio of unusual overdraft activity in the EMC accounts, all of which facilitated the embezzlement scheme and ultimately led to the final collapse of EMC in January 2007. In addition, EMC alleges that the Bank should have forgiven the line of credit indebtedness and released its lien on EMC s assets and that the Bank s failure to do so prevented EMC from obtaining additional financing and contributed to the demise of EMC s business. The Plaintiffs asserted the following causes of action against the Bank: breach of contract, breach of implied covenant of good faith and fair dealing, negligence, infliction of emotional distress, unjust enrichment and interference with advantageous relationship. The Bank denied any liability and asserted a counterclaim seeking repayment of indebtedness due under the line of credit and the personal guaranty of Mr. Pietrantonio.

The case was tried before a jury in February 2011. On March 10, 2011, the jury returned a verdict against the Bank, finding that the Bank was negligent and had breached the line of credit agreement with EMC and that the Bank had intentionally inflicted emotional distress on Mr. Pietrantonio. The jury awarded damages of $1.4 million to EMC for the loss of the business and $500,000 to Mr. Pietrantonio for lost wages and emotional distress. On March 30, 2011, the Court issued a judgment against Bank Rhode Island for $3.2 million comprising the following: (i) $2.4 million, including prejudgment interest of $1.0 million, for breach of contract; (ii) on the negligence claim, $2.4 million, including $1.0 million prejudgment interest, reduced by 15% under Rhode Island s comparative negligence statute, which award the Court ruled was duplicative of the breach of contract award; (iii) $220,000, including prejudgment interest of $72,000, for lost wages; and (iv) $580,000, including prejudgment interest of $231,000, for intentional infliction of emotional distress. The Company expects insurance to cover a substantial portion of the damages awarded in addition to certain expenses incurred as a result of the litigation process. For the three months ended March 31, 2011, the Company has recorded $745,000, the amount not expected to be covered by insurance, in other expenses in the Company s consolidated financial statements related to the judgment. The Company has filed post trial motions challenging the verdict and will appeal any adverse judgment to the Rhode Island Supreme Court.

**(10) Transfers and Servicing**

The Bank routinely enters into loan and lease participations with third parties. In accordance with U.S. GAAP, these participations are accounted for as sales and, therefore, are not included in the Company s consolidated financial statements. In some cases, the Bank has continuing involvement with the loan and lease participations in the form of servicing. Servicing of the loan and lease participations typically involves collecting principal and interest payments and monitoring delinquencies on behalf of the assigned party of the participation. The Bank typically receives just adequate compensation for its servicing responsibilities. As such, there are no servicing assets or liabilities recorded in the Company s consolidated financial statements at March 31, 2011 or December 31, 2010.

Through its Macrolease platform, the Bank has a recourse obligation under a lease sale agreement for up to 8.0% of the original sold balance of approximately $9.8 million. Historically, delinquency rates for the lease portfolio have been significantly lower. At March 31, 2011 and December 31, 2010, a liability for the recourse obligation of $51,000 and $61,000 respectively, was included in the Company s consolidated financial statements.

**(11) Subsequent Events**

On April 19, 2011, the Company and Brookline Bancorp, Inc. ( Brookline Bancorp ) entered into a definitive agreement and plan of merger (the Merger Agreement ) pursuant to which the Company will merge with and into Brookline Bancorp (the Merger ), whereupon the separate corporate existence of the Company will cease and its subsidiary, Bank Rhode Island, will become a wholly-owned subsidiary of Brookline Bancorp.

The Merger Agreement has been unanimously approved by the board of directors of each of the Company and Brookline Bancorp. Subject to the approval of the Merger by the Company s shareholders, regulatory approvals and other customary closing conditions, the parties anticipate completing the Merger in the fourth quarter of 2011.

Under the terms of the Merger Agreement, shareholders of the Company will receive, for each share of Company common stock and at the holder s election, either $48.25 in cash, or 4.686 shares of Brookline Bancorp common stock or a combination thereof, provided that, subject to certain adjustments, 2,347,000 shares of the Company s common stock (representing approximately 50% of the Company s shares outstanding on the date of the Merger Agreement) will be converted into Brookline Bancorp common stock and the remaining shares of the Company s common stock will be converted into cash. The total cash consideration will be approximately $121.0 million and total stock consideration will consist of approximately 11.0 million shares of Brookline Bancorp common stock. Elections will be subject to allocation procedures that are intended to ensure that approximately 50% of the outstanding shares of the Company s common stock will be converted into Brookline Bancorp common stock. The receipt of Brookline Bancorp common stock by shareholders of the Company is expected to be tax-free.

The Company s stock options, restricted stock and performance share awards will become fully vested upon completion of the Merger. Stock options will be cancelled and the holder will receive, for each share subject to an option, cash equal to the difference between the exercise price for the option and $48.25, net of all applicable withholding taxes. Each performance share award will be cancelled and the holder will receive $48.25 in cash for each performance share earned in accordance with the terms governing such award based on performance calculated through the last day of the calendar quarter ending immediately prior to consummation of the Merger, net of all applicable withholding taxes; provided that, for purposes of determining whether such performance shares have been earned, that the Company s earnings per share will be calculated without deduction for the expense attributable to the acceleration of vesting of restricted stock awards and any transaction related expenses.

The Merger Agreement includes customary representations, warranties and covenants of the Company and Brookline Bancorp. The Company has agreed to operate its business in the ordinary course consistent with past practice until the closing of the Merger and not to engage in certain kinds of transactions during such period (without the prior written consent of Brookline Bancorp). The Company also has agreed to cease all existing, and agreed not to solicit or initiate any additional, discussions with third parties regarding other proposals to acquire the Company, and to certain restrictions on its ability to respond to such proposals, subject to fulfillment of certain fiduciary requirements of its Board of Directors.

The Merger Agreement also includes certain termination provisions for both Brookline Bancorp and the Company and provides that, in connection with the termination of the Merger Agreement under specified circumstances, the Company may be required to pay Brookline Bancorp a termination fee of $8,900,000.

*ITEM 2. Management s Discussion and Analysis*

**General**

The Company s principal subsidiary, Bank Rhode Island, is a commercial bank chartered as a financial institution in the State of Rhode Island. The Bank pursues a community banking mission and is principally engaged in providing banking products and services to businesses and individuals in Rhode Island and nearby areas of Massachusetts. The Bank offers its customers a wide range of business, commercial real estate, consumer and residential loans and leases, deposit products, nondeposit investment products, cash management, private banking and other banking products and services designed to meet the financial needs of individuals and small- to mid-sized businesses. The Bank also offers both commercial and consumer online banking products and maintains a web site at http://www.bankri.com. The Bank competes with a variety of traditional and nontraditional financial service providers both within and outside of Rhode Island. The Company and Bank are subject to the regulations of certain federal and state agencies and undergo periodic examinations by certain of those regulatory authorities. The Bank s deposits are insured by the FDIC, subject to regulatory limits. The Bank is also a member of the Federal Home Loan Bank of Boston ( FHLB ). The Company s common stock is traded on the Nasdaq Global Select Market$^{SM}$ under the symbol BARI. The Company s financial reports can be accessed through its website within 24 hours of filing with the SEC.

**Critical Accounting Policies**

Accounting policies involving significant judgments and assumptions by management, which have, or could have, a material impact on the carrying value of certain assets or net income, are considered critical accounting policies. The preparation of financial statements in accordance with accounting principles generally accepted in the United States ( U.S. GAAP ) requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and disclosure of contingent assets and liabilities. Actual results could differ from those estimates. As discussed in the Company s 2010 Annual Report on Form 10-K, management has identified the accounting for the allowance for loan and lease losses, review of goodwill for impairment, valuation of available for sale securities and income taxes as the Company s most critical accounting policies.

**Overview**

The primary drivers of the Company s operating income are net interest income, which is strongly affected by the net yield on interest-earning assets and liabilities ( net interest margin ), and the quality of the Company s assets.

The Company s net interest income represents the difference between interest income and its cost of funds. Interest income depends on the amount of interest-earning assets outstanding during the year and the interest rates earned thereon. Cost of funds is a function of the average amount of deposits and borrowed money outstanding during the year and the interest rates paid thereon. The net interest margin is calculated by dividing net interest income by average interest-earning assets. Net interest spread is the difference between the average rate earned on interest-earning assets and the average rate paid on interest-bearing liabilities. Net interest margin generally exceeds the net interest spread as a portion of interest-earning assets is funded by various noninterest-bearing sources (primarily noninterest-bearing deposits and shareholders equity). The increases (decreases) in the components of interest income and interest expense, expressed in terms of fluctuation in average volume and rate, are summarized under *Rate/Volume Analysis* on page 41. Information as to the components of interest income and interest expense and average rates is provided under *Average Balances, Yields and Costs* on page 40.

Because the Company s assets are not identical in duration and in repricing dates to its liabilities, the spread between the two is vulnerable to changes in market interest rates as well as the overall shape of the yield curve. These vulnerabilities are inherent to the business of banking and are commonly referred to as interest rate risk. How to measure interest rate risk and, once measured, how much risk to take are based on numerous assumptions and other subjective judgments. See also discussion under *Interest Rate Risk* on page 44.

The quality of the Company s assets also influences its earnings. Loans and leases that are not paid on a timely basis and exhibit other weaknesses can result in the loss of principal and/or interest income. Additionally, the Company must make timely provisions to the allowance for loan and lease losses based on estimates of probable losses inherent in the loan and lease portfolio; these additions, which are charged against earnings, are necessarily greater when greater probable losses are expected. Further, the Company incurs expenses as a result of resolving troubled assets. All of these reflect the credit risk that the Company takes on in the ordinary course of business and are further discussed under *Financial Condition Asset Quality* on pages 34 to 36.

The Company s business strategy has been to concentrate its asset generation efforts on commercial and consumer loans and its deposit generation efforts on demand deposit, NOW, money market and savings accounts. These deposit accounts are commonly referred to as core deposits. This strategy is based on the Company s belief that it can distinguish itself from its larger competitors, and indeed attract customers from them, through a higher level of service and through its ability to set policies and procedures, as well as make decisions, locally. The loan and deposit products referenced also tend to be geared more toward customers who are relationship oriented than those who are seeking stand-alone or single transaction products. The Company believes that its service-oriented approach enables it to compete successfully for relationship-oriented customers. Additionally, the Company is predominantly an urban franchise with a high concentration of businesses, which makes deployment of funds in the commercial lending area practicable. Commercial loans are attractive to the Company, among other reasons, because of their higher yields. Similarly, core deposits are attractive to the Company because of their generally lower interest cost and potential for fee income.

The deposit market in Rhode Island is highly concentrated. The State s three largest banks have an aggregate market share of approximately 88% (based upon June 2010 FDIC statistics, excluding one bank that draws its deposits primarily from the internet) in Providence and Kent Counties, the Bank s primary marketplace. Competition for loans and deposits remains intense. This competition has resulted in considerable advertising and promotional product offerings by competitors, including print, radio and television media, as well as, web-based advertising and promotions.

The Company also seeks to leverage business opportunities presented by its customer base, franchise footprint and resources. In 2005, the Bank completed the acquisition of an equipment leasing company located in Long Island, New York ( Macrolease ) and formed a private banking division. Historically, the Bank has used the Macrolease platform to generate additional income by originating equipment loans and leases for third parties and to grow the loan and lease portfolio. Due to the lack of purchasers in the market during recent years, the amount of Macrolease-generated loans and leases held by the Bank has grown substantially. Currently, the Bank seeks to maintain the level of Macrolease-generated loans and leases at approximately $100.0 million. Additionally, the Bank continues to seek generation of additional income by originating equipment loans and leases for third parties as opportunities arise.

For the three months ended March 31, 2011, approximately 85% of the Company s revenues (defined as net interest income plus noninterest income) were derived from its net interest income. In a continuing effort to diversify its sources of revenue, the Company has sought to expand its sources of noninterest income (primarily fees and charges for products and services the Bank offers). Service charges on deposit accounts remain the largest component of noninterest income. The future operating results of the Company will depend upon the ability to maintain its net interest margin, while minimizing its exposure to credit risk, along with increasing sources of noninterest income, while controlling the growth of noninterest or operating expenses.

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**Financial Condition Executive Summary**

Selected balance sheet data is presented in the table below as of the dates indicated:

| | March 31, 2011 | December 31, 2010 | September 30, 2010 | June 30, 2010 | March 31, 2010 |
|---|---|---|---|---|---|
| | *(Dollars in thousands, except per share data)* | | | | |
| Total assets | $ 1,606,508 | $ 1,603,759 | $ 1,573,323 | $ 1,613,520 | $ 1,586,778 |
| Loans and leases receivable | 1,154,448 | 1,155,489 | 1,135,227 | 1,136,524 | 1,123,838 |
| Available for sale securities | 361,579 | 360,025 | 342,080 | 345,566 | 365,110 |
| Goodwill, net | 12,262 | 12,262 | 12,262 | 12,262 | 12,262 |
| Core deposits [1] | 775,830 | 772,553 | 755,105 | 813,697 | 728,969 |
| Certificates of deposit | 325,831 | 347,613 | 360,578 | 360,323 | 378,102 |
| Borrowings | 342,854 | 335,289 | 301,455 | 294,137 | 341,344 |
| Common shareholders equity | 130,192 | 128,678 | 130,769 | 129,127 | 123,679 |
| Book value per common share | 27.77 | 27.53 | 27.98 | 27.63 | 26.69 |
| Tangible book value per common share | 25.15 | 24.91 | 25.35 | 25.00 | 24.05 |
| Tangible common equity ratio [2] [3] | 7.40% | 7.31% | 7.59% | 7.30% | 7.08% |
| Core deposits to total deposits[1] [3] | 70.4% | 69.0% | 67.7% | 69.3% | 65.8% |

(1) Core deposits consist of demand deposit, NOW, money market and savings accounts.

(2) Calculated by dividing common shareholders equity less goodwill by total assets less goodwill.

(3) Non-GAAP performance measure.

Total assets increased by $2.7 million since December 31, 2010. Total loans and leases decreased by $1.0 million during the first three months of 2011, with an increase in commercial loans and leases of $3.4 million, or 0.4%. This increase was offset by decreases in the residential mortgage loan portfolio of $4.2 million, or 2.6%, and consumer and other loans of $254,000, or 0.1%. Available for sale securities increased $1.6 million, or 0.4%, since year-end. The Bank s core deposits increased by $3.3 million, or 0.4%, since year-end. Within this increase, money market accounts increased by $16.8 million, or 17.5%, and savings accounts increased by $1.6 million, or 0.5%. Certificate of deposit accounts decreased by $21.8 million, or 6.3%, demand deposit accounts decreased by $10.0 million, or 3.8%, and NOW accounts decreased by $5.2 million, or 7.4%, since year-end. Borrowings increased by $7.6 million, or 2.3%, since December 31, 2010. Shareholders equity as a percentage of total assets was 8.1% and 8.0% at March 31, 2011 and December 31, 2010, respectively.

The Company s financial position at March 31, 2011 as compared to March 31, 2010 reflects net growth of $30.6 million in total loans and leases. This increase reflects the continuing conversion of the balance sheet to a more commercial profile with increases in commercial loans and leases of $31.5 million, or 4.2%. Consumer loans increased $8.6 million, or 4.3%, from the prior year quarter-end. The residential mortgage portfolio declined $9.5 million, or 5.6%, from March 31, 2010. Available for sale securities at March 31, 2011 decreased by $3.5 million, or 1.0%, from the same period in 2010. Core deposits have increased $46.9 million, or 6.4%, since the prior year quarter-end, with growth centered in demand deposit accounts of $51.1 million and money market accounts of $34.3 million. These increases were offset by decreases in certificate of deposit accounts ( CDs ) of $52.3 million,

savings accounts of $34.9 million and NOW accounts of $3.6 million since March 31, 2010. Borrowings have increased by $1.5 million from the same period in 2010.

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**Financial Condition Detailed Analysis**

*Investments*

Total investments consist of available for sale securities, stock in the FHLB and overnight investments. Total investments comprised $378.4 million, or 23.6% of total assets at March 31, 2011, compared to $376.7 million, or 23.5% of total assets at December 31, 2010, representing an increase of $1.7 million, or 0.5%. Available for sale securities are recorded at fair value. At March 31, 2011, the fair value of available for sale securities was $361.6 million and carried a total of $2.3 million of net unrealized gains at the end of the quarter, compared to $2.6 million at December 31, 2010.

The investment portfolio provides the Company a source of short-term liquidity and acts as a counterbalance to loan and deposit flows. During the first three months of 2011, the Company purchased $30.1 million of available for sale securities compared to $31.3 million during the same period in 2010. Maturities, calls and principal repayments totaled $39.1 million for the three months ended March 31, 2011 compared to $41.1 million for the same period in 2010. Additionally, in the first three months of 2011, the Company sold $4.2 million of available for sale securities generating gains of $212,000 compared to sales of $8.8 million and gains of $475,000 for the same period in 2010.

The Company performs regular analysis on the available for sale securities portfolio to determine whether a decline in fair value indicates that an investment is other-than-temporarily impaired. In making these other-than-temporary determinations, management considers, among other factors, the length of time and extent to which the fair value has been less than amortized cost, projected future cash flows, credit subordination and the creditworthiness, capital adequacy and near-term prospects of the issuers. Management also considers the Company s capital adequacy, interest rate risk, liquidity and business plans in assessing whether it is more likely than not that the Company will sell or be required to sell the securities before recovery.

If the Company determines that a decline in fair value is other-than-temporary and that it is more likely than not that the Company will not sell or be required to sell the security before recovery of its amortized cost, the credit portion of the impairment loss is recognized in earnings and the noncredit portion is recognized in accumulated other comprehensive income. The credit portion of the other-than-temporary impairment represents the difference between the amortized cost and the present value of the expected future cash flows of the security. If the Company determines that a decline in fair value is other-than-temporary and it will more likely than not sell or be required to sell the security before recovery of its amortized cost, the entire difference between the amortized cost and the fair value of the security will be recognized in earnings.

In performing the analysis for the two collateralized debt obligations ( CDO A and CDO B ) held by the Company, which are backed by pools of trust preferred securities, future cash flow scenarios for each security were estimated based on varying levels of severity for assumptions of future delinquencies, recoveries and prepayments. These estimated cash flow scenarios were used to determine whether the Company expects to recover the amortized cost basis of the securities. Projected credit losses were compared to the current level of credit enhancement to assess whether the security is expected to incur losses in any future period and therefore become other-than-temporarily impaired.

CDO A has experienced $99.0 million, or 42.8%, in deferrals/defaults of the security s underlying collateral to date, including an additional $5.0 million during the first quarter of 2011. Projected credit loss severity assumptions were increased in estimated future cash flow scenarios and it was determined that management expects to recover the security s amortized cost. At March 31, 2011, credit related other-than-temporary impairment losses on this security since its purchase totaled $484,000.

CDO B has experienced $176.5 million, or 30.6%, in deferrals/defaults of the security s underlying collateral to date. The Company has not received its scheduled quarterly interest payments since June 30, 2009 because the security is adding interest to the principal rather than paying out. Projected credit loss severity assumptions were increased in estimated future cash flow scenarios and it was determined that management expects to recover the security s amortized cost. At March 31, 2011, credit related other-than-temporary impairment losses on this security since its purchase totaled $932,000.

The decline in fair value of the remaining available for sale securities in an unrealized loss position is due to general market concerns of the liquidity and creditworthiness of the issuers of the securities. Management believes that it will recover the amortized cost basis of the securities and that it is more likely than not that it will not sell the securities before recovery. As such, management has determined that the securities are not other-than-temporarily impaired as of March 31, 2011. If market conditions for securities worsen or the creditworthiness of the underlying issuers deteriorates, it is possible that the Company may recognize additional other-than-temporary impairments in future periods.

*Loans and Leases*

Total loans and leases decreased by $1.0 million since December 31, 2010 and stood at $1.15 billion at March 31, 2011. As a percentage of total assets, loans and leases increased to 71.9% at March 31, 2011, compared to 72.0% at December 31, 2010. This decrease was centered in residential mortgage loans, which the Company has historically purchased and was partially offset by increases in commercial loans, where the Company concentrates its origination efforts. Total loans and leases as of March 31, 2011 are comprised of three broad categories: commercial loans and leases that aggregate $783.7 million, or 67.9% of the portfolio; residential mortgages that aggregate $160.7 million, or 13.9% of the portfolio; and consumer and other loans that aggregate $210.1 million, or 18.2% of the portfolio.

*Commercial loans and leases* The commercial loan and lease portfolio (consisting of commercial real estate, commercial and industrial, equipment leases, multifamily real estate, construction and small business loans) increased $3.4 million, or 0.4%, during the three months of 2011.

The Bank s business lending group originates business loans, also referred to as commercial and industrial loans. In addition, Macrolease-generated equipment loans are included in the commercial and industrial loan portfolio. Total commercial and industrial loans increased $3.1 million, or 2.0%, since year-end.

The Bank s business lending group also originates owner-occupied commercial real estate loans, term loans and revolving lines of credit. Since December 31, 2010, owner-occupied commercial real estate loans increased by $3.3 million, or 1.9%.

The Bank s commercial real estate ( CRE ) group originates nonowner-occupied commercial real estate, multifamily residential real estate and construction loans. These real estate secured commercial loans are offered as both fixed and adjustable-rate products. Since December 31, 2010, CRE loans have decreased $1.7 million, or 0.6%.

The Bank purchases equipment leases from originators outside of the Bank. The U.S. Government or its agencies are the principal lessees on these purchased leases. These government leases generally have maturities of less than fifteen years and are not dependent on residual collateral values. At March 31, 2011, $19.0 million of purchased government leases were included in the commercial loan and lease portfolio representing a decrease of $949,000, or 4.8%, since year-end.

With the Macrolease platform, the Bank originates and purchases equipment loans and leases for its own portfolio, as well as originates loans and leases for third parties as a source of noninterest income. Macrolease-generated equipment loans of $40.4 million and $40.8 million were included in the commercial and industrial portfolio at March 31, 2011 and December 31, 2010, respectively. Macrolease-generated equipment leases were $48.4 million at March 31, 2011 and December 31, 2010. Since December 31, 2010, total Macrolease-generated equipment loans and leases decreased $369,000, or 0.4%, to $88.8 million.

At March 31, 2011, small business loans (business lending relationships of approximately $500,000 or less) were $62.2 million compared to $62.8 million at December 31, 2010. At March 31, 2011 and December 31, 2010, small business loans represented 7.9% and 8.1%, respectively, of the commercial loan and lease portfolio. These loans reflect those originated by the Bank s business development group, as well as throughout the Bank s branch system. The Bank utilizes credit scoring and streamlined documentation, as well as traditional review standards, in originating these credits.

The Bank is a participant in the U.S. Small Business Administration ( SBA ) Lender Program in both Rhode Island and Massachusetts. The Bank was named the No. 1 SBA lender in Rhode Island for the second consecutive year as of the SBA s September 30, 2010 fiscal year end. SBA guaranteed loans exist throughout the portfolios managed by the Bank s various lending groups.

The Company believes it is well positioned for continued commercial growth. The Bank places particular emphasis on the generation of small- to medium-sized commercial relationships (those with $10.0 million or less in total loan commitments).

*Residential mortgage loans* Since inception, the Bank has concentrated its portfolio lending efforts on commercial and consumer lending opportunities. Historically, the Bank has purchased high credit quality residential mortgage loans from third-party originators and, on a limited basis, originated mortgage loans for its own portfolio. In 2010, the Bank hired three mortgage loan originators and increased its mortgage origination efforts. At March 31, 2011, residential mortgage loans decreased $4.2 million, or 2.6%, to $160.7 million from year-end. During this period, the Bank originated $7.0 million of mortgages for the portfolio. Comparatively, during the first three months of 2010, the Bank originated $2.6 million of mortgages for the portfolio.

*Consumer loans* The consumer loan portfolio decreased $254,000, or 0.1%, during the first three months of 2011 as repayments of $10.7 million exceeded advances of $10.4 million. The Company continues to offer consumer lending as it believes that these amortizing fixed rate products, along with floating rate lines of credit, possess attractive cash flow characteristics.

The following is a summary of loans and leases receivable:

| | March 31, 2011 | December 31, 2010 |
|---|---|---|
| | *(In thousands)* | |
| **Commercial loans and leases:** | | |
| Commercial real estate nonowner occupied | $ 196,353 | $ 200,809 |
| Commercial real estate owner occupied | 183,111 | 179,766 |
| Commercial and industrial | 161,004 | 157,879 |
| Multifamily | 84,772 | 79,934 |
| Small business | 62,233 | 62,841 |
| Construction | 28,273 | 30,349 |
| Leases and other | 72,156 | 73,054 |
| Subtotal | 787,902 | 784,632 |
| Unearned lease income | (5,962) | (6,159) |
| Net deferred loan origination costs | 1,756 | 1,791 |
| Total commercial loans and leases | 783,696 | 780,264 |
| **Residential mortgage loans:** | | |
| One- to four-family adjustable rate | 100,976 | 106,341 |
| One- to four-family fixed rate | 59,106 | 57,948 |
| Subtotal | 160,082 | 164,289 |
| Premium on loans acquired | 576 | 598 |
| Net deferred loan origination fees | | (10) |
| Total residential mortgage loans | 160,658 | 164,877 |

| | | |
|---|---|---|
| **Consumer loans:** | | |
| Home equity term loans | 125,639 | 125,114 |
| Home equity lines of credit | 82,038 | 82,778 |
| Unsecured and other | 1,489 | 1,511 |
| Subtotal | 209,166 | 209,403 |
| Net deferred loan origination costs | 928 | 945 |
| Total consumer loans | 210,094 | 210,348 |
| Total loans and leases receivable | $ 1,154,448 | $ 1,155,489 |

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*Deposits*

Total deposits decreased by $18.5 million, or 1.7%, during the first three months of 2011, from $1.12 billion, or 69.8% of total assets at December 31, 2010, to $1.10 billion, or 68.6% of total assets at March 31, 2011.

The following table sets forth certain information regarding deposits:

| | March 31, 2011 | | | December 31, 2010 | | |
|---|---|---|---|---|---|---|
| | Amount | Percent Of Total | Weighted Average Rate | Amount | Percent of Total | Weighted Average Rate |
| | | | (In thousands) | | | |
| NOW accounts | $ 65,127 | 5.9% | 0.06% | $ 70,327 | 6.3% | 0.06% |
| Money market accounts | 113,126 | 10.3% | 0.66% | 96,285 | 8.6% | 0.68% |
| Savings accounts | 343,286 | 31.1% | 0.32% | 341,667 | 30.5% | 0.32% |
| Certificate of deposit accounts | 325,831 | 29.6% | 1.05% | 347,613 | 31.0% | 1.34% |
| Total interest bearing deposits | 847,370 | 76.9% | 0.63% | 855,892 | 76.4% | 0.75% |
| Noninterest bearing accounts | 254,291 | 23.1% | 0.00% | 264,274 | 23.6% | 0.00% |
| Total deposits | $ 1,101,661 | 100.0% | 0.48% | $ 1,120,166 | 100.0% | 0.58% |

During the first three months of 2011, competition for deposits remained strong in the Company s market areas. CDs, demand deposit accounts and NOW accounts declined by $21.8 million, $10.0 million and $5.2 million, respectively, compared to year-end. These decreases were offset by growth in money market accounts of $16.8 million and savings accounts of $1.6 million. At March 31, 2011, brokered CDs were $36.3 million, or 3.3% of total deposits, compared to $30.0 million, or 2.7%, at year-end. The Bank may continue to utilize brokered CDs if rates are attractive compared to wholesale funding.

*Borrowings*

On a long-term basis, the Company intends to continue concentrating on increasing its core deposits and may utilize FHLB borrowings or repurchase agreements as cash flows dictate, as opportunities present themselves and as part of the Bank s overall strategy to manage interest rate risk. The Bank also may borrow from the Federal Reserve discount window on occasion to support its liquidity.

The Bank routinely enters into repurchase agreements with its larger deposit and commercial customers as part of its cash management services. These repurchase agreements represent an additional source of funds and are typically overnight borrowings. Repurchase agreements with Bank customers totaled $35.4 million and $39.3 million at March 31, 2011 and December 31, 2010, respectively. The Bank also borrows funds through the use of wholesale repurchase agreements with correspondent banks. Overnight and short-term borrowings decreased $4.9 million during the first three months of 2011 from the December 31, 2010 level of $41.0 million. FHLB borrowings increased by $12.7 million from the December 31, 2010 amount of $260.9 million. Wholesale repurchase agreements declined $199,000 compared to the December 31, 2010 balance of $20.0 million.

*Asset Quality*

Nonperforming assets consist of nonperforming loans and other real estate owned ( OREO ). Nonperforming loans nonaccrual loans, loans past due 90 days or more, but still accruing and impaired loans. Under certain circumstances the Company may restructure the terms of a loan as a concession to a borrower. These restructured loans are generally considered nonperforming loans until a history of collection on the restructured terms of the loan has been established. OREO consists of real estate acquired through foreclosure proceedings and real estate acquired through acceptance of

a deed in lieu of foreclosure.

*Nonperforming assets* At March 31, 2011, the Company had nonperforming assets of $17.5 million, representing 1.09% of total assets compared to nonperforming assets of $17.6 million, or 1.10% of total assets, at December 31, 2010.

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The following table sets forth information regarding nonperforming assets and loans and leases 60-89 days past due as of the dates indicated:

| | March 31, 2011 | December 31, 2010 |
|---|---|---|
| | (In thousands) | |
| Loans and leases accounted for on a nonaccrual basis | $ 13,840 | $ 15,069 |
| Loans and leases past due 90 days or more, but still accruing | 645 | |
| Restructured loans and leases on a nonaccrual basis | 1,413 | 1,444 |
| Total nonperforming loans and leases | 15,898 | 16,513 |
| Other real estate owned | 1,575 | 1,130 |
| Total nonperforming assets | $ 17,473 | $ 17,643 |
| Delinquent loans and leases 60-89 days past due | $ 3,179 | $ 2,429 |
| Restructured loans and leases not included in nonperforming assets | 481 | 485 |
| Nonperforming loans and leases as a percent of total loans and leases | 1.38% | 1.43% |
| Nonperforming assets as a percent of total assets | 1.09% | 1.10% |
| Delinquent loans and leases 60-89 days past due as a percent of total loans and leases | 0.28% | 0.21% |

Included in nonaccrual loans and leases at March 31, 2011 were $9.6 million of impaired loans and leases with specific impairment reserves against these loans and leases of $651,000. At December 31, 2010, there were $10.8 million of impaired loans and leases with specific impairment reserves of $1.5 million.

The following table provides further detailed information regarding the types of nonperforming loans and leases as of the dates indicated:

| | March 31, 2011 | December 31, 2010 |
|---|---|---|
| | (In thousands) | |
| Nonperforming loans and leases: | | |
| Commercial real estate | $ 4,792 | $ 5,272 |
| Commercial and industrial | 2,255 | 2,462 |
| Multifamily | 1,050 | 717 |
| Small business | 1,059 | 1,090 |
| Construction | 232 | 470 |
| Leases | 591 | 581 |
| Residential | 4,926 | 5,045 |
| Consumer | 993 | 876 |
| Total nonperforming loans and leases | $ 15,898 | $ 16,513 |

The Company evaluates the underlying collateral of each nonperforming loan and lease and continues to pursue the collection of interest and principal. Management believes that the current level of nonperforming assets remains low relative to the size of the Company s loan portfolio and as compared to peer institutions. If economic conditions were to worsen or if the marketplace experiences prolonged economic stress, management believes it is likely that the level of nonperforming assets would increase, as would the level of charged-off loans.

*Higher-Risk Loans* Certain types of loans, such as option ARM products, junior lien loans, high loan-to-value ratio loans, interest only loans, subprime loans and loans with initial teaser rates, can have a greater risk of non-collection than other loans. Additional information about higher-risk loans may be useful in understanding the risks associated with the loan portfolio and in evaluating any known trends or uncertainties that could have a material impact on the results of operations.

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The following table sets forth information regarding loan balances that may have higher risk and the related allowance for loan and lease losses for these loans.

| | March 31, 2011 | | December 31, 2010 | |
|---|---|---|---|---|
| | Principal Balance | Allowance for Loan and Lease Losses | Principal Balance | Allowance for Loan and Lease Losses |
| | (In thousands) | | | |
| Option ARM mortgages | $ 1,119 | $ 11 | $ 1,124 | $ 11 |
| Interest-only residential first mortgages | 21,852 | 995 | 23,531 | 235 |
| Junior lien home equity loans | 39,226 | 351 | 40,919 | 363 |
| Junior lien home equity lines of credit | 59,206 | 533 | 60,262 | 539 |
| Total higher-risk loans | $ 121,403 | $ 1,890 | $ 125,836 | $ 1,148 |

At March 31, 2011 and December 31, 2010, the above higher risk loans had weighted average credit scores of 739.

*Watch List Assets* The Company s management negatively classifies certain assets as special mention or substandard based on criteria established under banking regulations. These negatively classified loans and leases are collectively referred to as watch list assets. Loans and leases classified as special mention have potential weaknesses that deserve management s close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects of the loan or lease at some future date. Loans and leases categorized as substandard are inadequately protected by the payment capacity of the obligor or of the collateral pledged, if any. Substandard loans and leases have a well-defined weakness or weaknesses that jeopardize the liquidation of debt and are characterized by the distinct possibility that the Company will sustain some loss if existing deficiencies are not corrected.

Loans and leases classified as special mention totaled $17.7 million and $20.9 million at March 31, 2011 and December 31, 2010, respectively.

At March 31, 2011, the Company had $30.8 million of assets that were classified as substandard. This compares to $28.8 million of assets that were classified as substandard at December 31, 2010. The Company had no assets that were classified as loss or doubtful at either date. Performing loans may or may not be adversely classified depending upon management s judgment with respect to each individual loan. At March 31, 2011, included in the assets that were classified as substandard were $14.9 million of performing loans. This compares to $12.3 million of adversely classified performing loans as of December 31, 2010. These amounts constitute assets that, in the opinion of management, could potentially migrate to nonperforming or doubtful status. If economic conditions were to worsen or if the marketplace experiences prolonged economic stress, management believes it is likely that the level of adversely classified assets would increase. This in turn may necessitate further increases to the provision for loan losses in future periods.

*Allowance for Loan and Lease Losses*

During the first three months of 2011, the Company made additions to the allowance for loan and lease losses of $1.1 million and experienced net charge-offs of $1.6 million compared to additions to the allowance for loan and lease losses of $1.6 million and net charge-offs of $1.5 million for the first three months of 2010. The net charge-offs were primarily within the residential mortgage and commercial loan and lease portfolios. At March 31, 2011, the allowance for loan and lease losses stood at $18.2 million and represented 114.62% of nonperforming loans and leases and 1.58% of total loans and leases outstanding. This compares to an allowance for loan and lease losses of $18.7 million, representing 112.97% of nonperforming loans and leases and 1.61% of total loans and leases outstanding at December 31, 2010.

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An analysis of the activity in the allowance for loan and lease losses is as follows:

| | Three Months Ended March 31, 2011 | Three Months Ended March 31, 2010 |
|---|---|---|
| | *(In thousands)* | |
| Balance at beginning of period | $ 18,654 | $ 16,536 |
| Loans and leases charged-off: | | |
| Commercial real estate loans | (532) | (627) |
| Commercial and industrial loans | (109) | |
| Small business loans | (334) | (200) |
| Construction | (237) | |
| Leases | (75) | (336) |
| Residential mortgage loans | (379) | (347) |
| Consumer and other loans | (20) | (102) |
| Total loans charged-off | (1,686) | (1,612) |
| Recoveries of loans and leases previously charged-off: | | |
| Commercial real estate loans | | 79 |
| Commercial and industrial loans | 110 | 11 |
| Small business loans | 1 | 1 |
| Leases | 11 | 6 |
| Residential mortgage loans | | |
| Consumer and other loans | 7 | 4 |
| Total recoveries of loans previously charged-off | 129 | 101 |
| Net charge-offs | (1,557) | (1,511) |
| Provision for loan and lease losses charged against income | 1,125 | 1,600 |
| Balance at end of period | $ 18,222 | $ 16,625 |

The following table represents the allocation of the allowance for loan and lease losses as of the dates indicated:

| | March 31, 2011 | December 31, 2010 |
|---|---|---|
| | *(In thousands)* | |
| Loan category | | |
| Commercial loans and leases | $ 12,988 | $ 13,370 |
| Residential mortgage loans | 1,659 | 1,780 |
| Consumer and other loans | 1,578 | 1,681 |
| Unallocated | 1,997 | 1,823 |
| Total | $ 18,222 | $ 18,654 |

Assessing the appropriateness of the allowance for loan and lease losses involves substantial uncertainties and is based upon management s evaluation of the amounts required to meet estimated charge-offs in the loan and lease portfolio after weighing various factors. Management s methodology to estimate loss exposure includes an analysis of individual loans and leases deemed to be impaired, reserve allocations for various loan types based on payment status or loss experience and an unallocated allowance that is maintained based on management s assessment of many factors including the growth, composition and quality of the loan portfolio, historical loss experiences, general economic conditions and other pertinent factors. These risk factors are reviewed and revised by management where conditions indicate that the estimates initially applied are different from actual results. If credit performance is worse than anticipated, the Company could incur additional loan and lease losses in future periods. The unallocated allowance for loan and lease losses was $2.0 million at March 31, 2011 compared to $1.8 million at December 31, 2010. Management believes that the allowance for loan and lease losses as of March 31, 2011 is appropriate.

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While management evaluates currently available information in establishing the allowance for loan and lease losses, future adjustments to the allowance for loan and lease losses may be necessary if conditions differ substantially from the assumptions used in making the evaluations. Management performs a comprehensive review of the allowance for loan and lease losses on a quarterly basis. In addition, various regulatory agencies, as an integral part of their examination process, periodically review a financial institution s allowance for loan and lease losses and carrying amounts of other real estate owned. Such agencies may require the financial institution to recognize additions to the allowance based on their judgments about information available to them at the time of their examination.

**Results of Operations Executive Overview**

Selected income statement, per share data and operating ratios are presented in the table below for the three-month periods indicated:

| | For the three month periods ended | | | | |
|---|---|---|---|---|---|
| | March 31, 2011 | December 31, 2010 | September 30, 2010 | June 30, 2010 | March 31, 2010 |
| | *(Dollars in thousands, except per share data)* | | | | |
| Income statement data: | | | | | |
| Net interest income | $ 13,515 | $ 13,215 | $ 13,478 | $ 13,626 | $ 13,088 |
| Noninterest income | 2,332 | 2,673 | 2,289 | 2,285 | 2,315 |
| Noninterest expense | 11,269 | 9,935 | 10,350 | 10,430 | 10,488 |
| Net income | 2,307 | 2,126 | 2,808 | 2,681 | 2,219 |
| Per share data: | | | | | |
| Diluted earnings per share | $ 0.49 | $ 0.45 | $ 0.60 | $ 0.57 | $ 0.48 |
| Dividends per common share | $ 0.19 | $ 0.19 | $ 0.17 | $ 0.17 | $ 0.17 |
| Operating ratios: | | | | | |
| Net interest margin (1) (5) | 3.58% | 3.49% | 3.61% | 3.67% | 3.52% |
| Return on assets (2) (5) | 0.59% | 0.53% | 0.71% | 0.68% | 0.57% |
| Return on equity (3) (5) | 7.25% | 6.46% | 8.57% | 8.54% | 7.32% |
| Efficiency ratio (4) (5) | 71.11% | 62.53% | 65.64% | 65.55% | 68.09% |

(1) Calculated by dividing annualized net interest income by average interest-earning assets.

(2) Calculated by dividing annualized net income by average total assets.

(3) Calculated by dividing annualized net income applicable to common shares by average common shareholders equity.

(4) Calculated by dividing noninterest expense by net interest income plus noninterest income.

(5) Non-GAAP performance measure.

The Company s 2011 first quarter net income of $2.3 million increased by $181,000, or 8.5%, from the prior quarter (three months ended December 31, 2010). Net income was up $88,000, or 4.0%, on a comparative quarter basis (as compared to the three months ended March 31, 2010). Diluted earnings per common share ( EPS ) were up 8.9% on a linked-quarter basis (as compared to the three months ended December 31, 2010) and increased 2.1% as compared to the same quarter a year ago.

The first quarter 2011 net interest income increased by $300,000, or 2.3%, as compared to the fourth quarter of 2010. The increase in the net interest margin of 9 basis points ( bps ), to 3.58%, was due to the lower cost of liabilities of 11

bps.

Compared to the first quarter of 2010, net interest income increased by $427,000. The decrease in cost of funds of 34 bps exceeded the decrease in the yield on interest-earning assets of 29 bps.

The provision for loan and lease losses of $1.1 million for the three months ended March 31, 2011 decreased by $1.3 million on a linked-quarter basis. In comparison to the first quarter of 2010, the provision for loan and lease losses decreased by $475,000.

Noninterest income for the first quarter of 2011 decreased on a linked-quarter basis by $341,000, with a decrease in loan related fees of $132,000, service charges on deposit accounts of $89,000, net gains on lease sales and commissions on loans originated for others of $45,000 and other miscellaneous income of $42,000.

In comparison to the 2010 first quarter, noninterest income was up $17,000. The Company recognized credit losses on other-than-temporarily impaired securities of $571,000 during the first quarter of 2010, while there were no other-than-temporarily impaired securities during the same period of 2011. Gains on the sale of available for sale securities decreased by $263,000 during the first quarter of 2011, compared to the same period in 2010. Additionally, service charges on deposit accounts decreased $124,000, other miscellaneous income decreased $103,000 and commissions on nondeposit investment products decreased $43,000.

Noninterest expenses increased on a linked-quarter basis by $1.3 million. The Company recorded $745,000 of expenses in connection with an adverse legal judgment that was determined in March 2011. In addition, salaries and employee benefits costs increased $379,000, marketing costs increased $116,000 and loan workout and other real estate costs increased $88,000.

First quarter 2011 noninterest expenses increased $781,000, compared to the first quarter of 2010. In addition to the aforementioned $745,000 adverse legal judgment, marketing costs increased $95,000 and salaries and employee benefits costs increased $91,000, compared to the first quarter a year ago. Offsetting these increases were decreases in loan workout and other real estate owned expenses of $130,000.

The Company s key operating ratios are return on assets, return on equity and the efficiency ratio. For the first quarter of 2011, the return on assets and the return on equity metrics improved on a linked-quarter basis. The efficiency ratio increase to 71.11% from 62.53% compared to the fourth quarter of 2010 was largely driven by the adverse legal judgment. Compared to the same quarter of the prior year, return on assets improved 2 bps, while return on equity and the efficiency ratio declined 7 bps and 302 bps, respectively. The Company continues to focus on growing revenue while controlling the increase in expenses as part of its effort to improve earnings and build shareholder value.

**Results of Operations Comparison of the Three Months Ended March 31, 2011 and 2010**

*General*

Net income for the three months ended March 31, 2011 increased $88,000, or 4.0%, to $2.3 million, or $0.49 per diluted common share, from $2.2 million, or $0.48 per diluted common share, for the same period of 2010.

*Net Interest Income*

Net interest income for the quarter ended March 31, 2011 was up $427,000, or 3.3%, from the $13.1 million earned in the first quarter of 2010. Net interest margin for the first quarter of 2011 of 3.58% increased 6 bps from the net interest margin for the 2010 period of 3.52%. Average earning assets were up $26.1 million, or 1.7%, and average interest-bearing liabilities were down $39.8 million, or 3.2%, from the comparable period a year earlier.

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*Average Balances, Yields and Costs* The following table sets forth certain information relating to the Company s average balance sheet and reflects the average yield on assets and average cost of liabilities for the three month periods indicated. Such yields and costs are derived by dividing income or expense by the average balance of assets or liabilities. Average balances are derived from daily balances and include nonperforming loans and leases. Available for sale securities are stated at amortized cost.

| | For the three months ended March 31, | | | | | |
|---|---|---|---|---|---|---|
| | 2011 | | | 2010 | | |
| **(In thousands)** | **Average Balance** | **Interest Earned/ Paid** | **Average Yield** | **Average Balance** | **Interest Earned/ Paid** | **Average Yield** |
| **Assets** | | | | | | |
| Earning assets: | | | | | | |
| Overnight investments | $ 762 | $ | 0.19% | $ 2,292 | $ 5 | 0.87% |
| Available for sale securities | 355,404 | 3,022 | 3.40% | 372,516 | 3,779 | 4.06% |
| Stock in the FHLB | 16,274 | 12 | 0.31% | 16,274 | | 0.00% |
| Loans and leases receivable: | | | | | | |
| Commercial loans and leases | 777,681 | 10,656 | 5.54% | 730,907 | 10,311 | 5.71% |
| Residential mortgage loans | 163,640 | 1,699 | 4.15% | 172,408 | 2,029 | 4.71% |
| Consumer and other loans | 210,548 | 2,195 | 4.23% | 203,840 | 2,228 | 4.43% |
| Total earning assets | 1,524,309 | 17,584 | 4.65% | 1,498,237 | 18,352 | 4.94% |
| Cash and due from banks | 17,117 | | | 13,451 | | |
| Allowance for loan and lease losses | (18,528) | | | (17,225) | | |
| Premises and equipment | 11,797 | | | 12,359 | | |
| Goodwill, net | 12,262 | | | 12,179 | | |
| Accrued interest receivable | 4,269 | | | 4,372 | | |
| Bank-owned life insurance | 31,388 | | | 30,118 | | |
| Prepaid expenses and other assets | 15,366 | | | 18,579 | | |
| Total assets | $ 1,597,980 | | | $ 1,572,070 | | |
| **Liabilities and Shareholders Equity** | | | | | | |
| Interest-bearing liabilities: | | | | | | |
| Deposits: | | | | | | |
| NOW accounts | $ 68,042 | $ 46 | 0.27% | $ 68,669 | $ 15 | 0.08% |
| Money market accounts | 105,289 | 172 | 0.66% | 71,387 | 149 | 0.85% |
| Savings accounts | 343,366 | 270 | 0.32% | 369,750 | 531 | 0.58% |
| Certificate of deposit accounts | 335,236 | 971 | 1.17% | 385,599 | 1,583 | 1.67% |
| Overnight and short-term borrowings | 39,769 | 10 | 0.10% | 39,161 | 18 | 0.19% |
| Wholesale repurchase agreements | 20,045 | 139 | 2.77% | 18,222 | 139 | 3.06% |

| | | | | | | |
|---|---|---|---|---|---|---|
| FHLB borrowings | 272,971 | 2,296 | 3.37% | 271,742 | 2,665 | 3.92% |
| Subordinated deferrable interest debentures | 13,403 | 165 | 4.94% | 13,403 | 164 | 4.90% |
| Total interest-bearing liabilities | 1,198,121 | 4,069 | 1.38% | 1,237,933 | 5,264 | 1.72% |
| Noninterest-bearing deposits | 254,722 | | | 199,735 | | |
| Other liabilities | 16,076 | | | 11,427 | | |
| Total liabilities | 1,468,919 | | | 1,449,095 | | |
| Shareholders equity: | 129,061 | | | 122,975 | | |
| Total liabilities and shareholders equity | $ 1,597,980 | | | $ 1,572,070 | | |
| Net interest income | | $ 13,515 | | | $ 13,088 | |
| Net interest rate spread | | | 3.27% | | | 3.22% |
| Net interest rate margin | | | 3.58% | | | 3.52% |

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*Rate/Volume Analysis* The following table sets forth certain information regarding changes in the Company s interest income and interest expense for the periods indicated. For each category of interest-earning assets and interest-bearing liabilities, information is provided on changes attributable to (i) changes in rate (changes in rate multiplied by comparative period average balance) and (ii) changes in volume (changes in average balances multiplied by comparative period rate). The net change attributable to the combined impact of rate and volume was allocated proportionally to the individual rate and volume changes.

| | Three Months Ended March 31, 2011 vs. 2010 Increase/(Decrease) Due to | | |
|---|---|---|---|
| ***(In thousands)*** | **Rate** | **Volume** | **Total** |
| Interest income: | | | |
| Overnight Investments | $ (3) | $ (2) | $ (5) |
| Available for sale securities | (563) | (194) | (757) |
| Stock in the FHLB | 12 | | 12 |
| Commercial loans and leases | (297) | 642 | 345 |
| Residential mortgage loans | (253) | (77) | (330) |
| Consumer and other loans | (142) | 109 | (33) |
| Total interest income | (1,246) | 478 | (768) |
| Interest expense: | | | |
| NOW accounts | 31 | | 31 |
| Money market accounts | (37) | 60 | 23 |
| Savings accounts | (226) | (35) | (261) |
| Certificate of deposit accounts | (412) | (200) | (612) |
| Overnight and short-term borrowings | (8) | | (8) |
| Wholesales repurchase agreements | (13) | 13 | |
| FHLB borrowings | (381) | 12 | (369) |
| Subordinated deferrable interest debentures | 1 | | 1 |
| Total interest expense | (1,045) | (150) | (1,195) |
| Net interest income | $ (201) | $ 628 | $ 427 |

*Interest Income Investments* Total investment income (consisting of interest on overnight investments and available for sale securities) was $3.0 million for the quarter ended March 31, 2011, compared to $3.8 million for the 2010 period. The decrease in total investment income was $750,000, or 19.8%.

With respect to duration and repricing of the Company s available for sale investment portfolio, the majority of the Company s investments are comprised of government-sponsored enterprise ( GSE ) obligations and private-labeled and GSE mortgage-backed securities with repricing periods or expected durations of less than five years.

*Interest Income Loans and Leases* Interest from loans and leases was $14.6 million for the quarter ended March 31, 2011 and represented a yield on total loans and leases of 5.10%. This compares to $14.6 million of interest and a yield of 5.32% for the first quarter of 2010. Interest income on loans and leases decreased $18,000, or 0.1%, with the decrease in yield on loans and leases of 22 bps offset by the increase in the average balance of loans and leases of $44.7 million, or 4.0%.

The average balance of the various components of the loan and lease portfolio changed from the first quarter of 2010 as follows: commercial loans and leases increased $46.8 million, or 6.4%; consumer and other loans increased $6.7 million, or 3.3%; and residential mortgage loans decreased $8.8 million, or 5.1%. Changes in the average yields from the first quarter of 2010 were as follows: commercial loans and leases decreased 17 bps to 5.54%; consumer and other loans decreased 20 bps to 4.23%; and residential mortgage loans decreased 56 bps to 4.15%.

*Interest Expense Deposits and Borrowings* Interest paid on deposits and borrowings decreased $1.2 million, or 22.7%, to $4.1 million for the three months ended March 31, 2011, down from $5.3 million for the same period during 2010. The overall average cost for interest-bearing liabilities decreased 34 bps to 1.38% for the first quarter of 2011, compared to 1.72% for the first quarter of 2010. The average balance of total interest-bearing liabilities decreased $39.8 million, or 3.2%, to $1.20 billion for the three months ended March 31, 2011 compared to the same period in 2010.

The decline in deposit average balances was attributable to CDs, down $50.4 million, or 13.1%, savings accounts, down $26.4 million, or 7.1%, and NOW accounts down $627,000, or 0.9%. The decrease was offset by an increase in money market accounts of $33.9 million, or 47.5% (primarily due to new retail products available and the Bank s strategy to allow short-term CDs with higher costs to decline).

Average borrowings increased as compared to the first quarter of 2010, with an increase in wholesale repurchase agreements of $1.8 million, or 10.0%, an increase in FHLB funding of $1.2 million, or 0.5%, and an increase in short-term borrowings of $608,000, or 1.6%.

Market competition from bank and non-bank financial institutions continues to be strong in the Company s market area. However, disciplined deposit pricing and maturation and/or repricing of higher yielding CDs to lower rates and reduced FHLB borrowing levels have decreased the cost of interest-bearing liabilities in the first quarter of 2011 compared to the same period in 2010.

Overall, the Company s liability costs continue to be dependent upon a number of factors including general economic conditions, national and local interest rates, competition in the local deposit marketplace, interest rate tiers offered and the Company s cash flow needs.

Provision for Loan and Lease Losses

The provision for loan and lease losses was $1.1 million for the quarter ended March 31, 2011, compared to $1.6 million for the first quarter of 2010. This represents a decrease of $475,000, or 29.7%.

Management evaluates several factors including new loan originations, actual and estimated charge-offs, risk characteristics of the loan and lease portfolio and general economic conditions when determining the provision for loan and lease losses. Growth in the loan and lease portfolio necessitates increases in the provision for loan and lease losses. As the loans and leases mature, or if economic conditions were to worsen or if the marketplace experiences prolonged economic stress, management believes it likely that the level of nonperforming assets would increase, which may in turn lead to increases to the provision for loan and lease losses. Also see discussion under *Allowance for Loan and Lease Losses.*

Noninterest Income

Total noninterest income increased $17,000, or 0.7%, to $2.3 million for the first quarter of 2011, compared to the same period of 2010. During the first quarter of 2011, there were no credit losses on other-than-temporarily impaired securities, while $571,000 were recognized during the first quarter of 2010. Gains on the sale of available for sale securities decreased by $263,000, or 55.4%, during the first quarter of 2011. Additionally, service charges on deposit accounts decreased $124,000, or 9.8%, other miscellaneous income decreased $103,000, or 27.8%, and commissions on nondeposit investment products decreased $43,000, or 18.1%.

Noninterest Expense

Noninterest expense for the first quarter of 2011 increased $781,000, or 7.4%, to $11.3 million from $10.5 million in 2010.

The Company recorded $745,000 of expenses in connection with an adverse legal judgment that was determined in March 2011. See *Note 9 Contingent Liabilities* of the Company s consolidated financial statements for further details. Marketing costs increased $95,000, or 36.8%, and salaries and employee benefits costs increased $91,000, or 1.6%, compared to the first quarter of 2010. Decreases in loan workout and other real estate owned expenses of $130,000, or 38.7%, offset the increases in noninterest expenses.

Overall, the Company s efficiency ratio of 71.11% for the first three months of the year increased from the efficiency ratio of 68.09% for the same period in the prior year.

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*Income Tax Expense*

Income tax expense increased by $50,000, or 4.6%, to $1.1 million for the three months ended March 31, 2011 from the same period in 2010. This represented total effective tax rates of 33.2% and 33.1%, respectively. Tax-favored income from bank-owned life insurance, along with the Company s utilization of a Rhode Island passive investment company, has reduced the effective tax rate from the 40.9% combined statutory federal and state tax rate.

As discussed in *Note 9 Contingent Liabilities* of the Company s consolidated financial statements, the Massachusetts Department of Revenue has challenged a tax position of the Bank. While management believes it more likely than not that the Bank will prevail in its tax position, the Company s tax expense would increase if it does not.

**Liquidity and Capital Resources**

*Liquidity*

Liquidity is defined as the ability to meet current and future financial obligations of a short-term nature. The Company further defines liquidity as the ability to respond to the needs of depositors and borrowers, as well as to earnings enhancement opportunities, in a changing marketplace.

The primary source of funds for the payment of dividends and expenses by the Company is dividends paid to it by the Bank. Bank regulatory authorities generally restrict the amounts available for payment of dividends if the effect thereof would cause the capital of the Bank to be reduced below applicable capital requirements. These restrictions indirectly affect the Company s ability to pay dividends. The primary sources of liquidity for the Bank consist of deposit inflows, loan repayments, borrowed funds and maturing investment securities and sales of securities from the available for sale portfolio. While management believes that these sources are sufficient to fund the Bank s lending and investment activities, the availability of these funding sources are subject to broad economic conditions and could be restricted in the future. Such restrictions would impact the Company s immediate liquidity and/or additional liquidity.

Management is responsible for establishing and monitoring liquidity targets as well as strategies and tactics to meet these targets. In general, the Company seeks to maintain a high degree of flexibility with a liquidity target of 10% to 30% of total assets. At March 31, 2011, overnight investments and available for sale securities amounted to $362.1 million, or 22.5% of total assets. This compares to $360.4 million, or 22.5% of total assets at December 31, 2010. The Bank is a member of the FHLB and, as such, has access to both short- and long-term borrowings. The Bank also has access to funding through wholesale repurchase agreements and brokered deposits, and may utilize additional sources of funding in the future, including borrowings at the Federal Reserve discount window, to supplement its liquidity. Management believes that the Company has adequate liquidity to meet its commitments.

*Capital Resources*

Total shareholders equity of the Company was $130.2 million at March 31, 2011 compared to $128.7 million at December 31, 2010. Net income of $2.3 million, and net stock option activity (stock option exercises, share repurchases and share-based compensation) of $320,000 were offset by decreased net unrealized holding gains on available for sale securities of $223,000, and common stock dividends of $890,000.

All FDIC-insured institutions must meet specified minimal capital requirements. These regulations require banks to maintain a minimum leverage capital ratio. In addition, the FDIC has adopted capital guidelines based upon ratios of a bank s capital to total assets adjusted for risk. The risk-based capital guidelines include both a definition of capital and a framework for calculating risk-weighted assets by assigning balance sheet assets and off-balance sheet items to broad risk categories. These regulations require banks to maintain minimum capital levels for capital adequacy purposes and higher capital levels to be considered well-capitalized.

The Federal Reserve Board ( FRB ) has also issued capital guidelines for bank holding companies. These guidelines require the Company to maintain minimum capital levels for capital adequacy purposes. In general, the FRB has adopted substantially identical capital adequacy guidelines as the FDIC. Such standards are applicable to bank holding companies and their bank subsidiaries on a consolidated basis.

As of March 31, 2011, the Company and the Bank met all applicable minimum capital requirements and were considered well-capitalized by both the FRB and the FDIC.

The Company s and the Bank s actual and required capital amounts and ratios are as follows:

| | Actual | | Minimum Required For Capital Adequacy Purposes | | Minimum Required To Be Considered Well-Capitalized | |
|---|---|---|---|---|---|---|
| | **Amount** | **Ratio** | **Amount** | **Ratio** | **Amount** | **Ratio** |
| | | | *(Dollars in thousands)* | | | |
| **At March 31, 2011:** | | | | | | |
| Bancorp Rhode Island, Inc. | | | | | | |
| Tier I capital (to average assets) | $ 129,448 | 8.14% | $ 63,592 | 4.00% | $ 79,490 | 5.00% |
| Tier I capital (to risk weighted assets) | 129,448 | 11.46% | 45,197 | 4.00% | 67,795 | 6.00% |
| Total capital (to risk weighted assets) | 143,620 | 12.71% | 90,394 | 8.00% | 112,992 | 10.00% |
| Bank Rhode Island | | | | | | |
| Tier I capital (to average assets) | $ 127,659 | 8.03% | $ 63,578 | 4.00% | $ 79,472 | 5.00% |
| Tier I capital (to risk weighted assets) | 127,659 | 11.30% | 45,173 | 4.00% | 67,759 | 6.00% |
| Total capital (to risk weighted assets) | 141,831 | 12.56% | 90,345 | 8.00% | 112,932 | 10.00% |
| **At December 31, 2010:** | | | | | | |
| Bancorp Rhode Island, Inc. | | | | | | |
| Tier I capital (to average assets) | $ 127,711 | 8.10% | $ 63,035 | 4.00% | $ 78,794 | 5.00% |
| Tier I capital (to risk weighted assets) | 127,711 | 11.27% | 45,316 | 4.00% | 67,975 | 6.00% |
| Total capital (to risk weighted assets) | 141,925 | 12.53% | 90,633 | 8.00% | 113,291 | 10.00% |
| Bank Rhode Island | | | | | | |
| Tier I capital (to average assets) | $ 126,031 | 8.00% | $ 63,047 | 4.00% | $ 78,809 | 5.00% |
| Tier I capital (to risk weighted assets) | 126,031 | 11.13% | 45,292 | 4.00% | 67,938 | 6.00% |
| Total capital (to risk weighted assets) | 140,245 | 12.39% | 90,584 | 8.00% | 113,231 | 10.00% |

**Recent Accounting Pronouncements**

See *Note 4 Recently Issued Accounting Pronouncements* of the consolidated financial statements for details of recently issued accounting pronouncements and their expected impact on the Company s consolidated financial statements.

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***ITEM 3. Quantitative and Qualitative Disclosures About Market Risk***

Interest Rate Risk

The principal market risk facing the Company is interest rate risk. The Company s objective regarding interest rate risk is to manage its assets and funding sources to produce results which are consistent with its liquidity, capital adequacy, growth and profitability goals, while maintaining interest rate risk exposure within established parameters over a range of possible interest rate scenarios.

Interest rate risk management is governed by the Bank s Asset/Liability Committee ( ALCO ). The ALCO establishes exposure limits that define the Company s tolerance for interest rate risk. The ALCO monitors current exposures versus limits and reports results to the Board of Directors. The policy limits and guidelines serve as benchmarks for measuring interest rate risk and for providing a framework for evaluation and interest rate risk management decision making. The primary tools for managing interest rate risk currently are the securities portfolio, purchased mortgages, wholesale repurchase agreements and borrowings from the FHLB.

The Company s interest rate risk position is measured using both income simulation and interest rate sensitivity gap analysis. Income simulation is the primary tool for measuring the interest rate risk inherent in the Company s balance sheet at a given point in time by showing the effect on net interest income, over a 12-month period, of interest rate shocks of 300 bps. These simulations take into account repricing, maturity and prepayment characteristics of individual products. The ALCO reviews simulation results to determine whether the exposure resulting from changes in market interest rates remains within established tolerance levels over a 12-month horizon, and develops appropriate strategies to manage this exposure. The Company s guidelines for interest rate risk specify that if interest rates were to shift immediately up or down 300 bps over a 12-month time period, estimated net interest income should decline by no more than 15.0%. Due to the low interest rate environment at March 31, 2011, interest rate shocks down were not performed. As of March 31, 2011, net interest income simulation indicated that the Company s exposure to changing interest rates was within this tolerance. The ALCO reviews the methodology utilized for calculating interest rate risk exposure and may periodically adopt modifications to this methodology.

The following table presents the estimated impact of interest rate shocks on the Company s estimated net interest income over a 12- month period beginning April 1, 2011:

| | Estimated Exposure to Net Interest Income | |
|---|---|---|
| | **Dollar Change** | **Percent Change** |
| | *(Dollars in thousands)* | |
| **Initial Twelve Month Period:** | | |
| Up 300 bps | $ (3,066) | -5.53% |

The Company also uses interest rate sensitivity gap analysis to provide a more general overview of its interest rate risk profile. The interest rate sensitivity gap is defined as the difference between interest-earning assets and interest-bearing liabilities maturing or repricing within a given time period. At March 31, 2011, the Company s one year cumulative gap was a positive $67.7 million, or 4.2% of total assets.

For additional discussion on interest rate risk see the section titled *Asset and Liability Management* on pages 53 through 54 of the Company s 2010 Annual Report on Form 10-K.

### *ITEM 4. Controls and Procedures*

As required by Rule 13a-15 under the Securities Exchange Act of 1934, as amended (the Exchange Act ), the Company carried out an evaluation of the effectiveness of the design and operation of the Company s disclosure controls and procedures as of the end of the period covered by this report. This evaluation was carried out under the supervision and with the participation of the Company s management, including the Company s Chief Executive Officer and the Company s Chief Financial Officer. Based upon that evaluation, the Chief Executive Officer and the Chief Financial Officer concluded that the Company s disclosure controls and procedures are effective to ensure that information required to be disclosed by the Company in reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms.

There was no significant change in the Company s internal control over financial reporting that occurred during the Company s most recent fiscal quarter that has materially affected, or is reasonably likely to affect, the Company s internal control over financial reporting. The Company continues to enhance its internal controls over financial reporting, primarily by evaluating and enhancing process and control documentation. Management discusses with and discloses these matters to the Audit Committee of the Board of Directors and the Company s auditors.

## PART II. Other Information

*Item 1. Legal Proceedings*

There are no material pending legal proceedings to which the Company or its subsidiaries are a party, or to which any of their property is subject, other than ordinary routine litigation incidental to the business of banking.

*Item 1A. Risk Factors*

In addition to the risk factors described in the Company s Annual Report on Form 10-K for the year ended December 31, 2010, management believes the following risks and uncertainties could materially affect the Company.

*The Merger Agreement May Be Terminated in Accordance with Its Terms and the Merger May Not Be Completed.*

The merger agreement with Brookline Bancorp is subject to a number of conditions which must be fulfilled in order to complete the merger. Those conditions include: approval of the merger agreement by the Company s shareholders, regulatory approvals, absence of court orders prohibiting the completion of the merger, effectiveness of the registration statement to be filed by Brookline Bancorp in connection with the merger, the continued accuracy of the representations and warranties by both parties and the performance by both parties of their covenants and agreements, and the receipt by both parties of legal opinions from their respective tax counsels.

In addition, certain circumstances exist whereby the Company may choose to terminate the merger agreement, including if Brookline Bancorp s share price declines to below $8.278 (subject to customary anti-dilution adjustments) as of the latest of the date when all regulatory approvals for the merger have been received and shareholder approval of the merger has been obtained, combined with such decline being at least 20% greater than a corresponding decline in the value of the NASDAQ Bank Index. If this situation occurs, the agreement allows Brookline Bancorp the ability to make an adjustment to the exchange ratio, pursuant to a specified formula, to cure any shortfall caused by the decline in share price as previously described. There can be no assurance that the conditions to closing of the merger will be fulfilled or that the merger will be completed.

*Termination of the Merger Agreement Could Negatively Impact the Company.*

If the merger agreement is terminated, there may be various consequences, including:

- the Company s business may have been adversely impacted by the failure to pursue other beneficial opportunities due to the focus of management on the merger, without realizing any of the anticipated benefits of completing the merger; and
- the market price of the Company s common stock might decline to the extent that the current market price reflects a market assumption that the merger will be completed.

If the merger agreement is terminated and the Company s board of directors seeks another merger or business combination, the Company s shareholders cannot be certain that the Company will be able to find a party willing to offer equivalent or more attractive consideration than the consideration Brookline Bancorp has agreed to provide in the merger.

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*The Company Will Be Subject to Business Uncertainties and Contractual Restrictions While the Merger is Pending.*
Uncertainty about the effect of the merger on employees and customers may have an adverse effect on the Company and consequently on Brookline Bancorp. These uncertainties may impair the Company s ability to attract, retain and motivate key personnel until the merger is completed, and could cause customers and others that deal with the Company to seek to change existing business relationships with the Company. Retention of certain employees may be challenging during the pendency of the merger, as certain employees may experience uncertainty about their future roles. If key employees depart because of issues relating to the uncertainty and difficulty of integration or a desire not to remain with the business, Brookline Bancorp s business following the merger could be negatively impacted. In addition, the merger agreement restricts the Company from taking specified actions until the merger occurs without the consent of Brookline Bancorp. These restrictions may prevent the Company from pursuing business opportunities that may arise prior to the completion of the merger.

*The Merger Agreement Limits the Company s Ability to Pursue Alternatives to the Merger.*
The merger agreement contains no-shop provisions that, subject to limited exceptions, limit the Company s ability to initiate, solicit, induce or knowingly encourage, or take any action to facilitate any inquiries or competing third-party proposals, or participate in any discussions or negotiations or provide any confidential information relating to a proposal to acquire all or a significant part of the Company. In addition, the Company has agreed to pay Brookline Bancorp a termination fee in the amount of $8.9 million in the event that Brookline Bancorp terminates the merger agreement for certain reasons. These provisions might discourage a potential competing acquirer that might have an interest in acquiring all or a significant part of the Company from considering or proposing that acquisition even if it were prepared to pay consideration with a higher per share market price than that proposed in the merger, or might result in a potential competing acquirer s proposing to pay a lower per share price to acquire the Company than it might otherwise have proposed to pay. Until the merger agreement is adopted by the Company s shareholders, the Company can consider and participate in discussions and negotiations with respect to an alternative unsolicited bona fide acquisition proposal (subject to its obligation to pay a termination fee under certain circumstances) so long as the Company s board of directors determines in good faith (after consultation with its outside legal counsel) that failure to do so would result in a violation of its fiduciary duties to the Company s shareholders under Rhode Island law and (after consultation with outside legal counsel and a nationally recognized, independent financial advisor) that such alternative acquisition proposal constitutes a superior proposal or would reasonably be likely to result in a superior proposal. The Company shall also keep Brookline Bancorp appraised of developments, discussions and negotiations relating to any such acquisition proposal.

*Following Completion of the Merger, Brookline Bancorp Will Face Risks Different from Those Faced by Brookline Bancorp Today, which May Affect the Market Price of the Shares of Brookline Bancorp Common Stock.*
Upon completion of the merger, the Company s separate legal existence will cease, its wholly-owned subsidiary, Bank Rhode Island, will become a direct wholly owned subsidiary of Brookline Bancorp, and certain holders of the Company s common stock will become holders of Brookline Bancorp common stock. Some of Brookline Bancorp s current businesses and markets differ from those of the Company and, accordingly, the results of operations of Brookline Bancorp after the merger may be affected by factors different from those currently affecting the results of operations of the Company.

*Item 2. Unregistered Sales of Equity Securities and Use of Proceeds*

The table below summarizes the Company s repurchases of common stock during the quarter ended March 31, 2011:

| Period | Total Number of Shares Purchased (a) | Average Price Paid per Share | Total Number of Shares Purchased as Part of Announced Plan | Maximum Number of Shares That May yet Be Purchased Under the Plan |
|---|---|---|---|---|
| 1/1/11 through 1/31/11 | | | | |
| 2/1/11 through 2/28/11 | 12,100 | $ 30.56 | | |
| 3/1/11 through 3/31/11 | | | | |

(a) In February 2011, the Company s Chief Executive Officer delivered 12,100 shares of the Company s common stock to satisfy the exercise price for 25,200 stock options exercised. The shares delivered were valued at $30.56 per share. The Chief Executive Officer paid the balance of the exercise price and all taxes in cash.

*Item 3. Defaults Upon Senior Securities*

No defaults upon senior securities have taken place.

*Item 5. Other Information*

No information to report.

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*Item 6. Exhibits*

| | |
|---|---|
| 10.6(c) | Amendment No. 3 to Amended and Restated Supplemental Executive Retirement Plan |
| 31.1 | Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 |
| 31.2 | Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 |
| 32.1 | Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 |
| 32.2 | Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 |

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**BANCORP RHODE ISLAND, INC.**

SIGNATURES

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

| | **Bancorp Rhode Island, Inc.** |
|---|---|
| May 4, 2011 | /s/ Merrill W. Sherman |
| (Date) | Merrill W. Sherman<br>President and<br>Chief Executive Officer |
| May 4, 2011 | /s/ Linda H. Simmons |
| (Date) | Linda H. Simmons<br>Chief Financial Officer<br>and Treasurer |