

NORTHEAST COMMUNITY BANCORP INC  
Form 10-Q  
May 15, 2013

**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, DC 20549**

**FORM 10-Q**

(Mark One)

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

For the quarterly period ended March 31, 2013

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number: 0-51852

**Northeast Community Bancorp, Inc.**

(Exact name of registrant as specified in its charter)

|  |                                      |
|--|--------------------------------------|
| <u>United States of America</u>                                | <u>06-1786701</u>                    |
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification No.) |

|  |              |
|--|--------------|
| <u>325 Hamilton Avenue, White Plains, New York</u> | <u>10601</u> |
| (Address of principal executive offices)           | (Zip Code)   |

**(914) 684-2500**

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(Registrant's telephone number, including area code)

**N/A**

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(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  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definition of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one)

Large Accelerated Filer

Accelerated Filer

Non-accelerated Filer

Smaller Reporting Company

(Do not check if a smaller reporting company)

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

As of May 10, 2013, there were 12,644,752 shares of the registrant's common stock outstanding.

**NORTHEAST COMMUNITY BANCORP, INC.**

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Table of Contents**PART I. FINANCIAL INFORMATION****Item 1. Financial Statements****CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION (UNAUDITED)**

|   | March 31,<br>2013                                     | December<br>31,<br>2012 |
|---|---|-------------------------|
|   | (In thousands,<br>except share and per<br>share data) |                         |
| <b>ASSETS</b>   |   |                         |
| Cash and amounts due from depository institutions   | \$ 2,360  | \$ 2,821                |
| Interest-bearing deposits   | 22,621  | 46,421                  |
| Cash and cash equivalents   | 24,981  | 49,242                  |
| Certificates of deposit   | 150   | 399                     |
| Securities available-for-sale   | 126   | 129                     |
| Securities held-to-maturity (fair value of \$11,588 and \$12,561, respectively)   | 11,069  | 11,987                  |
| Loans receivable, net of allowance for loan losses of \$4,706 and \$4,646, respectively   | 343,939   | 333,787                 |
| Premises and equipment, net   | 12,659  | 12,898                  |
| Federal Home Loan Bank of New York stock, at cost   | 905   | 1,355                   |
| Bank owned life insurance   | 20,009  | 19,852                  |
| Accrued interest receivable   | 1,029   | 976                     |
| Goodwill  | 1,083   | 1,083                   |
| Intangible assets   | 391   | 406                     |
| Real estate owned   | 4,271   | 4,271                   |
| Other assets  | 7,946   | 7,839                   |
| Total assets  | \$ 428,558  | \$ 444,224              |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>   |   |                         |
| <b>Liabilities</b>  |   |                         |
| <b>Deposits:</b>  |   |                         |
| Non-interest bearing  | \$ 20,101   | \$ 22,932               |
| Interest bearing  | 291,609   | 295,188                 |
| Total deposits  | 311,710   | 318,120                 |
| Advance payments by borrowers for taxes and insurance   | 4,108   | 3,516                   |
| Federal Home Loan Bank of NY advances   | 5,000   | 15,000                  |
| Accounts payable and accrued expenses   | 3,750   | 3,739                   |
| Total liabilities   | 324,568   | 340,375                 |
| <b>Stockholders' equity:</b>  |   |                         |
| Preferred stock, \$0.01 par value; 1,000,000 shares authorized, none issued   | —   | —                       |
| Common stock, \$0.01 par value; 19,000,000 shares authorized; 13,225,000 shares issued;<br>outstanding: 12,644,752 shares at March 31, 2013 and December 31, 2012 | 132   | 132                     |

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|  |            |            |
|--|------------|------------|
| Additional paid-in capital                             | 57,148     | 57,178     |
| Unearned Employee Stock Ownership Plan (“ESOP”) shares | (3,305 )   | (3,370 )   |
| Retained earnings                                      | 53,949     | 53,893     |
| Treasury stock – at cost, 580,248 shares               | (3,712 )   | (3,712 )   |
| Accumulated comprehensive loss                         | (222 )     | (272 )     |
| Total stockholders’ equity                             | 103,990    | 103,849    |
| Total liabilities and stockholders’ equity             | \$ 428,558 | \$ 444,224 |

See Notes to Consolidated Financial Statements

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Table of Contents**CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)**

|   | Three Months Ended<br>March 31,          |          |
|---|--|----------|
|   | 2013                                     | 2012     |
|   | (In thousands,<br>except per share data) |          |
| Interest Income:                                    |  |          |
| Loans   | \$ 4,646                                 | \$ 4,893 |
| Interest-earning deposits                           | 3  | 12       |
| Securities – taxable                                | 99                                       | 138      |
| Total Interest Income                               | 4,748                                    | 5,043    |
| Interest Expense:                                   |  |          |
| Deposits  | 728                                      | 1,032    |
| Borrowings  | 101                                      | 143      |
| Total Interest Expense                              | 829                                      | 1,175    |
| Net Interest Income                                 | 3,919                                    | 3,868    |
| Provision for Loan Losses                           | 60                                       | —        |
| Net Interest Income after Provision for Loan Losses | 3,859                                    | 3,868    |
| Non-Interest Income:                                |  |          |
| Other loan fees and service charges                 | 219                                      | 189      |
| Loss on disposition of equipment                    | —  | (12 )    |
| Earnings on bank owned life insurance               | 157                                      | 142      |
| Investment advisory fees                            | 177                                      | 206      |
| Other   | 5  | 3        |
| Total Non-Interest Income                           | 558                                      | 528      |
| Non-Interest Expenses:                              |  |          |
| Salaries and employee benefits                      | 2,346                                    | 2,151    |
| Occupancy expense                                   | 394                                      | 289      |
| Equipment   | 181                                      | 146      |
| Outside data processing                             | 276                                      | 235      |
| Advertising   | 10                                       | 57       |
| Real estate owned expense                           | 86                                       | 5        |
| FDIC insurance premiums                             | 30                                       | 93       |
| Other   | 868                                      | 1,102    |

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|   |         |         |
|---|---------|---------|
| Total Non-Interest Expenses                                     | 4,191   | 4,078   |
| Income before Provision for Income Taxes                        | 226     | 318     |
| Provision for Income Taxes                                      | 19      | 66      |
| Net Income  | \$ 207  | \$ 252  |
| Net Income per Common Share – Basic                             | \$ 0.02 | \$ 0.02 |
| Weighted Average Number of Common Shares<br>Outstanding – Basic | 12,311  | 12,285  |
| Dividends Declared per Common Share                             | \$ 0.03 | \$ 0.03 |

See Notes to Consolidated Financial Statements

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Table of Contents**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (UNAUDITED)**

|   | Three Months Ended |        |
|---|--------------------|--------|
|   | March 31,          |        |
|   | 2013               | 2012   |
|   | (In thousands)     |        |
| Net income                              | \$ 207             | \$ 252 |
| Other comprehensive income (loss):      |                    |        |
| Reclassification adjustments:           |                    |        |
| Amortization of prior service cost (1)  | 5                  | 5      |
| Amortization of actuarial loss (1)      | 9                  | —      |
| Gains (losses) arising during period    | 69                 | (58 )  |
| Total                                   | 83                 | (53 )  |
| Income tax effect                       | (33 )              | 16     |
| Total other comprehensive income (loss) | 50                 | (37 )  |
| <br>                                    |                    |        |
| Total comprehensive income              | \$ 257             | \$ 215 |

(1) Amounts are included in salaries and employees benefits in the unaudited consolidated statement of operations as part of net periodic pension cost. See note 4 for further information.

See Notes to Consolidated Financial Statements



Table of Contents**CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY (UNAUDITED)****Three Months Ended March 31, 2013 and 2012 (in thousands)**

|  | Common<br>Stock | Additional<br>Paid-in<br>Capital | Unearned<br>ESOP<br>Shares | Retained<br>Earnings | Treasury<br>Stock | Accumulated<br>Other<br>Comprehensive<br>Loss | Total<br>Equity |
|--|-----------------|----------------------------------|----------------------------|----------------------|-------------------|---|-----------------|
| Balance at December 31, 2011             | \$ 132          | \$ 57,292                        | \$ (3,629 )                | \$ 57,076            | \$ (3,712 )       | \$ (94 )                                      | \$ 107,065      |
| Net income                               | —               | —                                | —                          | 252                  | —                 | —   | 252             |
| Other comprehensive loss                 | —               | —                                | —                          | —                    | —                 | (37 )   | (37 )           |
| Cash dividend declared (\$.03 per share) | —               | —                                | —                          | (150 )               | —                 | —   | (150 )          |
| ESOP shares earned                       | —               | (25 )                            | 65                         | —                    | —                 | —   | 40              |
| Balance - March 31, 2012                 | \$ 132          | \$ 57,267                        | \$ (3,564 )                | \$ 57,178            | \$ (3,712 )       | \$ (131 )                                     | \$ 107,170      |
| Balance at December 31, 2012             | \$ 132          | \$ 57,178                        | \$ (3,370 )                | \$ 53,893            | \$ (3,712 )       | \$ (272 )                                     | \$ 103,849      |
| Net income                               | —               | —                                | —                          | 207                  | —                 | —   | 207             |
| Other comprehensive income               | —               | —                                | —                          | —                    | —                 | 50  | 50              |
| Cash dividend declared (\$.03 per share) | —               | —                                | —                          | (151 )               | —                 | —   | (151 )          |
| ESOP shares earned                       | —               | (30 )                            | 65                         | —                    | —                 | —   | 35              |
| Balance - March 31, 2013                 | \$ 132          | \$ 57,148                        | \$ (3,305 )                | \$ 53,949            | \$ (3,712 )       | \$ (222 )                                     | \$ 103,990      |

See Notes to Consolidated Financial Statements

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## CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

|   | Three Months Ended<br>March 31, |           |
|---|---------------------------------|-----------|
|   | 2013                            | 2012      |
|   | (In thousands)                  |           |
| Cash Flows from Operating Activities:   |                                 |           |
| Net income  | \$ 207                          | \$ 252    |
| Adjustments to reconcile net income to net cash provided by (used in) operating activities: |                                 |           |
| Net amortization of securities premiums and discounts, net                                  | 17                              | 21        |
| Provision for loan losses   | 60                              | —         |
| Depreciation  | 201                             | 163       |
| Net amortization of deferred loan fees and costs  | 46                              | 47        |
| Amortization of intangible assets   | 15                              | 15        |
| Deferred income taxes   | 5                               | (27 )     |
| Retirement plan expense   | 74                              | 68        |
| Gain (loss) on disposal of equipment  | —                               | 12        |
| Earnings on bank owned life insurance   | (157 )                          | (142 )    |
| ESOP compensation expense   | 35                              | 40        |
| Increase in accrued interest receivable   | (53 )                           | (101 )    |
| Increase in other assets  | (100 )                          | (249 )    |
| Increase (decrease) in accounts payable and accrued expenses                                | 20                              | (2,018 )  |
| Net Cash Provided by (Used in) Operating Activities   | 370                             | (1,919 )  |
| Cash Flows from Investing Activities:   |                                 |           |
| Net increase in loans   | (10,258 )                       | (2,302 )  |
| Principal repayments on securities available-for-sale                                       | 3                               | 5         |
| Principal repayments on securities held-to-maturity   | 901                             | 1,034     |
| Redemption of Federal Home Loan Bank of New York stock                                      | 450                             | 225       |
| Proceeds from maturities of certificates of deposit   | 249                             | 747       |
| Purchases of premises and equipment   | (7 )                            | (255 )    |
| Net Cash Used in Investing Activities   | (8,662 )                        | (546 )    |
| Cash Flows from Financing Activities:   |                                 |           |
| Net increase (decrease) in deposits   | (6,410 )                        | 22,758    |
| Repayment of FHLB of NY advances  | (10,000 )                       | (5,000 )  |
| Increase in advance payments by borrowers for taxes and insurance                           | 592                             | 1,274     |
| Cash dividends paid to minority shareholders  | (151 )                          | (150 )    |
| Net Cash Provided by (Used in) Financing Activities   | (15,969 )                       | 18,882    |
| Net Increase (Decrease) in Cash and Cash Equivalents  | (24,261 )                       | 16,417    |
| Cash and Cash Equivalents - Beginning   | 49,242                          | 82,583    |
| Cash and Cash Equivalents - Ending  | \$ 24,981                       | \$ 99,000 |

## SUPPLEMENTARY CASH FLOWS INFORMATION

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|                   |       |         |
|-------------------|-------|---------|
| Income taxes paid | \$—   | \$2,375 |
| Interest paid     | \$829 | \$1,175 |

See Notes to Consolidated Financial Statements

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**NORTHEAST COMMUNITY BANCORP, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 – BASIS OF PRESENTATION**

Northeast Community Bancorp, Inc. (the “Company”) is a federally-chartered corporation organized as a mid-tier holding company for Northeast Community Bank (the “Bank”), in conjunction with the Bank’s reorganization from a mutual savings bank to the mutual holding company structure on July 5, 2006. The Bank is a New York State-chartered savings bank and completed its conversion from a federally-chartered savings bank effective as of the close of business on June 29, 2012. The accompanying unaudited consolidated financial statements include the accounts of the Company, the Bank and the Bank’s wholly owned subsidiaries, New England Commercial Properties, LLC (“NECP”) and NECB Financial Services Group, LLC. NECB Financial Services Group was formed by the Bank in the second quarter of 2012 as a complement to the Bank’s existing investment advisory and financial planning services division, Hayden Wealth Management. As of the filing of this Form 10-Q, NECB Financial Services Group has not conducted any business. All significant intercompany accounts and transactions have been eliminated in consolidation.

The accompanying unaudited consolidated financial statements were prepared in accordance with generally accepted accounting principles for interim financial information as well as instructions for Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information or footnotes necessary for the presentation of financial position, results of operations, changes in stockholders’ equity and cash flows in conformity with accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, all adjustments (consisting only of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three-month period ended March 31, 2013 are not necessarily indicative of the results that may be expected for the full year or any other interim period. The December 31, 2012 consolidated statement of financial condition data was derived from audited consolidated financial statements, but does not include all disclosures required by U.S. generally accepted accounting principles. That data, along with the interim financial information presented in the consolidated statements of financial condition, income, stockholders’ equity, and cash flows should be read in conjunction with the consolidated financial statements and notes thereto, included in the Company’s annual report on Form 10-K for the year ended December 31, 2012.

The preparation of consolidated financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain recorded amounts and disclosures. Accordingly, actual results could differ from those estimates. The most significant estimate pertains to the allowance for loan losses. In preparing these consolidated financial statements, the Company evaluated the events that occurred after March 31, 2013 and through the date these consolidated financial statements were issued.

Loans

Loans are stated at unpaid principal balances plus net deferred loan origination fees and costs less an allowance for loan losses. Interest on loans receivable is recorded on the accrual basis. An allowance for uncollected interest is established on loans where management has determined that the borrowers may be unable to meet contractual principal and/or interest obligations or where interest or principal is 90 days or more past due, unless the loans are well secured and in the process of collection. When a loan is placed on nonaccrual, an allowance for uncollected interest is established and charged against current income. Thereafter, interest income is not recognized unless the financial condition and payment record of the borrower warrant the recognition of interest income. Interest on loans that have been restructured is accrued according to the renegotiated terms, unless on non-accrual. Net loan origination fees and costs are deferred and amortized into income over the contractual lives of the related loans by use of the level yield method. Past due status of loans is based upon the contractual due date.

### **Allowance for Loan Losses**

The allowance for loan losses represents management's estimate of losses inherent in the loan portfolio as of the statement of financial condition date and is recorded as a reduction to loans. The allowance for loan losses is increased by the provision for loan losses, and decreased by charge-offs, net of recoveries. Loans deemed to be uncollectible are charged against the allowance for loan losses, and subsequent recoveries, if any, are credited to the allowance. All, or part, of the principal balance of loans receivable are charged off to the allowance as soon as it is determined that the repayment of all, or part, of the principal balance is highly unlikely.

The allowance for loan losses is maintained at a level considered adequate to provide for losses that can be reasonably anticipated. Management performs a quarterly evaluation of the adequacy of the allowance. The allowance is based on the Company's past loan loss experience, known and inherent risks in the portfolio, adverse situations that may affect the borrower's ability to repay, the estimated value of any underlying collateral, composition of the loan portfolio, current economic conditions, and other relevant factors.

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**NOTE 1 – BASIS OF PRESENTATION (Continued)**

**Allowance for Loan Losses (Continued)**

This evaluation is inherently subjective as it requires material estimates that may be susceptible to significant revision as more information becomes available.

Risk characteristics associated with the types of loans the Company underwrites are as follows:

**Multi-family, Mixed-use and Non-residential Real Estate Loans.** Loans secured by multi-family, mixed-use, and non-residential real estate generally have larger balances and involve a greater degree of risk than one- to four-family residential mortgage loans. Of primary concern in multi-family, mixed-use and non-residential real estate lending is the current and potential cash flow of the property and the borrower's demonstrated ability to operate that type of property. Payments on loans secured by income properties often depend on successful operation and management of the properties. As a result, repayment of such loans may be subject to a greater extent than residential real estate loans to adverse conditions in the real estate market or the economy. To monitor cash flows on income producing properties, we require borrowers to provide annual financial statements for all multi-family, mixed-use and non-residential real estate loans. In reaching a decision on whether to make a multi-family, mixed-use or non-residential real estate loan, we consider the net operating income of the property, the borrower's expertise, credit history and profitability and the value of the underlying property. In addition, with respect to non-residential real estate properties, we also consider the term of the lease and the quality of the tenants. An appraisal of the real estate used as collateral for the real estate loan is also obtained as part of the underwriting process. We have generally required that the properties securing these real estate loans have debt service coverage ratios (the ratio of earnings after subtracting all operating expenses to debt service payments) of at least 1.25x. In underwriting these loans, we take into account projected increases in interest rates in determining whether a loan meets our debt service coverage ratios at the higher interest rate under the adjustable rate mortgage. Environmental surveys and property inspections are utilized for all loans.

**Commercial and Industrial Loans.** Unlike multi-family, mixed-use, and non-residential mortgage loans, which are generally made on the basis of a borrower's ability to make repayment from the operation and cash flow from the real property whose value tends to be more ascertainable, commercial and industrial loans are of higher risk and tend to be made on the basis of a borrower's ability to make repayment from the cash flow of the borrower's business. As a result, the availability of funds for the repayment of commercial and industrial loans may depend substantially on the success of the business itself. Further, any collateral securing such loans may depreciate over time, may be difficult to appraise and may fluctuate in value.

**Construction Loans.** Construction financing affords us the opportunity to achieve higher interest rates and fees with shorter terms to maturity than does residential mortgage loans. However, construction financing is generally considered to involve a higher degree of risk of loss than long-term financing on improved, occupied real estate due to (1) the increased difficulty at the time the loan is made of estimating the building costs and the selling price of the property to be built; (2) the increased difficulty and costs of monitoring the loan; (3) the higher degree of sensitivity to increases in market rates of interest; and (4) the increased difficulty of working out loan problems. We have sought to minimize this risk by limiting the amount of construction loans outstanding at any time and by spreading the loans among multi-family, mixed-use and non-residential projects. In connection with construction loans that convert to permanent loans with us, we underwrite these loans using the same underwriting standards as our multi-family, mixed-use and non-residential real estate loans. If we do not offer permanent financing to the borrower, we minimize risks by requiring the borrower to obtain permanent financing from another financial institution.

**Consumer Loans.** We offer personal loans, loans secured by passbook savings accounts, certificates of deposit accounts or statement savings accounts, and overdraft protection for checking accounts. We do not believe these loans represent a significant risk of loss to the Company.

The allowance consists of specific and general reserves. The specific component relates to loans that are classified as impaired. For loans that are classified as impaired, a specific allowance is established or a partial charge-off is taken when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan. Beginning in the fourth quarter of 2012, the Company discontinued the use of specific allowances. If an impairment is identified, the Company now charges off the impaired portion immediately. A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment records, and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan-by-loan basis.

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**NOTE 1 – BASIS OF PRESENTATION (Continued)**

**Allowance for Loan Losses (Continued)**

The Company does not evaluate consumer or residential one- to four-family loans for impairment, unless such loans are part of a larger relationship that is impaired, or are classified as a troubled debt restructuring.

The estimated fair values of substantially all of the Company's impaired loans are measured based on the estimated fair value of the loan's collateral or discounted cash flows.

For loans secured by real estate, estimated fair values are determined primarily through in-house or third-party appraisals. When a real estate secured loan becomes impaired, a decision is made regarding whether an updated certified appraisal of the real estate is necessary. This decision is based on various considerations, including the age of the most recent appraisal, the loan-to-value ratio based on the original appraisal and the condition of the property. Appraised values might be discounted to arrive at the estimated selling price of the collateral, which is considered to be the estimated fair value. The discounts also include estimated costs to sell the property.

For loans secured by non-real estate collateral, such as accounts receivable, inventory and equipment, estimated fair values are determined based on the borrower's financial statements, inventory reports, accounts receivable aging or equipment appraisals or invoices. Indications of value from these sources are generally discounted based on the age of the financial information or the quality of the assets.

The general component covers pools of loans by loan class including loans not considered impaired, as well as smaller balance homogeneous loans, such as residential real estate and consumer loans. These pools of loans are evaluated for loss exposure based upon historical loss rates, adjusted for qualitative factors. These qualitative risk factors include:

- 1.Changes in policies and procedures in underwriting standards and collections.
- 2.Changes in economic conditions.
- 3.Changes in nature and volume of lending.
- 4.Experience of origination team.
- 5.Changes in past due loan volume and severity of classified assets.



6. Quality of loan review system.
7. Collateral values in general throughout lending territory.
8. Concentrations of credit.
9. Competition, legal and regulatory issues.

Each factor is assigned a value to reflect improving, stable or declining conditions based on management's best judgment using relevant information available at the time of the evaluation. Adjustments to the factors are supported through documentation of changes in conditions in a narrative accompanying the allowance for loan loss calculation.

The allowance calculation methodology includes further segregation of loan classes into risk rating categories. The borrower's overall financial condition, repayment sources, guarantors and value of collateral, if appropriate, are evaluated annually for commercial loans or when credit deficiencies arise, such as delinquent loan payments, for commercial, residential and consumer loans. Credit quality risk ratings include regulatory classifications of pass, special mention, substandard, doubtful and loss. Loans criticized as special mention have potential weaknesses that deserve management's close attention. If uncorrected, the potential weaknesses may result in deterioration of the repayment prospects. Loans classified substandard have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They include loans that are inadequately protected by the current sound net worth and paying capacity of the obligor or of the collateral pledged, if any.

Loans classified doubtful have all the weaknesses inherent in loans classified substandard with the added characteristic that collection or liquidation in full, on the basis of current conditions and facts, is highly improbable. Loans classified as a loss are considered uncollectible and are charged to the allowance for loan losses. Loans not classified are rated pass.

The allowance calculation for each pool of loans is also based on the loss factors that reflect the Company's historical charge-off experience adjusted for current economic conditions applied to loan groups with similar characteristics or classifications in the current portfolio. To help ensure that risk ratings are accurate and reflect the present and future capacity of borrowers to repay a loan as agreed, the Company has a structured loan rating process which allows for a periodic review of its loan portfolio and the early identification of potential impaired loans. Such system takes into consideration, among other things, delinquency status, size of loans, type of collateral and financial condition of the borrowers. The Company's Chief Executive Officer is ultimately responsible for the timely and accurate risk rating of the loan portfolio.

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**NOTE 1 – BASIS OF PRESENTATION (Continued)**

**Allowance for Loan Losses (Continued)**

Loans whose terms are modified are classified as troubled debt restructurings if the Company grants such borrowers concessions and it is deemed that those borrowers are experiencing financial difficulty. Concessions granted under a troubled debt restructuring generally involve a temporary reduction in interest rate or an extension of a loan's stated maturity date. Adversely classified, non-accrual troubled debt restructurings may be reclassified if principal and interest payments, under the modified terms, are current for six consecutive months after modification.

In addition, banking regulatory agencies, as an integral part of their examination process, periodically review the Company's allowance for loan losses and may require the Company to recognize additions to the allowance based on their judgments about information available to them at the time of their examination, which may not be currently available to management. Based on management's comprehensive analysis of the loan portfolio, management believes the allowance for loan losses is adequate as of March 31, 2013.

**Goodwill**

The Company recognized goodwill in connection with the acquisition of its wealth management division in 2007. In the fourth quarter of 2012, the Company performed its annual impairment test and determined that the fair value of this division was less than its carrying value and accordingly, recorded a \$227,000 impairment.

The 2012 impairment was the result of a reduction in expected cash flow from this division resulting from the departure of two employees, one of which had generated significant other commission income from sales of insurance and annuity products. We expect future commission income to decline 50% from prior levels. This decline resulted in a decrease in the value of this division.

The Company has recently determined that an adjustment to the goodwill impairment previously recorded is necessary. The Company is currently reviewing the analysis and has not yet made a final determination as to the amount of the adjustment. However, the Company does not believe that the adjustment is material. The adjusted goodwill impairment will be reflected in future filings.

**NOTE 2 – EARNINGS PER SHARE**

Basic earnings per common share is calculated by dividing the net income available to common stockholders by the weighted-average number of common shares outstanding during the period. Diluted earnings per common share is computed in a manner similar to basic earnings per common share except that the weighted average number of common shares outstanding is increased to include the incremental common shares (as computed using the treasury stock method) that would have been outstanding if all potentially dilutive common stock equivalents were issued during the period. Common stock equivalents may include restricted stock awards and stock options. Anti-dilutive shares are common stock equivalents with weighted-average exercise prices in excess of the weighted-average market value for the periods presented. The Company has not granted any restricted stock awards or stock options and, during the three-month periods ended March 31, 2013 and 2012, had no potentially dilutive common stock equivalents. Unallocated common shares held by the Employee Stock Ownership Plan (“ESOP”) are not included in the weighted-average number of common shares outstanding for purposes of calculating both basic and diluted earnings per common share until they are committed to be released.

### NOTE 3 – EMPLOYEE STOCK OWNERSHIP PLAN

As of December 31, 2012 and March 31, 2013, the ESOP trust held 518,420 shares of the Company’s common stock, which represents all allocated and unallocated shares held by the plan. As of December 31, 2012, the Company had allocated 155,526 shares to participants, and an additional 25,921 shares had been committed to be released. As of March 31, 2013, the Company had allocated 181,447 shares to participants, and an additional 6,480 shares had been committed to be released. The Company recognized compensation expense of \$35,000 and \$40,000 during the three-month periods ended March 31, 2013 and 2012, respectively, which equals the fair value of the ESOP shares when they became committed to be released.

### NOTE 4 -Outside Director Retirement Plan (“DRP”)

Net periodic pension cost for the Company’s DRP was as follows:

|                                    | Three Months Ended<br>March 31, |       |
|------------------------------------|---------------------------------|-------|
|                                    | 2013                            | 2012  |
|                                    | (In thousands)                  |       |
| Service cost                       | \$ 18                           | \$ 11 |
| Interest cost                      | 11                              | 15    |
| Amortization of prior service cost | 5                               | 5     |
| Amortization of actuarial loss     | 9                               | —     |
| Net periodic pension cost          | \$ 43                           | \$ 31 |

This plan is an unfunded, non-contributory defined benefit pension plan covering all non-employee directors meeting eligibility requirements as specified in the plan document. The amortization of prior service cost and actuarial loss in the three-month periods ended March 31, 2013 and 2012 is also reflected in other comprehensive income during those periods.

Table of Contents**NOTE 5 – INVESTMENTS**

The following table sets forth the amortized cost and fair values of our securities portfolio at the dates indicated (in thousands):

|   | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Fair<br>Value |
|---|-------------------|------------------------------|-------------------------------|---------------|
| March 31, 2013                            |                   |                              |                               |               |
| Securities available for sale:            |                   |                              |                               |               |
| Mortgage-backed securities – residential: |                   |                              |                               |               |
| Federal Home Loan Mortgage Corporation    | \$ 73             | \$ 2                         | \$ —                          | \$75          |
| Federal National Mortgage Association     | 49                | 2                            | —                             | 51            |
| Total                                     | \$ 122            | \$ 4                         | \$ —                          | \$ 126        |
| Securities held to maturity:              |                   |                              |                               |               |
| Mortgage-backed securities – residential: |                   |                              |                               |               |
| Government National Mortgage Association  | \$ 8,428          | \$ 396                       | \$ —                          | \$8,824       |
| Federal Home Loan Mortgage Corporation    | 259               | 10                           | —                             | 269           |
| Federal National Mortgage Association     | 203               | 9                            | —                             | 212           |
| Collateralized mortgage obligations-GSE   | 2,178             | 104                          | —                             | 2,282         |
| Other                                     | 1                 | —                            | —                             | 1             |
| Total                                     | \$ 11,069         | \$ 519                       | \$ —                          | \$11,588      |
| December 31, 2012                         |                   |                              |                               |               |
| Securities available for sale:            |                   |                              |                               |               |
| Mortgage-backed securities – residential: |                   |                              |                               |               |
| Federal Home Loan Mortgage Corporation    | \$ 76             | \$ 2                         | \$ —                          | \$78          |
| Federal National Mortgage Association     | 49                | 2                            | —                             | 51            |
| Total                                     | \$ 125            | \$ 4                         | \$ —                          | \$ 129        |
| Securities held to maturity:              |                   |                              |                               |               |
| Mortgage-backed securities – residential: |                   |                              |                               |               |
| Government National Mortgage Association  | \$ 9,044          | \$ 442                       | \$ —                          | \$9,486       |
| Federal Home Loan Mortgage Corporation    | 267               | 9                            | —                             | 276           |
| Federal National Mortgage Association     | 215               | 8                            | —                             | 223           |
| Collateralized mortgage obligations-GSE   | 2,460             | 115                          | —                             | 2,575         |
| Other                                     | 1                 | —                            | —                             | 1             |
| Total                                     | \$ 11,987         | \$ 574                       | \$ —                          | \$12,561      |

Contractual final maturities of mortgage-backed securities available for sale were as follows:

|                     | March 31, 2013    |            |
|---------------------|-------------------|------------|
|                     | Amortized<br>Cost | Fair Value |
|                     | (In Thousands)    |            |
| Due after ten years | \$ 122            | \$ 126     |
|                     | \$ 122            | \$ 126     |

Table of Contents**NOTE 5 – INVESTMENTS (Continued)**

Contractual final maturities of mortgage-backed securities held to maturity were as follows:

|                                     | March 31, 2013    |            |
|-------------------------------------|-------------------|------------|
|                                     | Amortized<br>Cost | Fair Value |
|                                     | (In Thousands)    |            |
| Due after one but within five years | \$60              | \$ 62      |
| Due after five but within ten years | 157               | 164        |
| Due after ten years                 | 10,852            | 11,362     |
|                                     | \$11,069          | \$ 11,588  |

The maturities shown above are based upon contractual final maturity. Actual maturities will differ from contractual maturities due to scheduled monthly repayments and due to the underlying borrowers having the right to prepay their obligations.

**NOTE 6 – FAIR VALUE DISCLOSURES**

The Company uses fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. The Company's securities available for sale are recorded at fair value on a recurring basis. Additionally, from time to time, we may be required to record at fair value other assets and liabilities on a non-recurring basis, such as securities held to maturity, impaired loans and other real estate owned. U.S. GAAP has established a fair value hierarchy that prioritizes the inputs to valuation methods used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are as follows:

*Level 1:* Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities.

*Level 2:* Quoted prices in markets that are not active, or inputs that are observable either directly or indirectly, for substantially the full term of the asset or liability.

*Level 3:* Prices or valuation techniques that require inputs that are both significant to the fair value measurement and unobservable (i.e., supported with little or no market activity).

An asset's or liability's level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement.



Table of Contents**NOTE 6 – Fair Value DISCLOSURES (Continued)**

For financial assets measured at fair value on a recurring and nonrecurring basis, the fair value measurements by level within the fair value hierarchy used are as follows:

| Description                               | Total          | (Level 1)<br>Quoted Prices<br>in Active<br>Markets for<br>Identical<br>Assets | (Level 2)<br>Significant<br>Other<br>Observable<br>Inputs | (Level 3)<br>Significant<br>Unobservable<br>Inputs |
|---|----------------|---|---|--|
| March 31, 2013:                           | (In Thousands) |   |   |  |
| Recurring:                                |                |   |   |  |
| Mortgage-backed securities - residential: |                |   |   |  |
| Federal Home Loan Mortgage Corporation    | \$ 75          | \$ —  | \$ 75   | \$ —   |
| Federal National Mortgage Association     | 51             | —   | 51  | —  |
| Total                                     | \$ 126         | \$ —  | \$ 126  | \$ —   |
| Nonrecurring:                             |                |   |   |  |
| Impaired loans                            | \$ 14,294      | \$ —  | \$ —  | \$ 14,294  |
| Real estate owned                         | \$ 4,271       | \$ —  | \$ —  | \$ 4,271   |
| December 31, 2012:                        |                |   |   |  |
| Recurring:                                |                |   |   |  |
| Mortgage-backed securities - residential: |                |   |   |  |
| Federal Home Loan Mortgage Corporation    | \$ 78          | \$ —  | \$ 78   | \$ —   |
| Federal National Mortgage Association     | 51             | —   | 51  | —  |
| Total                                     | \$ 129         | \$ —  | \$ 129  | \$ —   |
| Nonrecurring:                             |                |   |   |  |
| Impaired loans                            | \$ 10,515      | \$ —  | \$ —  | \$ 10,515  |
| Real estate owned                         | \$ 4,271       | \$ —  | \$ —  | \$ 4,271   |

The following table presents additional quantitative information about assets measured at fair value on a nonrecurring basis and for which the Company has utilized Level 3 inputs to determine fair value:

| (in thousands)    | Quantitative Information about Level 3 Fair Value Measurements |                                   |                                     |
|-------------------|--|-----------------------------------|-------------------------------------|
|                   | Fair Value Estimate  | Unobservable Valuation Techniques | Input Range                         |
| March 31, 2013:   |  |                                   |                                     |
| Impaired loans    | \$ 14,294  | Appraisal of collateral (1)       | Appraisal adjustments (2) 2% to 71% |
| Real estate owned | \$ 4,271   | Appraisal of collateral (1)       | Appraisal adjustments (2) 7% to 50% |

(1)

Fair value is generally determined through independent appraisals of the underlying collateral, which generally include various level 3 inputs which are not identifiable.

Appraisals may be adjusted by management for qualitative factors such as economic conditions and estimated (2) liquidation expenses. The range of liquidation expenses and other appraisal adjustments are presented as a percent of the appraisal.

Table of Contents**NOTE 6 – Fair Value DISCLOSURES (Continued)**

| (in thousands)     | Quantitative Information about Level 3 Fair Value Measurements |                             |                           |             |
|--------------------|--|-----------------------------|---------------------------|-------------|
|                    | Fair Value Estimate  | Valuation Techniques        | Input                     | Range       |
| December 31, 2012: |  |                             |                           |             |
| Impaired loans     | \$10,515   | Appraisal of collateral (1) | Appraisal adjustments (2) | 6.4% to 63% |
| Real estate owned  | \$4,271  | Appraisal of collateral (1) | Appraisal adjustments (2) | 6.8% to 50% |

(1) Fair value is generally determined through independent appraisals of the underlying collateral, which generally include various level 3 inputs which are not identifiable.

(2) Appraisals may be adjusted by management for qualitative factors such as economic conditions and estimated liquidation expenses. The range of liquidation expenses and other appraisal adjustments are presented as a percent of the appraisal.

Management uses its best judgment in estimating the fair value of the Company's financial instruments; however, there are inherent weaknesses in any estimation technique. Therefore, for substantially all financial instruments, the fair value estimates herein are not necessarily indicative of the amounts the Company could have realized in a sale transaction on the dates indicated. The estimated fair value amounts have been measured as of their respective year-ends and have not been re-evaluated or updated for purposes of these financial statements subsequent to those respective dates. As such, the estimated fair values of these financial instruments subsequent to the respective reporting dates may be different than the amounts reported at each year-end.

The following information should not be interpreted as an estimate of the fair value of the entire Company since a fair value calculation is only provided for a limited portion of the Company's assets and liabilities. Due to a wide range of valuation techniques and the degree of subjectivity used in making the estimates, comparisons between the Company's disclosures and those of other companies may not be meaningful. The following methods and assumptions were used to estimate the fair values of the Company's financial instruments at March 31, 2013 and December 31, 2012:

**Cash and Cash Equivalents, Certificates of Deposit and Accrued Interest Receivable and Payable**

For these short-term instruments, the carrying amount is a reasonable estimate of fair value.

**Securities**

Fair values for securities available for sale and held to maturity are determined utilizing Level 2 inputs. For these securities, the Company obtains fair value measurements from an independent pricing service. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayments speeds, credit information and the security's terms and conditions, among other things.

### **Loans Receivable**

Fair values are estimated for portfolios of loans with similar financial characteristics. The total loan portfolio is first divided into performing and non-performing categories. Performing loans are then segregated into adjustable and fixed rate interest terms. Fixed rate loans are segmented by type, such as construction and land development, other loans secured by real estate, commercial and industrial loans, and loans to individuals. Certain types, such as commercial loans and loans to individuals, are further segmented by maturity and type of collateral.

For performing loans, fair value is calculated by discounting scheduled future cash flows through estimated maturity using a current market rate. The discounted value of the cash flows is reduced by a credit risk adjustment based on internal loan classifications.

For certain impaired loans, fair value is calculated by first reducing the carrying value by a credit risk adjustment based on internal loan classifications, and then discounting the estimated future cash flows from the remaining carrying value at a market rate.

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**NOTE 6 – Fair Value DISCLOSURES (Continued)**

For the remaining impaired loans which the Company has measured and recorded impairment generally based on the fair value of the loan's collateral, fair value is generally determined based upon independent third-party appraisals of the properties. These assets are typically included as Level 3 fair values, based upon the lowest level of input that is significant to the fair value measurements.

**FHLB of New York Stock**

The carrying amount of the FHLB of New York stock is equal to its fair value, and considers the limited marketability of this security.

**Deposit Liabilities**

The fair value of deposits with no stated maturity, such as non-interest-bearing demand deposits, money market accounts, interest checking accounts, and savings accounts is equal to the amount payable on demand. Time deposits are segregated by type, size, and remaining maturity. The fair value of time deposits is based on the discounted value of contractual cash flows. The discount rate is based on rates currently offered in the market.

**FHLB of New York Advances**

The fair value of the FHLB advances is estimated based on the discounted value of future contractual payments. The discount rate is equivalent to the estimated rate at which the Company could currently obtain similar financing.

**Off-Balance- Sheet Financial Instruments**

The fair value of commitments to extend credit is estimated based on an analysis of the interest rates and fees currently charged to enter into similar transactions, considering the remaining terms of the commitments and the credit-worthiness of the potential borrowers. At March 31, 2013 and December 31, 2012, the estimated fair values of these off-balance-sheet financial instruments were immaterial.

The carrying amounts and estimated fair values of the Company's financial instruments are summarized below:

| (in thousands)                       | Carrying Amount | Fair Value Estimate | Fair Value at March 31, 2013                                   |   |   |
|--------------------------------------|-----------------|---------------------|--|---|---|
|                                      |                 |                     | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| <b>Financial Assets</b>              |                 |                     |  |   |   |
| Cash and cash equivalents            | \$24,981        | \$24,981            | \$24,981   | \$—   | \$—                                       |
| Certificates of deposit              | 150             | 150                 | —  | 150   | —   |
| Securities available for sale        | 126             | 126                 | —  | 126   | —   |
| Securities held to maturity          | 11,069          | 11,588              | —  | 11,588  | —   |
| Loans receivable                     | 343,939         | 358,906             | —  | —   | 358,906                                   |
| FHLB of New York stock               | 905             | 905                 | —  | 905   | —   |
| Accrued interest receivable          | 1,029           | 1,029               | —  | 1,029   | —   |
| <b>Financial Liabilities</b>         |                 |                     |  |   |   |
| Deposits, including accrued interest | 311,710         | 314,799             | —  | 314,799                                       | —   |
| FHLB of New York advances            | 5,000           | 5,163               | —  | 5,163   | —   |

Table of Contents**NOTE 6 – Fair Value DISCLOSURES (Continued)**

| (In thousands)                       | Carrying Amount | Fair Value Estimate | Fair Value at December 31, 2012                                |   |   |
|--------------------------------------|-----------------|---------------------|--|---|---|
|                                      |                 |                     | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| <b>Financial Assets</b>              |                 |                     |  |   |   |
| Cash and cash equivalents            | \$49,242        | \$49,242            | \$49,242   | \$—   | \$—                                       |
| Certificates of deposit              | 399             | 399                 | —  | 399   | —   |
| Securities available for sale        | 129             | 129                 | —  | 129   | —   |
| Securities held to maturity          | 11,987          | 12,561              | —  | 12,561  | —   |
| Loans receivable                     | 333,787         | 350,420             | —  | —   | 350,420                                   |
| FHLB of New York stock               | 1,355           | 1,355               | —  | 1,355   | —   |
| Accrued interest receivable          | 976             | 976                 | —  | 976   | —   |
| <b>Financial Liabilities</b>         |                 |                     |  |   |   |
| Deposits, including accrued interest | 318,120         | 321,236             | —  | 321,236                                       | —   |
| FHLB of New York advances            | 15,000          | 15,256              | —  | 15,256  | —   |

**NOTE 7 – LOANS RECEIVABLE AND THE ALLOWANCE FOR LOAN LOSSES**

|                                 | March 31, 2013 | December 31, 2012 |
|---------------------------------|----------------|-------------------|
| (In thousands)                  |                |                   |
| <b>Residential real estate:</b> |                |                   |
| One-to-four family              | \$8,043        | \$ 7,761          |
| Multi-family                    | 183,537        | 178,644           |
| Mixed use                       | 41,902         | 41,895            |
| Total residential real estate   | 233,482        | 228,300           |
| Non-residential real estate     | 84,714         | 82,312            |
| Construction                    | 2,216          | 841               |
| Commercial and industrial       | 27,459         | 26,274            |
| Consumer                        | 164            | 77                |
| <b>Total Loans</b>              | <b>348,035</b> | <b>337,804</b>    |

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|                              |           |            |
|------------------------------|-----------|------------|
| Allowance for loan losses    | (4,706 )  | (4,646 )   |
| Deferred loan fees and costs | 610       | 629        |
| Net Loans                    | \$343,939 | \$ 333,787 |

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## NOTE 7 – LOANS RECEIVABLE AND THE ALLOWANCE FOR LOAN LOSSES (Continued)

The following is an analysis of the allowance for loan losses:

**At and for the Three Months Ended March 31, 2013 (in thousands)**

|   | Residential<br>Real<br>Estate | Non-<br>residential<br>Real<br>Estate | Construction | Commercial<br>and<br>Industrial | Consumer | Total     |
|---|-------------------------------|---------------------------------------|--------------|---------------------------------|----------|-----------|
| Allowance for loan losses:                            |                               |                                       |              |                                 |          |           |
| Beginning balance                                     | \$3,216                       | \$996                                 | \$—          | \$434                           | \$—      | \$4,646   |
| Charge-offs   | —                             | —                                     | —            | —                               | —        | —         |
| Recoveries  | —                             | —                                     | —            | —                               | —        | —         |
| Provision   | 45                            | (12 )                                 | —            | 27                              | —        | 60        |
| Ending balance  | \$3,261                       | \$984                                 | \$—          | \$461                           | \$—      | \$4,706   |
| Ending balance: individually evaluated for impairment | \$—                           | \$—                                   | \$—          | \$—                             | \$—      | \$—       |
| Ending balance: collectively evaluated for impairment | \$3,261                       | \$984                                 | \$—          | \$461                           | \$—      | \$4,706   |
| Loans receivable:                                     |                               |                                       |              |                                 |          |           |
| Ending balance  | \$233,482                     | \$84,714                              | \$2,216      | \$27,459                        | \$164    | \$348,035 |
| Ending balance: individually evaluated for impairment | \$11,494                      | \$11,531                              | \$—          | \$1,851                         | \$—      | \$24,876  |
| Ending balance: collectively evaluated for impairment | \$221,988                     | \$73,183                              | \$2,216      | \$25,608                        | \$164    | \$323,159 |

**At and for the Three Months Ended March 31, 2012 (in thousands)**

|   | Residential<br>Real<br>Estate | Non-<br>residential<br>Real<br>Estate | Construction | Commercial<br>and<br>Industrial | Consumer | Total   |
|---|-------------------------------|---------------------------------------|--------------|---------------------------------|----------|---------|
| Allowance for loan losses:                            |                               |                                       |              |                                 |          |         |
| Beginning balance                                     | \$3,781                       | \$1,596                               | \$1,724      | \$296                           | \$—      | \$7,397 |
| Charge-offs   | (305 )                        | —                                     | (11 )        | —                               | —        | (316 )  |
| Recoveries  | 5                             | —                                     | —            | —                               | —        | 5       |
| Provision   | (201 )                        | 259                                   | (53 )        | (5 )                            | —        | —       |
| Ending balance  | \$3,280                       | \$1,855                               | \$1,660      | \$291                           | \$—      | \$7,086 |
| Ending balance: individually evaluated for impairment | \$490                         | \$603                                 | \$1,660      | \$—                             | \$—      | \$2,753 |

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|   |           |          |         |          |      |           |
|---|-----------|----------|---------|----------|------|-----------|
| Ending balance: collectively evaluated for impairment | \$2,790   | \$1,252  | \$—     | \$291    | \$—  | \$4,333   |
| Loans receivable:                                     |           |          |         |          |      |           |
| Ending balance  | \$240,388 | \$89,862 | \$7,674 | \$21,554 | \$62 | \$359,540 |
| Ending balance: individually evaluated for impairment | \$11,156  | \$9,856  | \$7,674 | \$—      | \$—  | \$28,686  |
| Ending balance: collectively evaluated for impairment | \$229,232 | \$80,006 | \$—     | \$21,554 | \$62 | \$330,854 |

Table of Contents**NOTE 7 – LOANS RECEIVABLE AND THE ALLOWANCE FOR LOAN LOSSES (Continued)****At and for the Year Ended December 31, 2012 (in thousands)**

|   | Residential<br>Real<br>Estate | Non-<br>residential<br>Real<br>Estate | Construction | Commercial<br>and<br>Industrial | Consumer | Total     |
|---|-------------------------------|---------------------------------------|--------------|---------------------------------|----------|-----------|
| Allowance for loan losses:                            |                               |                                       |              |                                 |          |           |
| Beginning balance                                     | \$3,781                       | \$1,596                               | \$1,724      | \$296                           | \$—      | \$7,397   |
| Charge-offs   | (4,372 )                      | (2,374 )                              | (1,715 )     | (28 )                           | —        | (8,489 )  |
| Recoveries  | 115                           | —                                     | —            | —                               | —        | 115       |
| Provision   | 3,692                         | 1,774                                 | (9 )         | 166                             | —        | 5,623     |
| Ending balance  | \$3,216                       | \$996                                 | \$—          | \$434                           | \$—      | \$4,646   |
| Ending balance: individually evaluated for impairment | \$—                           | \$—                                   | \$—          | \$—                             | \$—      | \$—       |
| Ending balance: collectively evaluated for impairment | \$3,216                       | \$996                                 | \$—          | \$434                           | —        | \$4,646   |
| Loans receivable:                                     |                               |                                       |              |                                 |          |           |
| Ending balance  | \$228,300                     | \$82,312                              | \$841        | \$26,274                        | \$77     | \$337,804 |
| Ending balance: individually evaluated for impairment | \$10,272                      | \$8,272                               | \$—          | \$2,152                         | \$—      | \$20,696  |
| Ending balance: collectively evaluated for impairment | \$218,028                     | \$74,040                              | \$841        | \$24,122                        | \$77     | \$317,108 |

The following is an analysis of the Company's impaired loans.

**Impaired Loans as of or for the three months ended March 31, 2013 (in thousands)**

| <u>2013</u>                          | Recorded<br>Investment | Unpaid<br>Principal<br>Balance | Related<br>Allowance | Average<br>Recorded<br>Investment | Interest<br>Income<br>Recognized |
|--------------------------------------|------------------------|--------------------------------|----------------------|-----------------------------------|----------------------------------|
| With no related allowance recorded:  |                        |                                |                      |                                   |                                  |
| Residential real estate-Multi-family | \$ 11,494              | \$ 12,552                      | \$ —                 | \$ 10,883                         | \$ 169                           |
| Non-residential real estate          | 11,531                 | 14,604                         | —                    | 9,902                             | 15                               |
| Commercial and industrial            | 1,851                  | 1,851                          | —                    | 2,001                             | 29                               |
| Subtotal                             | 24,876                 | 29,007                         | —                    | 22,786                            | 213                              |

With an allowance recorded:

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|                                      |           |           |      |           |        |
|--------------------------------------|-----------|-----------|------|-----------|--------|
| Residential real estate-Multi-family | —         | —         | —    | —         | —      |
| Non-residential real estate          | —         | —         | —    | —         | —      |
| Commercial and industrialonstruction | —         | —         | —    | —         | —      |
| Subtotal                             | —         | —         | —    | —         | —      |
| Total:                               |           |           |      |           |        |
| Residential real estate-Multi-family | 11,494    | 12,552    | —    | 10,883    | 169    |
| Non-residential real estate          | 11,531    | 14,604    | —    | 9,902     | 15     |
| Commercial and industrial            | 1,851     | 1,851     | —    | 2,001     | 29     |
| Total                                | \$ 24,876 | \$ 29,007 | \$ — | \$ 22,786 | \$ 213 |

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## NOTE 7 – LOANS RECEIVABLE AND THE ALLOWANCE FOR LOAN LOSSES (Continued)

**Impaired Loans as of or for the three months ended March 31, 2012 (in thousands)**

| <u>2012</u>                          | Recorded<br>Investment | Unpaid<br>Principal<br>Balance | Related<br>Allowance | Average<br>Recorded<br>Investment | Interest<br>Income<br>Recognized |
|--------------------------------------|------------------------|--------------------------------|----------------------|-----------------------------------|----------------------------------|
| With no related allowance recorded:  |                        |                                |                      |                                   |                                  |
| Residential real estate-Multi-family | \$ 10,145              | \$ 10,145                      | \$ —                 | \$ 10,286                         | \$ 65                            |
| Non-residential real estate          | 6,612                  | 6,612                          | —                    | 6,561                             | 9                                |
| Construction                         | —                      | —                              | —                    | —                                 | —                                |
| Subtotal                             | 16,757                 | 16,757                         | —                    | 16,847                            | 74                               |
| With an allowance recorded:          |                        |                                |                      |                                   |                                  |
| Residential real estate-Multi-family | 1,011                  | 1,011                          | 490                  | 988                               | —                                |
| Non-residential real estate          | 3,244                  | 3,244                          | 603                  | 3,201                             | 7                                |
| Construction                         | 7,674                  | 7,674                          | 1,660                | 7,628                             | —                                |
| Subtotal                             | 11,929                 | 11,929                         | 2,753                | 11,817                            | 7                                |
| Total:                               |                        |                                |                      |                                   |                                  |
| Residential real estate-Multi-family | 11,156                 | 11,156                         | 490                  | 11,274                            | 65                               |
| Non-residential real estate          | 9,856                  | 9,856                          | 603                  | 9,762                             | 16                               |
| Construction                         | 7,674                  | 7,674                          | 1,660                | 7,628                             | —                                |
| Total                                | \$ 28,686              | \$ 28,686                      | \$ 2,753             | \$ 28,664                         | \$ 81                            |

**Impaired Loans as of and for the Year Ended December 31, 2012 (in thousands)**

| <u>2012</u>                          | Recorded<br>Investment | Unpaid<br>Principal<br>Balance | Related<br>Allowance | Average<br>Recorded<br>Investment | Interest<br>Income<br>Recognized |
|--------------------------------------|------------------------|--------------------------------|----------------------|-----------------------------------|----------------------------------|
| With no related allowance recorded:  |                        |                                |                      |                                   |                                  |
| Residential real estate-Multi-family | \$ 10,272              | \$ 11,742                      | \$ —                 | \$ 10,876                         | \$ 496                           |
| Non-residential real estate          | 8,272                  | 11,345                         | —                    | 11,322                            | 1,439                            |
| Construction                         | —                      | —                              | —                    | 3,067                             | —                                |
| Commercial and industrial            | 2,152                  | 2,179                          | —                    | 1,130                             | 126                              |
| Subtotal                             | 20,696                 | 25,266                         | —                    | 26,395                            | 2,061                            |
| With an allowance recorded:          |                        |                                |                      |                                   |                                  |
| Residential real estate-Multi-family | —                      | —                              | —                    | —                                 | —                                |
| Non-residential real estate          | —                      | —                              | —                    | —                                 | —                                |
| Commercial and industrial            | —                      | —                              | —                    | —                                 | —                                |
| Subtotal                             | —                      | —                              | —                    | —                                 | —                                |

Total:

|                                      |           |           |      |           |          |
|--------------------------------------|-----------|-----------|------|-----------|----------|
| Residential real estate-Multi-family | 10,272    | 11,742    | —    | 10,876    | 496      |
| Non-residential real estate          | 8,272     | 11,345    | —    | 11,322    | 1,439    |
| Construction                         | —         | —         | —    | 3,067     | —        |
| Commercial and industrial            | 2,152     | 2,179     | —    | 1,130     | 126      |
| Total                                | \$ 20,696 | \$ 25,266 | \$ — | \$ 26,395 | \$ 2,061 |

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## NOTE 7 – LOANS RECEIVABLE AND THE ALLOWANCE FOR LOAN LOSSES (Continued)

The following table provides information about delinquencies in our loan portfolio at the dates indicated.

**Age Analysis of Past Due Loans as of March 31, 2013 (in thousands)**

|                                 | 30-59<br>Days<br>Past Due | 60 – 89<br>Days Past<br>Due | Greater<br>Than 90<br>Days | Total Past<br>Due | Current   | Total<br>Loans<br>Receivable | Recorded<br>Investment<br>> 90 Days<br>and<br>Accruing |
|---------------------------------|---------------------------|-----------------------------|----------------------------|-------------------|-----------|------------------------------|--|
| Residential real estate:        |                           |                             |                            |                   |           |                              |  |
| One- to four-family             | \$ —                      | \$ —                        | \$ —                       | \$ —              | \$8,043   | \$ 8,043                     | \$ —   |
| Multi-family                    | 942                       | —                           | —                          | 942               | 182,595   | 183,537                      | —  |
| Mixed-use                       | —                         | 312                         | —                          | 312               | 41,590    | 41,902                       | —  |
| Non-residential real estate     | —                         | 3,159                       | 2,030                      | 5,189             | 79,525    | 84,714                       | —  |
| Construction loans              | —                         | —                           | —                          | —                 | 2,216     | 2,216                        | —  |
| Commercial and industrial loans | —                         | —                           | —                          | —                 | 27,459    | 27,459                       | —  |
| Consumer.                       | —                         | —                           | —                          | —                 | 164       | 164                          | —  |
| Total loans                     | \$ 942                    | \$ 3,471                    | \$ 2,030                   | \$ 6,443          | \$341,592 | \$ 348,035                   | \$ —   |

**Age Analysis of Past Due Loans as of December 31, 2012 (in thousands)**

|                                 | 30-59<br>Days<br>Past Due | 60 – 89<br>Days Past<br>Due | Greater<br>Than 90<br>Days | Total Past<br>Due | Current   | Total<br>Loans<br>Receivable | Recorded<br>Investment<br>> 90 Days<br>and<br>Accruing |
|---------------------------------|---------------------------|-----------------------------|----------------------------|-------------------|-----------|------------------------------|--|
| Residential real estate:        |                           |                             |                            |                   |           |                              |  |
| One- to four-family             | \$ —                      | \$ —                        | \$ —                       | \$ —              | \$7,761   | \$ 7,761                     | \$ —   |
| Multi-family                    | —                         | 89                          | 1,266                      | 1,355             | 177,289   | 178,644                      | —  |
| Mixed-use                       | —                         | —                           | —                          | —                 | 41,895    | 41,895                       | —  |
| Non-residential real estate     | 1,259                     | —                           | 1,221                      | 2,480             | 79,832    | 82,312                       | —  |
| Construction loans              | —                         | —                           | —                          | —                 | 841       | 841                          | —  |
| Commercial and industrial loans | —                         | —                           | —                          | —                 | 26,274    | 26,274                       | —  |
| Consumer                        | —                         | —                           | —                          | —                 | 77        | 77                           | —  |
| Total loans                     | \$ 1,259                  | \$ 89                       | \$ 2,487                   | \$ 3,835          | \$333,969 | \$ 337,804                   | \$ —   |





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## NOTE 7 – LOANS RECEIVABLE AND THE ALLOWANCE FOR LOAN LOSSES (Continued)

The following tables provide certain information related to the credit quality of the loan portfolio.

**Credit Quality Indicators as of March 31, 2013 (in thousands)****Credit Risk Profile by Internally Assigned Grade**

|                 | Residential<br>Real Estate | Non-<br>residential<br>Real Estate | Construction | Commercial<br>and<br>Industrial | Consumer | Total     |
|-----------------|----------------------------|------------------------------------|--------------|---------------------------------|----------|-----------|
| Grade:          |                            |                                    |              |                                 |          |           |
| Pass            | \$ 226,007                 | \$ 73,182                          | \$ 2,216     | \$ 25,607                       | \$ 164   | \$327,176 |
| Special Mention | 2,376                      | 514                                | —            | —                               | —        | 2,890     |
| Substandard     | 5,099                      | 11,018                             | —            | 1,852                           | —        | 17,969    |
| Total           | \$ 233,482                 | \$ 84,714                          | \$ 2,216     | \$ 27,459                       | \$ 164   | \$348,035 |

**Credit Quality Indicators as of December 31, 2012 (in thousands)****Credit Risk Profile by Internally Assigned Grade**

|                 | Residential<br>Real Estate | Non-<br>residential<br>Real Estate | Construction | Commercial<br>and<br>Industrial | Consumer | Total     |
|-----------------|----------------------------|------------------------------------|--------------|---------------------------------|----------|-----------|
| Grade:          |                            |                                    |              |                                 |          |           |
| Pass            | \$ 221,794                 | \$ 74,040                          | \$ 841       | \$ 24,122                       | \$ 77    | \$320,874 |
| Special Mention | 2,553                      | 505                                | —            | —                               | —        | 3,058     |
| Substandard     | 3,953                      | 7,767                              | —            | 2,152                           | —        | 13,872    |
| Total           | \$ 228,300                 | \$ 82,312                          | \$ 841       | \$ 26,274                       | \$ 77    | \$337,804 |

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NOTE 7 - LOANS RECEIVABLE AND THE ALLOWANCE FOR LOAN LOSSES (Continued)

The following table sets forth the composition of our nonaccrual loans at the dates indicated.

**Loans Receivable on Nonaccrual Status as of March 31, 2013 and December 31, 2012 (in thousands)**

|                                      | 2013    | 2012    |
|--------------------------------------|---------|---------|
| Residential real estate-Multi-family | \$2,719 | \$1,477 |
| Non-residential real estate          | 5,189   | 2,480   |
| Total                                | \$7,908 | \$3,957 |

The following table shows the breakdown of loans modified for the periods indicated:

|  | <b>Three Months Ended March 31, 2013</b> |  |   |   |
|--|--|--|---|---|
|  | <b>Number of Modifications</b>           | <b>Recorded Investment Prior to Modification</b> | <b>Recorded Investment After Modification</b> |   |
| <b>(dollars in thousands)</b> Residential real estate: |  |  |   |   |
| Multi-family   | —  | \$ —   | \$ —  | — |

As of March 31, 2013, none of the loans that were modified during the previous twelve months had defaulted in the three month period ended March 31, 2013.

|  | <b>Three Months Ended March 31, 2012</b> |  |   |   |
|--|--|--|---|---|
|  | <b>Number of Modifications</b>           | <b>Recorded Investment Prior to Modification</b> | <b>Recorded Investment After Modification</b> |   |
| <b>(dollars in thousands)</b> Residential real estate: |  |  |   |   |
| Multi-family   | —  | \$ —   | \$ —  | — |

As of March 31, 2012, none of the loans that were modified during the previous twelve months had defaulted in the three month period ended March 31, 2012.

#### **NOTE 8 – EFFECT OF RECENT ACCOUNTING PRONOUNCEMENTS**

In July 2012, the FASB issued Accounting Standards Update (“ASU”) 2012-02, *Testing Indefinite-Lived Intangible Assets for Impairment. Similar to ASU 2011-08, Intangibles - Goodwill and Other (Topic 250) - Testing Goodwill for Impairment*. ASU 2012-02 addresses the growing cost and complexity of performing an analysis to evaluate indefinite-lived intangible assets (other than goodwill) for impairment. This ASU introduces qualitative factors which would simplify the analysis if facts and circumstances make it more-likely-than-not that impairment would not exist. Rather than requiring a purely quantitative impairment test, the ASU provides entities with the option to first examine qualitative factors to make this determination. Factors to be considered would include, but are not limited to:

Increases in interest rates, salaries, or other operating expenses, which would have a negative impact on future earnings or cash flows;

Recent financial performance and cash flow trends;

Aspects of the legal and regulatory environment which are expected to impact future cash flows, such as the Dodd-Frank Act;

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**NOTE 8 – EFFECT OF RECENT ACCOUNTING PRONOUNCEMENTS (Continued)**

Management turnover;

Economic and industry conditions.

Entities are required by the guidance to consider both positive and negative impacts of such factors before determining whether it is more-likely-than-not (i.e. greater than 50% probability) that the indefinite-lived intangible asset is impaired. It should be noted that the qualitative portion of the analysis is optional for all issuers.

This ASU is effective for impairment tests performed during fiscal years beginning after September 15, 2012, and may be early adopted if the entity's financial statements for the most recent fiscal or interim period have not yet been issued. The Company adopted this guidance in 2013. The adoption had no material effect on the Company's financial statements.

*ASU 2013-02: Comprehensive Income (Topic 220) – Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income.* The objective of this ASU is to improve the reporting of reclassifications out of accumulated other comprehensive income. This ASU requires an entity to report the effect of significant reclassifications out of accumulated other comprehensive income, by component, on the respective line items in the income statement if the amount being reclassified is required under U.S. generally accepted accounting principles (GAAP) to be reclassified in its entirety to net income. Reclassifications that are not required under U.S. GAAP to be reclassified in their entirety to net income in the same reporting period are required to be cross-referenced to other U.S. GAAP disclosures that provide additional detail about those amounts. This is the case when a portion of the amount reclassified out of accumulated other comprehensive income is reclassified to a balance sheet account rather than directly to income or expense in the same reporting period. For example, some portion of net periodic pension cost is immediately reported in net income, but other portions may be capitalized to an asset balance such as fixed assets or inventory. An entity with significant defined benefit pension costs reclassified out of accumulated other comprehensive income but not to net income in its entirety in the same reporting period should identify the amount of each pension cost component reclassified out of accumulated other comprehensive income and make reference to the relevant pension cost disclosure that provides greater detail about these reclassifications.

The amendments do not change the current requirements for reporting net income or other comprehensive income in financial statements. However, the amendments require an entity to provide information about the amounts reclassified out of accumulated other comprehensive income by component. In addition, an entity is required to present, either on the face of the statement where net income is presented or in the notes, significant amounts reclassified out of accumulated other comprehensive income.

The provisions of this ASU are effective for public entities prospectively for reporting periods beginning after December 15, 2012. The Company adopted this guidance in 2013. The adoption had no material effect on the Company's financial statements.

#### **NOTE 9 – DIVIDEND RESTRICTION**

The MHC held 7,273,750 shares, or 57.5%, of the Company's issued and outstanding common stock, and the minority public shareholders held 42.5% of outstanding stock, at March 31, 2013. The MHC filed notice with, and received approval from, the Federal Reserve Bank of Philadelphia to waive its right to receive cash dividends for the period from November 9, 2012 through November 9, 2013.

The MHC has waived receipt of all past dividends paid by the Company through March 31, 2013 with the exception of the dividend for the quarter ended June 30, 2012. Because the MHC determined not to waive receipt of the dividend for the quarter ended June 30, 2012, the MHC received \$218,000 in dividends in August 2012. The dividends waived are considered as a restriction on the retained earnings of the Company. As of March 31, 2013 and December 31, 2012, the aggregate retained earnings restricted for cash dividends waived were \$4,582,000 and \$4,364,000, respectively.

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

**FORWARD-LOOKING STATEMENTS**

This quarterly report contains forward-looking statements that are based on assumptions and may describe future plans, strategies and expectations of the Company. These forward-looking statements are generally identified by use of the words “believe,” “expect,” “intend,” “anticipate,” “estimate,” “project” or similar expressions. The Company’s ability to predict results or the actual effect of future plans or strategies is inherently uncertain. Factors which could have a material adverse effect on the operations of the Company include, but are not limited to, changes in interest rates, national and regional economic conditions, legislative and regulatory changes, monetary and fiscal policies of the U.S. government, including policies of the U.S. Treasury and the Federal Reserve Board, the quality and composition of the loan or investment portfolios, demand for loan products, deposit flows, competition, demand for financial services in the Company’s market area, changes in real estate market values in the Company’s market area, and changes in relevant accounting principles and guidelines. Additional factors that may affect the Company’s results are discussed in the Company’s Annual Report on Form 10-K under “Item 1A. Risk Factors.” These risks and uncertainties should be considered in evaluating forward-looking statements and undue reliance should not be placed on such statements. Except as required by applicable law or regulation, the Company does not undertake, and specifically disclaims any obligation, to release publicly the result of any revisions that may be made to any forward-looking statements to reflect events or circumstances after the date of the statements or to reflect the occurrence of anticipated or unanticipated events.

**CRITICAL ACCOUNTING POLICIES**

We consider accounting policies involving significant judgments and assumptions by management that have, or could have, a material impact on the carrying value of certain assets or on income to be critical accounting policies. We consider the allowance for loan losses to be a critical accounting policy.

***Allowance for Loan Losses.*** The allowance for loan losses is the amount estimated by management as necessary to cover probable credit losses in the loan portfolio at the statement of financial condition date. The allowance is established through the provision for loan losses, which is charged to income. Determining the amount of the allowance for loan losses necessarily involves a high degree of judgment. Among the material estimates required to establish the allowance are: loss exposure at default; the amount and timing of future cash flows on impaired loans; value of collateral; and determination of loss factors to be applied to the various elements of the portfolio. All of these estimates are susceptible to significant change. Management reviews the level of the allowance on a quarterly basis and establishes the provision for loan losses based upon an evaluation of the portfolio, past loss experience, current economic conditions and other factors related to the collectability of the loan portfolio. Although we believe that we use the best information available to establish the allowance for loan losses, future adjustments to the allowance may be necessary if economic conditions differ substantially from the assumptions used in making the evaluation.

Due to the conversion of the Bank to a New York State-chartered savings bank on June 29, 2012, the Federal Deposit Insurance Corporation (“FDIC”) and the New York State Department of Financial Services (“NYS”) are now the Bank’s primary regulator. As such, the FDIC and NYS, as an integral part of their examination process, periodically review our allowance for loan losses. The FDIC and NYS could require us to recognize adjustments to the allowance based on their judgments about information available to them at the time of their examinations. A large loss or a series of losses could deplete the allowance and require increased provisions to replenish the allowance, which would negatively affect earnings. For additional discussion, see Note 1 to the consolidated financial statements included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2012.

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**First Quarter Performance Highlights**

The Company's earnings for the quarter ended March 31, 2013 decreased by \$45,000 compared to the same period in 2012 primarily due to increases in non-interest expense and provision for loan losses, offset by increases in net interest income and non-interest income and a decrease in the provision for income taxes. The increase in non-interest expense was due to the expansion of our Massachusetts branch operations with the opening of two new branch sites in Framingham and Quincy, the hiring of additional employees to staff the new branches, and the purchase of additional equipment and services to support the expansion.

Despite operating in a challenging low interest rate environment, the Company improved its net interest income in 2013 compared to 2012, with an increase in our interest rate spread and net interest margin to 3.72% and 3.97%, respectively.

Although non-performing loans increased by \$3.9 million to \$7.9 million as of March 31, 2013 from \$4.0 million as of December 31, 2012 due to the addition of seven mortgage loans totaling \$4.6 million, our non-performing loans decreased by \$11.4 million to \$7.9 million as of March 31, 2013 from \$19.3 million as of March 31, 2012. The decrease in non-performing loans from March 31, 2012 to March 31, 2013 was due to the satisfaction of seven mortgage loans totaling \$3.8 million, the conversion from non-performing to performing status of five mortgage loans totaling \$8.9 million, and the conversion to real estate owned of two mortgage loans totaling \$5.0 million, partially offset by the addition of eleven non-performing mortgage loans totaling \$6.3 million.

We will continue to monitor our loan portfolio closely and adjust the level of allowance for loan losses appropriately as updated information becomes available.

**Comparison of Financial Condition at March 31, 2013 and December 31, 2012**

Total assets decreased by \$15.7 million, or 3.5%, to \$428.6 million at March 31, 2013 from \$444.2 million at December 31, 2012. The decrease in total assets was due to decreases of \$24.3 million in cash and cash equivalents, \$918,000 in securities held-to-maturity, \$450,000 in Federal Home Loan Bank of New York ("FHLB") stock, \$249,000 in certificates of deposits at other financial institutions, and \$239,000 in premises and equipment, partially offset by increases of \$10.2 million in loans receivable, net, and \$157,000 in bank owned life insurance.

The decrease in total assets resulted primarily from decreases of \$10.0 million in FHLB advances and \$6.4 million in deposits, partially offset by an increase of \$592,000 in advance payments by borrowers for taxes and insurance, and \$141,000 in stockholders' equity.



Cash and cash equivalents decreased by \$24.3 million, or 49.3%, to \$25.0 million at March 31, 2013 from \$49.2 million at December 31, 2012 due primarily to decreases of \$6.4 million in deposits and repayment of \$10.0 million in FHLB advances, and an increase of \$10.2 million in loans receivable, net, offset by increases of \$592,000 in advance payments by borrowers for taxes and insurance.

Securities held-to-maturity decreased by \$918,000, or 7.7%, to \$11.1 million at March 31, 2013 from \$12.0 million at December 31, 2012 due entirely to repayments of \$918,000. Certificates of deposits at other financial institutions decreased by \$249,000, or 62.4%, to \$150,000 at March 31, 2013 from \$399,000 at December 31, 2012 due to the maturity and redemption of various certificates of deposits.

Loans receivable, net, increased by \$10.2 million, or 3.0%, to \$343.9 million at March 31, 2013 from \$333.8 million at December 31, 2012 due primarily to loan originations totaling \$19.4 million that exceeded loan repayments totaling \$9.2 million.

FHLB stock decreased by \$450,000, or 33.2%, to \$905,000 at March 31, 2013 from \$1.4 million at December 31, 2012 due primarily to a decrease in the amount of FHLB stock that we are required to hold as a result of decreases in FHLB advances.

Premises and equipment decreased by \$239,000, or 1.9%, to \$12.7 million at March 31, 2013 from \$12.9 million at December 31, 2012 due primarily to depreciation.

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Bank owned life insurance increased by \$157,000, or 0.8%, to \$20.0 million at March 31, 2013 from \$19.9 million at December 31, 2012 due primarily to accrued earnings during the March 31, 2013 quarter.

Deposits decreased by \$6.4 million, or 2.0%, to \$311.7 million at March 31, 2013 from \$318.1 million at December 31, 2012. The decrease in deposits was primarily attributable to decreases of \$2.8 million in our non-interest bearing accounts, \$2.7 million in our regular savings accounts, and \$1.4 million in our NOW and money market accounts, offset by an increase of \$465,000 in certificates of deposits. The decrease in deposits was due to the Company's decision to reduce interest rates that resulted in an outflow of deposits that exceeded the deposit inflow, primarily in certificates of deposit, due to the opening of the two new branches in Framingham and Quincy, Massachusetts.

Advance payments by borrowers for taxes and insurance increased by \$592,000, or 16.8%, to \$4.1 million at March 31, 2013 from \$3.5 million at December 31, 2012 due primarily to an increase in the loan portfolio and the resulting accumulating balances paid into escrow accounts by borrowers.

FHLB advances decreased by \$10.0 million, or 66.7%, to \$5.0 million at March 31, 2013 from \$15.0 million at December 31, 2012 due to the maturity and repayment of two \$5.0 million FHLB advances.

Stockholders' equity increased by \$141,000, or 0.1%, to \$104.0 million at March 31, 2013, from \$103.8 million at December 31, 2012. This increase was primarily the result of comprehensive income of \$257,000 and the amortization of \$35,000 for the ESOP for the period, partially offset by cash dividends declared of \$151,000.

**Comparison of Operating Results for the Three Months Ended March 31, 2013 and 2012**

**General.** Net income decreased by \$45,000, or 17.9%, to \$207,000 for the quarter ended March 31, 2013, from \$252,000 for the quarter ended March 31, 2012. The decrease was primarily the result of increases of \$113,000 in non-interest expense and \$60,000 in provision for loan losses, partially offset by increases of \$51,000 in net interest income and \$30,000 in non-interest income and a decrease of \$47,000 in the provision for income taxes.

**Net Interest Income.** Net interest income increased by \$51,000, or 1.3%, to \$3.92 million for the three months ended March 31, 2013 from \$3.87 million for the three months ended March 31, 2012. The increase in net interest income was due primarily to a decrease of \$346,000 in interest expense that exceeded a decrease of \$295,000 in interest income for the comparable period in 2012 and increases in the net interest spread and the net interest margin.

The net interest spread increased by 71 basis points to 3.72% for the three months ended March 31, 2013 from 3.01% for the three months ended March 31, 2012. The net interest margin increased by 67 basis points between these periods to 3.97% for the quarter ended March 31, 2013 from 3.30% for the quarter ended March 31, 2012. The increase in the interest rate spread and the net interest margin in the first quarter of 2013 compared to the same period in 2012 was due to an increase in the yield on our interest-earning assets coupled with a decrease in the cost of our interest-bearing liabilities.

In this regard, the yield on our interest-earning assets increased by 51 basis points to 4.81% for the three months ended March 31, 2013 from 4.30% for the three months ended March 31, 2012 and the cost of our interest-bearing liabilities decreased by 19 basis points to 1.09% for the three months ended March 31, 2013 from 1.28% for the three months ended March 31, 2012. The increase in the yield on our interest-earning assets was due to a decrease in other interest-earning assets, resulting in a shift in the composition of interest-earning assets whereby higher yielding loans receivable represented a larger percentage of total interest-earning assets in the March 31, 2013 quarter compared to the March 31, 2012 quarter. The increase in the yield on our interest-earning assets was also due to a decrease in our non-performing assets by \$11.4 million, or 59%, to \$7.9 million as of March 31, 2013 from \$19.3 million as of March 31, 2012.

The decrease in the cost of our interest-bearing liabilities was due to the low interest rate environment in 2012 which continued into the first quarter of 2013 resulting in a decrease in the cost of our interest-bearing deposits as deposits continued to re-price to lower interest rates.

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The following table summarizes average balances and average yields and costs of interest-earning assets and interest-bearing liabilities for the three months ended March 31, 2013 and 2012.

|   | Three Months Ended March 31, |                              |                |                    |                              |                |
|---|------------------------------|------------------------------|----------------|--------------------|------------------------------|----------------|
|   | 2013                         |                              |                | 2012               |                              |                |
|   | Average<br>Balance           | Interest<br>and<br>Dividends | Yield/<br>Cost | Average<br>Balance | Interest<br>and<br>Dividends | Yield/<br>Cost |
|   | (Dollars in thousands)       |                              |                |                    |                              |                |
| <b>Assets:</b>  |                              |                              |                |                    |                              |                |
| <b>Interest-earning assets:</b>                         |                              |                              |                |                    |                              |                |
| Loans   | \$344,597                    | \$4,646                      | 5.39 %         | \$360,830          | \$4,893                      | 5.42 %         |
| Securities (including FHLB stock)                       | 12,993                       | 99                           | 3.05           | 17,495             | 138                          | 3.16           |
| Other interest-earning assets                           | 37,494                       | 3                            | 0.03           | 91,188             | 12                           | 0.05           |
| Total interest-earning assets                           | 395,084                      | 4,748                        | 4.81           | 469,513            | 5,043                        | 4.30           |
| Allowance for loan losses                               | (4,323 )                     |                              |                | (7,214 )           |                              |                |
| Non-interest-earning assets                             | 49,922                       |                              |                | 35,086             |                              |                |
| Total assets  | \$440,683                    |                              |                | \$497,385          |                              |                |
| <b>Liabilities and equity:</b>                          |                              |                              |                |                    |                              |                |
| <b>Interest-bearing liabilities:</b>                    |                              |                              |                |                    |                              |                |
| Interest-bearing demand                                 | \$61,857                     | \$50                         | 0.32           | \$119,307          | \$251                        | 0.84           |
| Savings and club accounts                               | 83,241                       | 109                          | 0.52           | 87,582             | 198                          | 0.90           |
| Certificates of deposit                                 | 148,011                      | 569                          | 1.54           | 140,677            | 583                          | 1.66           |
| Total interest-bearing deposits                         | 293,109                      | 728                          | 0.99           | 347,566            | 1,032                        | 1.19           |
| Borrowings  | 11,278                       | 101                          | 3.58           | 19,115             | 143                          | 2.99           |
| Total interest-bearing liabilities                      | 304,387                      | 829                          | 1.09           | 366,681            | 1,175                        | 1.28           |
| Noninterest-bearing demand                              | 23,667                       |                              |                | 16,498             |                              |                |
| Other liabilities                                       | 7,132                        |                              |                | 6,737              |                              |                |
| Total liabilities                                       | 335,186                      |                              |                | 389,916            |                              |                |
| Stockholders' equity                                    | 105,497                      |                              |                | 107,469            |                              |                |
| Total liabilities and Stockholders' equity              | \$440,683                    |                              |                | \$497,385          |                              |                |
| Net interest income                                     |                              | \$3,919                      |                |                    | \$3,868                      |                |
| Interest rate spread                                    |                              |                              | 3.72           |                    |                              | 3.01           |
| Net interest margin                                     |                              |                              | 3.97           |                    |                              | 3.30           |
| Net interest-earning assets                             | \$90,697                     |                              |                | \$102,832          |                              |                |
| Interest-earning assets to interest-bearing liabilities | 129.80 %                     |                              |                | 128.04 %           |                              |                |

Total interest income decreased by \$295,000, or 5.8%, to \$4.7 million for the three months ended March 31, 2013, from \$5.0 million for the three months ended March 31, 2012. Interest income on loans decreased by \$247,000, or 5.0%, to \$4.7 million for the three months ended March 31, 2013 from \$4.9 million for the three months ended March 31, 2012 as a result of a decrease of 3 basis points in the average yield on loans to 5.39% for the three months ended March 31, 2013 from 5.42% for the three months ended March 31, 2012. The decrease in interest income and the

average yield on loans was due to the pay-off of numerous higher yielding mortgage loans and the refinancing and/or re-pricing to lower interest rates of numerous mortgage loans in our loan portfolio. The decrease in interest income was also due to a decrease of \$16.2 million, or 4.5%, in the average balance of the loan portfolio to \$344.6 million for the three months ended March 31, 2013 from \$360.8 million for the three months ended March 31, 2012. The decrease in the average balance of the loan portfolio was due to repayments outpacing originations and charge-offs, net of recoveries, of \$8.5 million in loans in 2012.

Interest income on securities decreased by \$39,000, or 28.3%, to \$99,000 for the three months ended March 31, 2013 from \$138,000 for the three months ended March 31, 2012. The decrease was primarily due to a decrease of \$4.5 million, or 25.7%, in the average balance of securities to \$13.0 million for the three months ended March 31, 2013 from \$17.5 million for the three months ended March 31, 2012. The decrease in the average balance was due to the principal repayments on investment securities and a decrease in FHLB New York stock. The decrease in interest income on securities was also due to a decrease of 11 basis points in the average yield on securities to 3.05% for the three months ended March 31, 2013 from 3.16% for the three months ended March 31, 2012. The decline in the yield was due to the re-pricing of the yield of our adjustable rate investment securities and a decrease in FHLB stock yield from 4.5% at March 31, 2012 to 4.0% at March 31, 2013.

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Interest income on other interest-earning assets (consisting solely of interest-earning deposits) decreased by \$9,000, or 75.0%, to \$3,000 for the three months ended March 31, 2013 from \$12,000 for the three months ended March 31, 2012. The decrease was primarily due to a decrease of \$53.7 million, or 58.9%, in the average balance of other interest-earning assets to \$37.5 million for the three months ended March 31, 2013 from \$91.2 million for the three months ended March 31, 2012. The decrease was also due to a decrease of 2 basis points in the average yield on other interest-earning assets to 0.03% for the three months ended March 31, 2013 from 0.05% for the three months ended March 31, 2012.

The decrease in the average balance of other interest-earning assets was due to decreases in cash and cash equivalents and certificates of deposits at other financial institutions. The decline in the yield was due to the maturity of higher yielding certificates of deposits at other financial institutions.

Total interest expense decreased by \$346,000, or 29.4%, to \$829,000 for the three months ended March 31, 2013 from \$1.2 million for the three months ended March 31, 2012. Interest expense on deposits decreased by \$304,000, or 29.5%, to \$728,000 for the three months ended March 31, 2013 from \$1.0 million for the three months ended March 31, 2012. The decrease in the interest expense on deposits was a result of our decision to reduce our interest rates offered on our deposits in order to improve our net interest spread and net interest margin to increase profitability. This resulted in a decrease of 20 basis points in the average interest cost of deposits to 0.99% for the three months ended March 31, 2013 from 1.19% for the three months ended March 31, 2012.

The decrease in interest expense on deposits was also due to a decrease of \$54.5 million, or 15.7%, in the average balance of interest-bearing deposits to \$293.1 million for the three months ended March 31, 2013 from \$347.6 million for the three months ended March 31, 2012. The decrease in the average balance of interest-bearing deposits was due to decreases in the average balance of our interest-bearing demand deposits and interest-bearing savings and club accounts, offset by increases in the average balance of our interest-bearing certificates of deposits. The decrease in the average balances of our interest-bearing demand deposits and interest-bearing savings and club accounts was due to the Company's decision to reduce our interest rates offered on our deposits. The increase in the average balance of our interest-bearing certificates of deposit was due to the opening of two new branches in Framingham and Quincy, Massachusetts during 2012.

The interest expense of our interest-bearing demand deposits decreased by \$201,000, or 80.1%, to \$50,000 for the three months ended March 31, 2013 from \$251,000 for the three months ended March 31, 2012. The decrease in interest expense in our interest-bearing demand deposits was due to our decision to reduce our interest rates in interest-bearing demand deposits that resulted in a 52 basis point decrease in the average interest cost to 0.32% for the three months ended March 31, 2013 from 0.84% for the three months ended March 31, 2012. The decrease in interest expense on our interest-bearing demand deposits was also due to a decrease of \$57.5 million, or 48.2%, in the average balance of our interest-bearing demand deposits to \$61.9 million for the three months ended March 31, 2013 from \$119.3 million for the three months ended March 31, 2012.

The interest expense of our interest-bearing savings and club deposits decreased by \$89,000, or 45.0%, to \$109,000 for the three months ended March 31, 2013 from \$198,000 for the three months ended March 31, 2012. The decrease in interest expense in our interest-bearing savings and club deposits resulted from our decision to reduce our interest rates in interest-bearing savings and club deposits that resulted in a 38 basis point decrease in the average interest cost to 0.52% for the three months ended March 31, 2013 from 0.90% for the three months ended March 31, 2012. The decrease in interest expense on our interest-bearing savings and club deposits was also due to a decrease of \$4.3 million, or 5.0%, in the average balance of our interest-bearing savings and club deposits to \$83.2 million for the three months ended March 31, 2013 from \$87.5 million for the three months ended March 31, 2012.

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The interest expense of our interest-bearing certificates of deposit decreased by \$14,000, or 2.4%, to \$569,000 for the three months ended March 31, 2013 from \$583,000 for the three months ended March 31, 2012. The decrease in interest expense in our interest-bearing certificates of deposit was due to the re-pricing of interest-bearing certificates of deposit to lower interest rates upon maturity and our decision to reduce our interest rates in interest-bearing certificates of deposits. This resulted in a 12 basis point decrease in the average interest cost to 1.54% for the three months ended March 31, 2013 from 1.66% for the three months ended March 31, 2012. The decrease in interest expense on our interest-bearing certificates of deposit was offset by an increase of \$7.3 million, or 5.2%, in the average balance of our interest-bearing certificates of deposit to \$148.0 million for the three months ended March 31, 2013 from \$140.7 million for the three months ended March 31, 2012. The increase in the average balance of our interest-bearing certificates of deposit was due to the opening of two new branches in Framingham and Quincy, Massachusetts during 2012.

Interest expense on borrowings decreased by \$42,000, or 29.4%, to \$101,000 for the three months ended March 31, 2013 from \$143,000 for the three months ended March 31, 2012. The decrease was primarily due to a decrease of \$7.8 million, or 41.0%, in the average balance of borrowed money to \$11.3 million for the three months ended March 31, 2013 from \$19.1 million for the three months ended March 31, 2012, offset by an increase of 59 basis points in the average interest cost to 3.58% for the three months ended March 31, 2013 from 2.99% for the three months ended March 31, 2012. The increase in the average interest cost was due to the maturity and repayment of lower cost FHLB advances.

**Provision for Loan Losses.** The following table summarizes the activity in the allowance for loan losses and provision for loan losses for the three months ended March 31, 2013 and 2012.

|   | Three Months<br>Ended March 31,<br>2013      2012<br>(Dollars in thousands) |          |
|---|---|----------|
| Allowance at beginning of period  | \$ 4,646  | \$ 7,397 |
| Provision for loan losses   | 60  | —        |
| Charge-offs   | —   | (316 )   |
| Recoveries  | —   | 5        |
| Net charge-offs   | —   | (311 )   |
| Allowance at end of period  | \$ 4,706  | \$ 7,086 |
| Allowance to nonperforming loans  | 59.51 %   | 36.72 %  |
| Allowance to total loans outstanding at the end of the period               | 1.35 %  | 1.97 %   |
| Net charge-offs (recoveries) to average loans outstanding during the period | 0.00 %  | 0.09 %   |

The allowance to nonperforming loans ratio increased to 59.51% at March 31, 2013 from 36.72% at March 31, 2012 due primarily to a decrease in nonperforming loans to \$7.9 million in March 31, 2013 from \$19.3 million at March 31, 2012. The decrease in nonperforming loans was due to the identification, monitoring and resolution of several nonperforming loans that were paid-off and/or charge off between March 31, 2012 and March 31, 2013.



The allowance for loan losses was \$4.7 million at March 31, 2013, \$4.6 million at December 31, 2012, and \$7.1 million at March 31, 2012. We recorded a provision for loan losses of \$60,000 for the three-month period ended March 31, 2013 compared to no provision for loan losses for the three-month period ended March 31, 2012 due to an increase in the loan portfolio of \$10.2 million, or 3.0%, to \$343.9 million at March 31, 2013 from \$333.8 million at December 31, 2012, offset by an increase of \$4.2 million, or 20.3%, to \$24.9 million at March 31, 2013 from \$20.7 million at December 31, 2012 in loans that were individually evaluated for impairment. We did not record any provision for loan losses for the March 31, 2012 quarter due to a decrease of \$1.1 million, or 5.6%, in non-performing loans to \$19.3 million as of March 31, 2012 from \$20.4 million as of December 31, 2011.

We recorded no charge-offs during the three months ended March 31, 2013 compared to charge-offs of \$316,000 against two non-performing multi-family mortgage loan and one performing construction mortgage loan during the three months ended March 31, 2012. We recorded no recoveries during the three months ended March 31, 2013 compared to recoveries of \$5,000 during the three months ended March 31, 2012.

***Non-interest Income.*** Non-interest income increased by \$30,000, or 5.7%, to \$558,000 for the three months ended March 31, 2013 from \$528,000 for the three months ended March 31, 2012. The increase was due to increases of \$30,000 in other loan fees and service charges, \$15,000 in earnings on bank owned life insurance, and \$2,000 in other non-interest income, offset by a decrease of \$29,000 in investment advisory fee income.

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**Non-interest Expenses.** Non-interest expenses increased by \$113,000, or 2.8%, to \$4.19 million for the three months ended March 31, 2013 from \$4.08 million for the three months ended March 31, 2012. The increase resulted primarily from increases of \$195,000 in salaries and employee benefits, \$105,000 in occupancy expense, \$81,000 in real estate owned expenses, \$41,000 in outside data processing expense, and \$35,000 in equipment expense, which were partially offset by decreases of \$234,000 in other non-interest expense, \$63,000 in FDIC insurance expense, and \$47,000 in advertising expense.

Salaries and employee benefits, which represent 56.0% of the Company's non-interest expense, increased by \$195,000, or 9.1%, to \$2.3 million in 2013 from \$2.1 million in 2012 due to the hiring of additional branch operations personnel for the two new branch offices in Framingham and Quincy, Massachusetts, partially offset by a reduction in staff in various departments. In this regard, the Company has taken measures to control the increase in salaries and employee benefits by reducing staff in various departments, including the mortgage brokerage department and branch operations, during the first quarter of 2013. As a result, the number of full time equivalent employees decreased to 104 at March 31, 2013 from 113 at March 31, 2012. The Company expects the reduction in salaries and employee benefits will begin to be realized in the second quarter in 2013.

Due to the addition of two new branch offices in 2012, occupancy expense increased by \$105,000, or 36.3%, to \$394,000 in 2013 from \$289,000 in 2012 and equipment expenses increased by \$35,000, or 24.0%, to \$181,000 in 2013 from \$146,000 in 2012.

Outside data processing expense increased by \$41,000, or 17.4% to \$276,000 in 2013 from \$235,000 in 2012 due to the addition of two new branch offices in 2012 and additional services provided by the Company's core data processing vendor.

Real estate owned expenses increased by \$81,000, or 1,620.0% to \$86,000 in 2013 from \$5,000 in 2012 due to the addition of two foreclosed properties in 2012.

FDIC insurance expense decreased by \$63,000, or 67.7%, to \$30,000 in 2013 from \$93,000 in 2012 due to an adjustment to agree to the FDIC prepaid assessment amount as well as a decrease in the assessment base.

Advertising expense decreased by \$47,000, or 82.5%, to \$10,000 in 2013 from \$57,000 in 2012 due to an effort to reduce costs.

Other non-interest expense decreased by \$234,000, or 21.2%, to \$868,000 in 2013 from \$1.1 million in 2012 due mainly to decreases of \$146,000 in directors, officers and employee expenses, \$93,000 in recruitment expenses related

to the hiring of personnel, \$25,000 in consulting fees, \$19,000 in donations, \$18,000 in regulatory assessments, and \$9,000 in postage expenses. These decreases were partially offset by increases of \$30,000 in audit and accounting fees, \$29,000 in directors compensation, and \$11,000 in telephone expenses.

**Income Taxes.** Income tax expense decreased by \$47,000, or 71.2%, to \$19,000 for the three months ended March 31, 2013 from \$66,000 for the three months ended March 31, 2012. The decrease resulted primarily from a \$92,000 decrease in pre-tax income in 2013 compared to 2012. The effective tax rate was 8.4% for the three months ended March 31, 2013 and 20.8% for the three months ended March 31, 2012. The decrease in the effective tax rate between periods was due to a higher percentage of our pre-tax income being tax-exempt, specifically the earnings on bank-owned life insurance.

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The following table provides information with respect to our non-performing assets at the dates indicated.

|  | At<br>March<br>31, 2013 | At<br>December 31, 2012 |      |   |
|--|-------------------------|-------------------------|------|---|
|  | (Dollars in thousands)  |                         |      |   |
| Non-accrual loans  | \$ 7,908                | \$ 3,957                |      |   |
| Loans past due 90 days or more and accruing                                  | —                       | —                       |      |   |
| Total nonaccrual and 90 days or more past due loans                          | 7,908                   | 3,957                   |      |   |
| Other non-performing loans   | —                       | —                       |      |   |
| Total non-performing loans   | 7,908                   | 3,957                   |      |   |
| Real estate owned  | 4,271                   | 4,271                   |      |   |
| Total non-performing assets  | 12,179                  | 8,228                   |      |   |
| <br>   |                         |                         |      |   |
| Accruing troubled debt restructurings  | 12,264                  | 12,236                  |      |   |
| Nonaccrual troubled debt restructurings                                      | 1,226                   | 1,197                   |      |   |
| Total troubled debt restructurings   | 13,490                  | 13,433                  |      |   |
| Less nonaccrual troubled debt restructurings in total nonaccrual loans       | 1,226                   | 1,197                   |      |   |
| <br>   |                         |                         |      |   |
| Total troubled debt restructurings and non-performing assets                 | \$ 24,443               | \$ 20,464               |      |   |
| <br>   |                         |                         |      |   |
| Total non-performing loans to total loans                                    | 2.27                    | %                       | 1.17 | % |
| Total non-performing loans to total assets                                   | 1.85                    | %                       | 1.85 | % |
| Total non-performing assets and troubled debt restructurings to total assets | 5.70                    | %                       | 4.61 | % |

The non-accrual loans at March 31, 2013 consisted of thirteen loans in the aggregate – six multi-family mortgage loans, one mixed-use mortgage loan, and six non-residential mortgage loans.

Non-performing loans increased by \$3.9 million, or 99.8%, to \$7.9 million at March 31, 2013 from \$4.0 million at December 31, 2012. The increase in non-performing loans was due to the addition of seven mortgage loans totaling \$4.6 million that became non-performing at March 31, 2013, offset by the satisfaction of two non-accrual mortgage loans totaling \$196,000 and the conversion from non-performing to performing status of one mortgage loan totaling \$505,000.

The non-accrual multi-family mortgage loans totalled \$2.7 million at March 31, 2013, consisting primarily of the following mortgage loans:

A non-performing loan with an outstanding balance of \$1.1 million secured by an apartment building. We classified this loan as special mention. The non-performance was the result of a lawsuit filed by the previous owner (1) claiming that the debtor never owned record title to the mortgaged property. The Company filed a lawsuit seeking a declaration that the mortgage is a valid encumbrance against the property. The Court ruled in favor of the borrower and turned the building back to our borrower and dismissed the trustee.

A delinquent loan with an outstanding balance of \$942,000 secured by an apartment building. We classified this loan as substandard. The borrower refused to pay a prepayment penalty called for in the note and stopped making (2) the scheduled monthly payments. The Company defaulted the borrower, instituted a foreclosure action and obtained the appointment of a receiver of rents. Subsequent to March 31, 2013 the borrower, upon advice of counsel, brought the loan current and has agreed to pay the required prepayment penalty.

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The non-accrual mixed-use mortgage loan totalled \$312,000 at March 31, 2013, consisting of the following mortgage loan:

A delinquent loan with an outstanding balance of \$312,000 secured by a mixed-use building. We classified this loan as substandard. The Company had commenced a foreclosure action, but subsequent to March 31<sup>st</sup> the (1) borrower requested the Company consider a forbearance or restructure agreement to allow the borrower time to repair and re-rent vacant units and evict non-paying tenants. The Company has completed a restructure agreement and the borrower has made all required payments under the agreement to bring the loan current.

The six non-accrual non-residential mortgage loans, net of charge-offs of \$901,000, totaled \$5.2 million at March 31, 2013 consisting primarily of the following mortgage loans:

An outstanding balance of \$2.0 million secured by a multi-tenant office building. We classified this loan as substandard. The borrower is experiencing vacancy issues and has requested that the Company grant some form (1) of forbearance to assist with the cash flow problem the building is currently experiencing. Subsequent to March 31, 2013, the Company began negotiating a restructure agreement and currently expects to complete the agreement in the near future.

An outstanding balance of \$804,000, net of a charge-off of \$130,000, secured by a medical office building. We (2) classified this loan as substandard. The Company has commenced a foreclosure action and the Court has appointed a receiver. We are evaluating the options currently available to us.

An outstanding balance of \$789,000, net of a charge-off of \$371,000, secured by a gasoline service station and car (3) wash. We classified this loan as substandard. The Company has commenced a foreclosure action. We are evaluating the options currently available to us.

An outstanding balance of \$593,000 secured by a medical office building. We classified this loan as substandard. The Company had commenced a foreclosure action, but subsequent to March 31, 2013 the borrower requested the (4) Company consider a forbearance or restructure agreement to allow the borrower time to repair and re-rent vacant units and evict non-paying tenants. The Company has completed a restructure agreement and the borrower has made all required payments under the agreement to bring the loan current.

An outstanding balance of \$579,000 secured by an office building. We classified this loan as substandard. The Company had commenced a foreclosure action, but subsequent to March 31, 2013 the borrower requested the (5) Company consider a forbearance or restructure agreement to allow the borrower time to repair and re-rent vacant units and evict non-paying tenants. The Company has completed a restructure agreement and the borrower has made all required payments under the agreement to bring the loan current.

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(6) An outstanding balance of \$437,000, net of charge-offs of \$400,000, secured by a strip shopping center and warehouse. We classified this loan as substandard. The property was severely damaged by fire and the Company and borrower are currently suing the insurance company and the borrower's insurance agent as part of the Company's collection efforts. The borrower is making monthly escrow payments.

Based on a current fair value analysis of these properties, the Company does not anticipate any losses beyond the amounts already charged off.

At March 31, 2013, we owned two foreclosed properties with a net balance of \$4.3 million consisting of an office building located in New Jersey and a restaurant with 23 boat slips located in New York. The restaurant was destroyed by Hurricane Sandy and the Company has submitted a claim to the insurance agency and insurance company that underwrote the flood insurance. We have a contract of sale for the restaurant/marina property and have begun marketing the New Jersey office building.

Table of Contents**TROUBLED DEBT RESTRUCTURED LOANS**

There were no loans modified during the three months ended March 31, 2013 or March 31, 2012.

As of March 31, 2013 and 2012, none of the loans that were modified during the previous twelve months had defaulted in the three month periods ended March 31, 2013 and 2012.

The following tables show the activity in troubled debt restructured loans for the period indicated:

|                              | Residential<br>Real Estate | Nonresidential<br>Real Estate | Construction | Commercial<br>and<br>Industrial | Consumer | Total      |
|------------------------------|----------------------------|-------------------------------|--------------|---------------------------------|----------|------------|
| Balance at December 31, 2012 | \$ 6,444                   | \$ 6,989                      | \$           | — \$                            | — \$     | — \$13,433 |
| Additions                    | —                          | 66                            |              | —                               | —        | — 66       |
| Repayments                   | (9                         | ) —                           |              | —                               | —        | — (9 )     |
| Balance - March 31, 2013     | \$ 6,435                   | \$ 7,055                      | \$           | — \$                            | — \$     | — \$13,490 |
| Related allowance            | \$ —                       | \$ —                          | \$           | — \$                            | — \$     | — \$—      |

There were no charge offs of loans classified as troubled debt restructurings in the three months ended March 31, 2013.

Additions for the period consist of real estate taxes and similar items paid to protect the collateral position of the Company.

The following tables show the activity in troubled debt restructured loans for the period indicated:

|                              | Residential<br>Real Estate | Nonresidential<br>Real Estate | Construction | Commercial<br>and<br>Industrial | Consumer | Total      |
|------------------------------|----------------------------|-------------------------------|--------------|---------------------------------|----------|------------|
| Balance at December 31, 2011 | \$ 9,886                   | \$ 5,587                      | \$           | — \$                            | — \$     | — \$15,473 |
| Additions                    | 63                         | 49                            |              | —                               | —        | — 112      |
| Repayments                   | —                          | —                             |              | —                               | —        | — —        |
| Balance - March 31, 2012     | \$ 9,949                   | \$ 5,636                      | \$           | — \$                            | — \$     | — \$15,585 |



|                   |        |        |    |      |      |         |
|-------------------|--------|--------|----|------|------|---------|
| Related allowance | \$ 489 | \$ 231 | \$ | — \$ | — \$ | — \$720 |
|-------------------|--------|--------|----|------|------|---------|

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There were no charge offs of loans classified as troubled debt restructurings in the three months ended March 31, 2012.

Additions for the period consist of real estate taxes and similar items paid to protect the collateral position of the Company.

**Liquidity Management.** Liquidity is the ability to meet current and future financial obligations of a short-term nature. Our primary sources of funds consist of deposit inflows, loan repayments, maturities and sales of securities, and borrowings from the Federal Home Loan Bank of New York. While maturities and scheduled amortization of loans and securities are predictable sources of funds, deposit flows and loan prepayments are greatly influenced by general interest rates, economic conditions and competition.

We regularly adjust our investments in liquid assets based upon our assessment of: (1) expected loan demands; (2) expected deposit flows; (3) yields available on interest-earning deposits and securities; and (4) the objectives of our asset/liability management policy.

Our most liquid assets are cash and cash equivalents. The levels of these assets depend on our operating, financing, lending, and investing activities during any given period. Cash and cash equivalents totaled \$25.0 million at March 31, 2013 and consist primarily of interest-bearing deposits at other financial institutions and miscellaneous cash items. The Company can also borrow an additional \$62.1 million from the FHLB of New York to provide additional liquidity.

At March 31, 2013, we had \$38.6 million in loan commitments outstanding, consisting of \$21.3 million in unused commercial and industrial loan lines of credit, \$6.1 million in unused real estate equity lines of credit, \$6.0 million of real estate loan commitments, \$3.9 million in unused loans in process, \$1.2 million of commercial and industrial loan commitments, and \$136,000 in consumer lines of credit. Certificates of deposit due within one year of March 31, 2013 totaled \$66.0 million. This represented 44.5% of certificates of deposit at March 31, 2013. We believe a large percentage of certificates of deposit that mature within one year reflects customers' hesitancy to invest their funds for long periods in the current interest rate environment. If these maturing deposits do not remain with us, we will be required to seek other sources of funds, including other certificates of deposit and borrowings. Depending on market conditions, we may be required to pay higher rates on such deposits or other borrowings than we paid on the certificates of deposit due on or before March 31, 2013. We believe, however, based on past experience, a significant portion of our certificates of deposit will remain with us. We have the ability to attract and retain deposits by adjusting the interest rates offered.

Our primary investing activities are the origination of loans and the purchase of securities. Our primary financing activities consist of deposit accounts and FHLB advances. At March 31, 2013, we had the ability to borrow \$62.1

million, net of \$5.0 million in outstanding advances, from the FHLB of New York. At March 31, 2013, we had no overnight advances outstanding. Deposit flows are affected by the overall level of interest rates, the interest rates and products offered by us and our local competitors and other factors. We generally manage the pricing of our deposits to be competitive and to maintain or increase our core deposit relationships depending on our level of real estate loan commitments outstanding. Occasionally, we offer promotional rates on certain deposit products to attract deposits or to lengthen repricing time frames.

The Company is a separate legal entity from the Bank and must provide for its own liquidity. In addition to its operating expenses, the Company is responsible for paying any dividends declared to its shareholders and for the repurchase, if any, of its shares of common stock. At March 31, 2013, the Company had liquid assets of \$14.2 million.

**Capital Management.** The Bank is subject to various regulatory capital requirements administered by the FDIC, including a risk-based capital measure. 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. At March 31, 2013, the Bank exceeded all regulatory capital requirements. The Bank is considered “well capitalized” under regulatory guidelines.

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**Off-Balance Sheet Arrangements.** In the normal course of operations, we engage in a variety of financial transactions that, in accordance with U.S. generally accepted accounting principles, are not recorded in our financial statements. These transactions involve, to varying degrees, elements of credit, interest rate and liquidity risk. Such transactions are used primarily to manage customers' requests for funding and take the form of loan commitments, letters of credit and lines of credit.

For the three months ended March 31, 2013 and the year ended December 31, 2012, we engaged in no off-balance sheet transactions reasonably likely to have a material effect on our financial condition, results of operations or cash flows.

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

**Qualitative Aspects of Market Risk.** The Company's most significant form of market risk is interest rate risk. We manage the interest rate sensitivity of our interest-bearing liabilities and interest-earning assets in an effort to minimize the adverse effects of changes in the interest rate environment. Deposit accounts typically react more quickly to changes in market interest rates than mortgage loans because of the shorter maturities of deposits. As a result, sharp increases in interest rates may adversely affect our earnings while decreases in interest rates may beneficially affect our earnings. To reduce the potential volatility of our earnings, we have sought to improve the match between asset and liability maturities and rates, while maintaining an acceptable interest rate spread.

Our strategy for managing interest rate risk emphasizes: originating mortgage real estate loans that re-price to market interest rates in three to five years; purchasing securities that typically re-price within a three year time frame to limit exposure to market fluctuations; and, where appropriate, offering higher rates on long term certificates of deposit to lengthen the re-pricing time frame of our liabilities. We currently do not participate in hedging programs, interest rate swaps or other activities involving the use of derivative financial instruments.

We have an Asset/Liability Committee, comprised of our Chief Executive Officer, Chief Operating Officer, Chief Financial Officer, Chief Retail Banking Officer, Chief Lending Officer – New England Region, Chief Lending Officer – Mid-Atlantic Region, and Treasurer, whose function is to communicate, coordinate and control all aspects involving asset/liability management. The committee establishes and monitors the volume, maturities, pricing and mix of assets and funding sources with the objective of managing assets and funding sources to provide results that are consistent with liquidity, growth, risk limits and profitability goals.

Our goal is to manage asset and liability positions to moderate the effects of interest rate fluctuations on net interest income and net income.

**Quantitative Aspects of Market Risk.** We use an interest rate sensitivity analysis prepared an independent third party to review our level of interest rate risk. This analysis measures interest rate risk by computing changes in the net portfolio value of our cash flows from assets, liabilities and off-balance sheet items in the event of a range of assumed changes in market interest rates. Net portfolio value represents the market value of portfolio equity and is equal to the market value of assets minus the market value of liabilities, with adjustments made for off-balance sheet items. These analyses assess the risk of loss in market risk-sensitive instruments in the event of a sudden and sustained 100 to 500 basis point increase or 100 basis point decrease in market interest rates with no effect given to any steps that we might take to counter the effect of that interest rate movement.

The following table presents the change in our net portfolio value at March 31, 2013 that would occur in the event of an immediate change in interest rates based on the independent third party assumptions, with no effect given to any steps that we might take to counteract that change.

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| Basis Point (“bp”)<br>Change in Rates | Net Portfolio Value<br>(Dollars in thousands) |              |             | Net Portfolio Value<br>as % of<br>Portfolio Value of Assets |   |          |
|---------------------------------------|---|--------------|-------------|---|---|----------|
|                                       | \$<br>Amount                                  | \$<br>Change | %<br>Change | NPV<br>Ratio  | % | Change   |
| 500                                   | \$102,107                                     | (19,830)     | (16.3)%     | 25.33   | % | (194 )bp |
| 400                                   | 105,660                                       | (16,277)     | (13.3)      | 25.69   | % | (158 )bp |
| 300                                   | 108,591                                       | (13,346)     | (10.9)      | 25.91   | % | (136 )bp |
| 200                                   | 113,400                                       | (8,537 )     | (7.0 )      | 26.50   | % | (77 )bp  |
| 100                                   | 118,028                                       | (3,909 )     | (3.2 )      | 26.98   | % | (29 )bp  |
| 0                                     | 121,937                                       |              |             | 27.27   | % |          |
| (100)                                 | 124,030                                       | 2,093        | 1.7         | 27.36   | % | 9 bp     |

We use various assumptions in assessing interest rate risk. These assumptions relate to interest rates, loan prepayment rates, deposit decay rates and the market values of certain assets under differing interest rate scenarios, among others. As with any method of measuring interest rate risk, certain shortcomings are inherent in the methods of analyses presented in the foregoing tables. For example, although certain assets and liabilities may have similar maturities or periods to re-pricing, they may react in different degrees to changes in market interest rates. Also, the interest rates on certain types of assets and liabilities may fluctuate in advance of changes in market interest rates, while interest rates on other types may lag behind changes in market rates.

Additionally, certain assets, such as adjustable-rate mortgage loans, have features that restrict changes in interest rates on a short-term basis and over the life of the asset. Further, in the event of a change in interest rates, expected rates of prepayments on loans and early withdrawals from certificates could deviate significantly from those assumed in calculating the table. Prepayment rates can have a significant impact on interest income. Because of the large percentage of loans we hold, rising or falling interest rates have a significant impact on the prepayment speeds of our earning assets that in turn affect the rate sensitivity position. When interest rates rise, prepayments tend to slow. When interest rates fall, prepayments tend to rise. Our asset sensitivity would be reduced if prepayments slow and vice versa. While we believe these assumptions to be reasonable, there can be no assurance that assumed prepayment rates will approximate actual future loan repayment activity.

**Item 4. Controls and Procedures**

The Company’s management, including the Company’s principal executive officer and principal financial officer, have evaluated the effectiveness of the Company’s “disclosure controls and procedures,” as such term is defined in Rule 13a-15(e) promulgated under the Securities Exchange Act of 1934, as amended, (the “Exchange Act”). Based upon their evaluation, the principal executive officer and principal financial officer concluded that, as of the end of the period covered by this report, the Company’s disclosure controls and procedures were effective for the purpose of ensuring that the information required to be disclosed in the reports that the Company files or submits under the Exchange Act with the Securities and Exchange Commission (the “SEC”) (1) is recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms, and (2) is accumulated and communicated to the Company’s management, including its principal executive and principal financial officers, as appropriate to allow timely decisions

regarding required disclosure.

There were no changes in the Company's internal control over financial reporting during the three months ended March 31, 2013 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

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**PART II. OTHER INFORMATION**

**Item 1. Legal Proceedings**

On October 31, 2011 a complaint was filed by Stilwell Value Partners IV, L.P. in the Supreme Court of New York, New York County (the “Court”), against the Company, the MHC and each of the directors of the Company and the MHC. The complaint alleged that the directors had breached their fiduciary duties by not expanding the Company board to allow for disinterested consideration of a “second-step” conversion of the MHC. As relief, the complaint requested, among other things, that the Company’s board of directors be increased by at least three new members, that such new members be given sole responsibility to determine whether the Company should engage in a second-step conversion and that the Court order the Company to engage in a second-step conversion. A motion to dismiss the Complaint was filed on December 14, 2011. On September 27, 2012, the Court granted the Company’s motion to dismiss and dismissed the complaint granting Stilwell leave to file an amended complaint within 20 days. On December 14, 2012 Stilwell filed an amended complaint, alleging that the directors had breached their fiduciary duties by not voting to authorize a second step conversion. Stilwell asserted claims against the MHC, as majority shareholder of the Company, for breach of fiduciary duty and for aiding and abetting the directors’ alleged breach of fiduciary duty. The Company, filed a motion to dismiss on February 1, 2013. Stilwell filed his opposition on March 8, 2013, and the Company filed its reply brief on March 29, 2013. It is anticipated that the Court will rule on the motion in the next several months.

The Company and Bank are also subject to claims and litigation that arise primarily in the ordinary course of business. Based on information presently available and advice received from legal counsel representing the Company and Bank in connection with such claims and litigation, it is the opinion of management that the disposition or ultimate determination of such claims and litigation will not have a material adverse effect on the consolidated financial position, results of operations or liquidity of the Company.

**Item 1A. Risk Factors**

In addition to the other information set forth in this report, you should carefully consider the factors discussed in Part I, “Item 1A. Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2012, which could materially affect our business, financial condition or future results. The risks described in our Annual Report on Form 10-K are not the only risks that we face. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially affect our business, financial condition and/or operating results.

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

None

**Item 3. Defaults Upon Senior Securities**



Not applicable

**Item 4. Mine Safety Disclosures**

Not applicable

**Item 5. Other Information**

None

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**Item 6. Exhibits**

- 31.1 CEO certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 CFO certification pursuant to Section 302 of the Sarbanes Oxley Act of 2002.
- 32.1 CEO and CFO certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

The following materials from the Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 2013, formatted in XBRL (Extensible Business Reporting Language): (i) the Consolidated Statements of Financial Condition, (ii) the Consolidated Statements of Income, (iii) the Consolidated Statements of Comprehensive Income, (iv) the Consolidated Statements of Stockholders' Equity, (v) the Consolidated Statements of Cash Flows and (vi) the Notes to the Consolidated Financial Statements.

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\* Furnished, not filed.

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**Signatures**

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

Northeast Community Bancorp, Inc.

Date: May 15, 2013 By: /s/ Kenneth A. Martinek  
Kenneth A. Martinek  
Chief Executive Officer

Date: May 15, 2013 By: /s/ Salvatore Randazzo  
Salvatore Randazzo  
Executive Vice President and Chief Financial Officer

