First Bancorp, Inc /ME/
Form 10-Q
August 09, 2013

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-Q

[X] Quarterly Report Pursuant to Section 13 or 15(d) of The Securities Exchange Act of 1934
For the quarterly period ended June 30, 2013

Commission File Number 0-26589

THE FIRST BANCORP, INC.
(Exact name of Registrant as specified in its charter)

MAINE	01-0404322
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
MAIN STREET, DAMARISCOTTA, MAINE	04543
(Address of principal executive offices)	(Zip code)

(207) 563-3195
Registrant's telephone number, including area code

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.
Yes [X] No[_]

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every,Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).
Yes [X] No[_]

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):
Large accelerated filer [_] Accelerated filer [X] Non-accelerated filer [_]

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

Indicate the number of shares outstanding of each of the registrant's classes of common stock as of August 1, 2013
Common Stock: 10,663,193 shares

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Part I. Financial Information

Selected Financial Data (Unaudited)
The First Bancorp, Inc. and Subsidiary

Dollars in thousands,	As of and for the six months ended June 30,		For the quarters ended June 30,	
except for per share amounts	2013	2012	2013	2012
Summary of Operations				
Interest Income	$24,514	$26,239	$12,249	$13,133
Interest Expense	6,240	6,515	3,138	3,215
Net Interest Income	18,274	19,724	9,111	9,918
Provision for Loan Losses	2,700	4,900	1,200	2,800
Non-Interest Income	6,867	6,064	3,579	3,896
Non-Interest Expense	14,812	12,908	7,423	6,730
Net Income	6,098	6,236	3,242	3,323
Per Common Share Data				
Basic Earnings per Share	$0.56	$0.60	$0.29	$0.32
Diluted Earnings per Share	0.56	0.60	0.29	0.32
Cash Dividends Declared	0.390	0.390	0.195	0.195
Book Value per Common Share	13.69	14.32	13.69	14.32
Tangible Book Value per Common Share[2]	10.82	11.51	10.82	11.51
Market Value	17.48	17.00	17.48	17.00
Financial Ratios				
Return on Average Equity[1]	8.18 %	8.84 %	8.38 %	9.38 %
Return on Average Tangible Common Equity[1,2]	9.70 %	10.35 %	9.93 %	11.01 %
Return on Average Assets[1]	0.87 %	0.88 %	0.92 %	0.93 %
Average Equity to Average Assets	11.18 %	10.84 %	11.23 %	10.73 %
Average Tangible Equity to Average Assets[2]	9.01 %	8.89 %	9.06 %	8.81 %
Net Interest Margin Tax-Equivalent[1,2]	3.04 %	3.19 %	3.02 %	3.16 %
Dividend Payout Ratio	69.64 %	65.00 %	67.24 %	60.94 %
Allowance for Loan Losses/Total Loans	1.46 %	1.63 %	1.46 %	1.63 %
Non-Performing Loans to Total Loans	2.25 %	2.49 %	2.25 %	2.49 %
Non-Performing Assets to Total Assets	1.75 %	1.91 %	1.75 %	1.91 %
Efficiency Ratio[2]	57.26 %	50.74 %	57.90 %	51.06 %
At Period End				
Total Assets	$1,444,496	$1,424,757	$1,444,496	$1,424,757
Total Loans	866,071	881,814	866,071	881,814
Total Investment Securities	478,911	457,570	478,911	457,570
Total Deposits	1,027,682	1,005,274	1,027,682	1,005,274
Total Shareholders' Equity	145,972	153,405	145,972	153,405

[1]Annualized using a 365-day basis in 2013 and 366-day basis in 2012

[2]These ratios use non-GAAP financial measures. See Management's Discussion and Analysis of Financial Condition and Results of Operations for additional disclosures and information.

Item 1 – Financial Statements

Report of Independent Registered Public Accounting Firm

The Board of Directors and Shareholders
The First Bancorp, Inc.

We have reviewed the accompanying interim consolidated financial information of The First Bancorp, Inc. and Subsidiary as of June 30, 2013 and 2012 and for the three-month and six-month periods then ended. These financial statements are the responsibility of the Company's management.

We conducted our reviews in accordance with standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures to financial data and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit in accordance with standards of the Public Company Accounting Oversight Board (United States), the objective of which is to express an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our reviews, we are not aware of any material modifications that should be made to the accompanying interim consolidated financial statements for them to be in conformity with accounting principles generally accepted in the United States of America.

/s/ Berry Dunn McNeil & Parker, LLC

Portland, Maine
August 9, 2013

Consolidated Balance Sheets (Unaudited)
The First Bancorp, Inc. and Subsidiary

	June 30, 2013	December 31, 2012	June 30, 2012
Assets			
Cash and cash equivalents	$18,683,000	$14,958,000	$14,192,000
Interest bearing deposits in other banks	334,000	1,638,000	—
Securities available for sale	287,735,000	291,614,000	307,347,000
Securities to be held to maturity (fair value of $174,790,000 at June 30, 2013, $150,247,000 at December 31, 2012 and $143,628,000 at June 30, 2012)	177,264,000	143,320,000	135,775,000
Restricted equity securities, at cost	13,912,000	14,448,000	14,448,000
Loans held for sale	1,047,000	1,035,000	378,000
Loans	866,071,000	869,284,000	881,814,000
Less allowance for loan losses	12,670,000	12,500,000	14,384,000
Net loans	853,401,000	856,784,000	867,430,000
Accrued interest receivable	6,443,000	4,912,000	6,024,000
Premises and equipment, net	23,913,000	22,988,000	18,500,000
Other real estate owned	5,826,000	7,593,000	5,188,000
Goodwill	29,805,000	29,805,000	27,684,000
Other assets	26,133,000	25,904,000	27,791,000
Total assets	$1,444,496,000	$1,414,999,000	$1,424,757,000
Liabilities			
Demand deposits	$88,540,000	$90,252,000	$77,019,000
NOW deposits	139,022,000	147,309,000	123,897,000
Money market deposits	87,993,000	80,983,000	71,009,000
Savings deposits	142,718,000	135,250,000	119,471,000
Certificates of deposit	569,409,000	505,056,000	613,878,000
Total deposits	1,027,682,000	958,850,000	1,005,274,000
Borrowed funds – short term	116,956,000	142,750,000	118,767,000
Borrowed funds – long term	140,152,000	140,155,000	130,159,000
Other liabilities	13,734,000	16,921,000	17,152,000
Total liabilities	1,298,524,000	1,258,676,000	1,271,352,000
Shareholders' equity			
Preferred stock, $1,000 preference value per share	—	12,402,000	12,352,000
Common stock, one cent par value per share	106,000	98,000	98,000
Additional paid-in capital	58,066,000	46,314,000	46,110,000
Retained earnings	91,348,000	89,692,000	87,396,000
Accumulated other comprehensive income (loss)			
Net unrealized gain (loss) on securities available for sale	(3,433,000)	7,940,000	7,526,000
Net unrealized loss on postretirement benefit costs	(115,000)	(123,000)	(77,000)
Total shareholders' equity	145,972,000	156,323,000	153,405,000
Total liabilities & shareholders' equity	$1,444,496,000	$1,414,999,000	$1,424,757,000
Common Stock			
Number of shares authorized	18,000,000	18,000,000	18,000,000
Number of shares issued and outstanding	10,659,764	9,859,914	9,847,159
Book value per common share	$13.69	$14.60	$14.32
Tangible book value per common share	$10.82	$11.47	$11.51

See Report of Independent Registered Public Accounting Firm.

The accompanying notes are an integral part of these consolidated financial statements.

Consolidated Statements of Income and Comprehensive Income/(Loss) (Unaudited)
The First Bancorp, Inc. and Subsidiary

	For the six months ended June 30,		For the quarters ended June 30,	
	2013	2012	2013	2012
Interest income				
Interest and fees on loans	$17,530,000	$18,759,000	$8,738,000	$9,367,000
Interest on deposits with other banks	4,000	1,000	2,000	1,000
Interest and dividends on investments	6,980,000	7,479,000	3,509,000	3,765,000
Total interest income	24,514,000	26,239,000	12,249,000	13,133,000
Interest expense				
Interest on deposits	4,012,000	4,297,000	2,025,000	2,104,000
Interest on borrowed funds	2,228,000	2,218,000	1,113,000	1,111,000
Total interest expense	6,240,000	6,515,000	3,138,000	3,215,000
Net interest income	18,274,000	19,724,000	9,111,000	9,918,000
Provision for loan losses	2,700,000	4,900,000	1,200,000	2,800,000
Net interest income after provision for loan losses	15,574,000	14,824,000	7,911,000	7,118,000
Non-interest income				
Investment management and fiduciary income	968,000	844,000	519,000	448,000
Service charges on deposit accounts	1,423,000	1,351,000	775,000	713,000
Net securities gains	1,087,000	1,967,000	788,000	1,444,000
Mortgage origination and servicing income, net of amortization	1,387,000	304,000	491,000	460,000
Other operating income	2,002,000	1,598,000	1,006,000	831,000
Total non-interest income	6,867,000	6,064,000	3,579,000	3,896,000
Non-interest expense				
Salaries and employee benefits	6,994,000	6,202,000	3,520,000	3,118,000
Occupancy expense	1,069,000	819,000	522,000	405,000
Furniture and equipment expense	1,310,000	1,123,000	688,000	550,000
FDIC insurance premiums	584,000	606,000	294,000	305,000
Amortization of identified intangibles	163,000	141,000	81,000	70,000
Other operating expense	4,692,000	4,017,000	2,318,000	2,282,000
Total non-interest expense	14,812,000	12,908,000	7,423,000	6,730,000
Income before income taxes	7,629,000	7,980,000	4,067,000	4,284,000
Income tax expense	1,531,000	1,744,000	825,000	961,000
NET INCOME	$6,098,000	$6,236,000	$3,242,000	$3,323,000
Basic earnings per common share	$0.56	$0.60	$0.29	$0.32
Diluted earnings per common share	$0.56	$0.60	$0.29	$0.32
Other comprehensive income (loss), net of tax				
Net unrealized gain (loss) on securities available for sale	(11,373,000)	125,000	(8,907,000)	438,000
Amortization of unrecognized postretirement benefits	8,000	10,000	4,000	5,000
Other comprehensive income (loss)	(11,365,000)	135,000	(8,903,000)	443,000
Comprehensive income (loss)	$(5,267,000)	$6,371,000	$(5,661,000)	$3,766,000

See Report of Independent Registered Public Accounting Firm.
The accompanying notes are an integral part of these consolidated financial statements.

Consolidated Statements of Changes in Shareholders' Equity (Unaudited)
The First Bancorp, Inc. and Subsidiary

	Preferred stock	Common stock and additional paid-in capital Shares	Common stock and additional paid-in capital Amount	Retained earnings	Accumulated other comprehensive income (loss)	Total shareholders' equity
Balance at December 31, 2011	$12,303,000	9,812,180	$45,927,000	$85,314,000	$7,314,000	$150,858,000
Net income	—	—	—	6,236,000	—	6,236,000
Net unrealized gain on securities available for sale, net of tax	—	—	—	—	125,000	125,000
Amortization of unrecognized postretirement benefits, net of tax	—	—	—	—	10,000	10,000
Comprehensive income	—	—	—	6,236,000	135,000	6,371,000
Cash dividends declared ($0.195 per share)	—	—	—	(4,154,000)	—	(4,154,000)
Equity compensation expense	—	—	40,000	—	—	40,000
Amortization of premium for preferred stock issuance	49,000	—	(49,000)	—	—	—
Proceeds from sale of common stock	—	34,979	290,000	—	—	290,000
Balance at June 30, 2012	$12,352,000	9,847,159	$46,208,000	$87,396,000	$7,449,000	$153,405,000
Balance at December 31, 2012	$12,402,000	9,859,914	$46,412,000	$89,692,000	$7,817,000	$156,323,000
Net income	—	—	—	6,098,000	—	6,098,000
Net unrealized loss on securities available for sale, net of tax	—	—	—	—	(11,373,000)	(11,373,000)
Amortization of unrecognized postretirement benefits, net of tax	—	—	—	—	8,000	8,000
Comprehensive loss	—	—	—	6,098,000	(11,365,000)	(5,267,000)
Cash dividends declared ($0.195 per share)	—	—	—	(4,442,000)	—	(4,442,000)
Equity compensation expense	—	—	107,000	—	—	107,000
Amortization of premium for preferred stock issuance	98,000	—	(98,000)	—	—	—
Payment to repurchase preferred stock	(12,500,000)	—	—	—	—	(12,500,000)
	—	799,850	11,751,000	—	—	11,751,000

Proceeds from sale of common stock						
Balance at June 30, 2013	—	10,659,764	$58,172,000	$91,348,000	$(3,548,000)	$145,972,000

See Report of Independent Registered Public Accounting Firm.

The accompanying notes are an integral part of these consolidated financial statements.

Consolidated Statements of Cash Flows (Unaudited)
The First Bancorp, Inc. and Subsidiary

	For the six months ended	
	June 30, 2013	June 30, 2012
Cash flows from operating activities		
Net income	$6,098,000	$6,236,000
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation	838,000	663,000
Change in deferred taxes	(13,000)	(688,000)
Provision for loan losses	2,700,000	4,900,000
Loans originated for resale	(34,725,000)	(12,535,000)
Proceeds from sales and transfers of loans	35,549,000	12,720,000
Net gain on sales of loans	(836,000)	(369,000)
Net gain on sale or call of securities	(1,087,000)	(1,967,000)
Net amortization of premiums on investments	1,152,000	1,482,000
Net loss on sale of other real estate owned	24,000	39,000
Provision for losses on other real estate owned	332,000	198,000
Equity compensation expense	107,000	40,000
Net increase in other assets and accrued interest	(125,000)	(1,831,000)
Net increase in other liabilities	900,000	2,243,000
Net loss on disposal of premises and equipment	4,000	—
Amortization of investment in limited partnership	260,000	238,000
Net acquisition amortization	163,000	103,000
Net cash provided by operating activities	11,341,000	11,472,000
Cash flows from investing activities		
Decrease in interest-bearing deposits in other banks	1,304,000	—
Proceeds from sales of securities available for sale	10,563,000	25,137,000
Proceeds from maturities, payments and calls of securities available for sale	35,593,000	26,024,000
Proceeds from maturities, payments and calls of securities to be held to maturity	28,818,000	21,871,000
Proceeds from sales of other real estate owned	2,062,000	667,000
Purchases of securities available for sale	(59,873,000)	(71,706,000)
Purchases of securities to be held to maturity	(62,728,000)	(35,101,000)
Redemption of restricted equity securities	536,000	995,000
Net (increase) decrease in loans	32,000	(22,340,000)
Capital expenditures	(1,767,000)	(321,000)
Net cash used in investing activities	(45,460,000)	(54,774,000)
Cash flows from financing activities		
Net increase (decrease) in demand, savings, and money market accounts	4,479,000	(761,000)
Net increase in certificates of deposit	64,353,000	64,734,000
Net decrease in short-term borrowings	(25,797,000)	(16,730,000)
Repurchase of preferred stock	(12,500,000)	—
Proceeds from sale of common stock	11,751,000	290,000
Dividends paid	(4,442,000)	(4,154,000)
Net cash provided by financing activities	37,844,000	43,379,000
Net increase in cash and cash equivalents	3,725,000	77,000
Cash and cash equivalents at beginning of period	14,958,000	14,115,000

Cash and cash equivalents at end of period	$18,683,000	$14,192,000
Interest paid	$6,368,000	$6,640,000
Income taxes paid	950,000	869,000
Non-cash transactions		
Net transfer from loans to other real estate owned	$651,000	$1,998,000

See Report of Independent Registered Public Accounting Firm.

Notes to Consolidated Financial Statements
The First Bancorp, Inc. and Subsidiary

Note 1 – Basis of Presentation
The First Bancorp, Inc. (the Company) is a financial holding company that owns all of the common stock of The First, N.A. (the Bank). The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of Management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. All significant intercompany transactions and balances are eliminated in consolidation. The income reported for the 2013 period is not necessarily indicative of the results that may be expected for the year ending December 31, 2013. For further information, refer to the consolidated financial statements and notes included in the Company's annual report on Form 10-K for the year ended December 31, 2012.
Subsequent Events
Events occurring subsequent to June 30, 2013, have been evaluated as to their potential impact to the financial statements.

Note 2 – Investment Securities
The following table summarizes the amortized cost and estimated fair value of investment securities at June 30, 2013:

	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value (Estimated)
Securities available for sale				
Mortgage-backed securities	$157,023,000	$2,014,000	$(1,513,000)	$157,524,000
State and political subdivisions	134,376,000	1,955,000	(7,792,000)	128,539,000
Other equity securities	1,617,000	63,000	(8,000)	1,672,000
	$293,016,000	$4,032,000	$(9,313,000)	$287,735,000
Securities to be held to maturity				
U.S. Government-sponsored agencies	$92,179,000	$10,000	$(5,944,000)	$86,245,000
Mortgage-backed securities	42,389,000	1,883,000	(625,000)	43,647,000
State and political subdivisions	42,396,000	2,268,000	(66,000)	44,598,000
Corporate securities	300,000	—	—	300,000
	$177,264,000	$4,161,000	$(6,635,000)	$174,790,000
Restricted equity securities				
Federal Home Loan Bank Stock	$12,875,000	$—	$—	$12,875,000
Federal Reserve Bank Stock	1,037,000	—	—	1,037,000
	$13,912,000	$—	$—	$13,912,000

The following table summarizes the amortized cost and estimated fair value of investment securities at December 31, 2012:

	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value (Estimated)
Securities available for sale				
Mortgage-backed securities	$164,752,000	$4,636,000	$(295,000)	$169,093,000
State and political subdivisions	113,069,000	8,074,000	(199,000)	120,944,000
Other equity securities	1,578,000	43,000	(44,000)	1,577,000
	$279,399,000	$12,753,000	$(538,000)	$291,614,000
Securities to be held to maturity				
U.S. Government-sponsored agencies	$60,919,000	$242,000	$(182,000)	$60,979,000
Mortgage-backed securities	39,193,000	2,850,000	(19,000)	42,024,000
State and political subdivisions	42,908,000	4,036,000	—	46,944,000
Corporate securities	300,000	—	—	300,000
	$143,320,000	$7,128,000	$(201,000)	$150,247,000
Restricted equity securities				
Federal Home Loan Bank Stock	$13,412,000	$—	$—	$13,412,000
Federal Reserve Bank Stock	1,036,000	—	—	1,036,000
	$14,448,000	$—	$—	$14,448,000

The following table summarizes the amortized cost and estimated fair value of investment securities at June 30, 2012:

	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value (Estimated)
Securities available for sale				
Mortgage-backed securities	$201,552,000	$5,677,000	$(250,000)	$206,979,000
State and political subdivisions	92,353,000	6,291,000	(51,000)	98,593,000
Other equity securities	1,863,000	47,000	(135,000)	1,775,000
	$295,768,000	$12,015,000	$(436,000)	$307,347,000
Securities to be held to maturity				
U.S. Government-sponsored agencies	$41,197,000	$282,000	$(33,000)	$41,446,000
Mortgage-backed securities	49,992,000	3,524,000	(8,000)	53,508,000
State and political subdivisions	44,286,000	4,088,000	—	48,374,000
Corporate securities	300,000	—	—	300,000
	$135,775,000	$7,894,000	$(41,000)	$143,628,000
Restricted equity securities				
Federal Home Loan Bank Stock	$13,412,000	$—	$—	$13,412,000
Federal Reserve Bank Stock	1,036,000	—	—	1,036,000
	$14,448,000	$—	$—	$14,448,000

The following table summarizes the contractual maturities of investment securities at June 30, 2013:

	Securities available for sale		Securities to be held to maturity	
	Amortized Cost	Fair Value (Estimated)	Amortized Cost	Fair Value (Estimated)
Due in 1 year or less	$1,345,000	$1,368,000	$766,000	$773,000
Due in 1 to 5 years	139,000	140,000	6,081,000	6,462,000
Due in 5 to 10 years	2,426,000	2,563,000	24,873,000	26,299,000
Due after 10 years	287,489,000	281,992,000	145,544,000	141,256,000
Equity securities	1,617,000	1,672,000	—	—
	$293,016,000	$287,735,000	$177,264,000	$174,790,000

The following table summarizes the contractual maturities of investment securities at December 31, 2012:

	Securities available for sale		Securities to be held to maturity	
	Amortized Cost	Fair Value (Estimated)	Amortized Cost	Fair Value (Estimated)
Due in 1 year or less	$18,761,000	$18,926,000	$3,754,000	$3,785,000
Due in 1 to 5 years	27,243,000	27,816,000	11,950,000	12,701,000
Due in 5 to 10 years	16,686,000	17,666,000	27,461,000	29,986,000
Due after 10 years	215,131,000	225,629,000	100,155,000	103,775,000
Equity securities	1,578,000	1,577,000	—	—
	$279,399,000	$291,614,000	$143,320,000	$150,247,000

The following table summarizes the contractual maturities of investment securities at June 30, 2012:

	Securities available for sale		Securities to be held to maturity	
	Amortized Cost	Fair Value (Estimated)	Amortized Cost	Fair Value (Estimated)
Due in 1 year or less	$4,296,000	$4,328,000	$1,382,000	$1,399,000
Due in 1 to 5 years	55,317,000	56,358,000	13,556,000	14,134,000
Due in 5 to 10 years	23,143,000	24,034,000	21,137,000	22,958,000
Due after 10 years	211,149,000	220,852,000	99,700,000	105,137,000
Equity securities	1,863,000	1,775,000	—	—
	$295,768,000	$307,347,000	$135,775,000	$143,628,000

At June 30, 2013, securities with a fair value of $123,571,000 were pledged to secure public deposits, repurchase agreements, and for other purposes as required by law. This compares to securities with a fair value of $154,817,000 as of December 31, 2012 and $140,384,000 at June 30, 2012, pledged for the same purposes.

Gains and losses on the sale of securities available for sale are computed by subtracting the amortized cost at the time of sale from the security's selling price, net of accrued interest to be received. The following table shows securities gains and losses for the six months and quarters ended June 30, 2013 and 2012:

	For the six months ended June 30,		For the quarters ended June 30,	
	2013	2012	2013	2012
Proceeds from sales of securities	$10,563,000	$25,137,000	$5,598,000	$14,194,000
Gross realized gains	1,087,000	2,256,000	788,000	1,444,000
Gross realized losses	—	(289,000)	—	—
Net gain	$1,087,000	$1,967,000	$788,000	$1,444,000
Related income taxes	$380,000	$688,000	$275,000	$505,000

Management reviews securities with unrealized losses for other than temporary impairment. As of June 30, 2013, there were 280 securities with unrealized losses held in the Company's portfolio. These securities were temporarily impaired as a result of changes in interest rates reducing their fair value, of which six had been temporarily impaired for 12 months or more. At the present time, there have been no material changes in the credit quality of these securities resulting in other than temporary impairment, and in Management's opinion, no additional write-down for other-than-temporary impairment is warranted. Information regarding securities temporarily impaired as of June 30, 2013 is summarized below:

	Less than 12 months		12 months or more		Total	
	Fair Value (Estimated)	Unrealized Losses	Fair Value (Estimated)	Unrealized Losses	Fair Value (Estimated)	Unrealized Losses
U.S. Government-sponsored agencies	$85,453,000	$(5,944,000)	$—	$—	$85,453,000	$(5,944,000)
Mortgage-backed securities	58,706,000	(2,039,000)	1,585,000	(99,000)	60,291,000	(2,138,000)
State and political subdivisions	71,738,000	(7,858,000)	—	—	71,738,000	(7,858,000)
Other equity securities	—	—	110,000	(8,000)	110,000	(8,000)
	$215,897,000	$(15,841,000)	$1,695,000	$(107,000)	$217,592,000	$(15,948,000)

As of December 31, 2012, there were 42 securities with unrealized losses held in the Company's portfolio. These securities were temporarily impaired as a result of changes in interest rates reducing their fair value, of which seven had been temporarily impaired for 12 months or more. Information regarding securities temporarily impaired as of December 31, 2012 is summarized below:

	Less than 12 months		12 months or more		Total	
	Fair Value (Estimated)	Unrealized Losses	Fair Value (Estimated)	Unrealized Losses	Fair Value (Estimated)	Unrealized Losses
U.S. Government-sponsored agencies	$15,817,000	$(182,000)	$—	$—	$15,817,000	$(182,000)
Mortgage-backed securities	9,982,000	(231,000)	2,534,000	(83,000)	12,516,000	(314,000)
State and political subdivisions	8,621,000	(199,000)	—	—	8,621,000	(199,000)

Other equity securities	—	—	222,000	(44,000)	222,000	(44,000)
	$34,420,000	$(612,000)	$2,756,000	$(127,000)	$37,176,000	$(739,000)

As of June 30, 2012, there were 30 securities with unrealized losses held in the Company's portfolio. These securities were temporarily impaired as a result of changes in interest rates reducing their fair value, of which eight had been temporarily impaired for 12 months or more. Information regarding securities temporarily impaired as of June 30, 2012 is summarized below:

	Less than 12 months		12 months or more		Total	
	Fair Value (Estimated)	Unrealized Losses	Fair Value (Estimated)	Unrealized Losses	Fair Value (Estimated)	Unrealized Losses
U.S. Government-sponsored agencies	$7,942,000	$(33,000)	$—	$—	$7,942,000	$(33,000)
Mortgage-backed securities	9,822,000	(110,000)	5,137,000	(148,000)	14,959,000	(258,000)
State and political subdivisions	3,719,000	(51,000)	—	—	3,719,000	(51,000)
Other equity securities	—	—	191,000	(135,000)	191,000	(135,000)
	$21,483,000	$(194,000)	$5,328,000	$(283,000)	$26,811,000	$(477,000)

The Bank is a member of the Federal Home Loan Bank ("FHLB") of Boston, a cooperatively owned wholesale bank for housing and finance in the six New England States. As a requirement of membership in the FHLB, the Bank must own a minimum required amount of FHLB stock, calculated periodically based primarily on its level of borrowings from the FHLB. The Bank uses the FHLB for much of its wholesale funding needs. As of June 30, 2013 and 2012, and December 31, 2012, the Bank's investment in FHLB stock totaled $12,875,000, $13,412,000 and $13,412,000, respectively. FHLB stock is a non-marketable equity security and therefore is reported at cost, which equals par value.

Note 3 – Loans

The following table shows the composition of the Company's loan portfolio as of June 30, 2013 and 2012 and at December 31, 2012:

	June 30, 2013		December 31, 2012		June 30, 2012	
Commercial						
Real estate	$251,799,000	29.1 %	$251,335,000	28.9 %	$253,193,000	28.7 %
Construction	18,641,000	2.2 %	22,417,000	2.6 %	33,072,000	3.8 %
Other	91,393,000	10.6 %	81,183,000	9.3 %	87,833,000	10.0 %
Municipal	14,885,000	1.7 %	14,704,000	1.7 %	16,089,000	1.8 %
Residential						
Term	374,522,000	43.2 %	379,447,000	43.7 %	368,876,000	41.8 %
Construction	4,759,000	0.5 %	6,459,000	0.7 %	6,449,000	0.7 %
Home equity line of credit	95,013,000	11.0 %	99,082,000	11.4 %	100,689,000	11.4 %
Consumer	15,059,000	1.7 %	14,657,000	1.7 %	15,613,000	1.8 %
Total	$866,071,000	100.0 %	$869,284,000	100.0 %	$881,814,000	100.0 %

Loan balances include net deferred loan costs of $2,001,000 as of June 30, 2013, $1,783,000 as of December 31, 2012, and $1,664,000 as of June 30, 2012. Pursuant to collateral agreements, qualifying first mortgage loans, which totaled $254,417,000 at June 30, 2013, $256,378,000 at December 31, 2012, and $243,196,000 at June 30, 2012, were used to collateralize borrowings from the Federal Home Loan Bank of Boston. In addition, commercial, construction and home equity loans totaling $221,953,000 at June 30, 2013, $220,520,000 at December 31, 2012, and $232,598,000 at June 30, 2012, were used to collateralize a standby line of credit at the Federal Reserve Bank of Boston that is currently unused.

For all loan classes, loans over 30 days past due are considered delinquent. Information on the past-due status of loans by class of financing receivable as of June 30, 2013, is presented in the following table:

	30-59 Days Past Due	60-89 Days Past Due	90+ Days Past Due	All Past Due	Current	Total	90+ Days & Accruing
Commercial							
Real estate	$717,000	$—	$2,347,000	$3,064,000	$248,735,000	$251,799,000	$—
Construction	—	—	456,000	456,000	18,185,000	18,641,000	—
Other	244,000	3,482,000	2,547,000	6,273,000	85,120,000	91,393,000	503,000
Municipal	—	—	—	—	14,885,000	14,885,000	—
Residential							
Term	636,000	3,955,000	7,933,000	12,524,000	361,998,000	374,522,000	395,000
Construction	82,000	—	—	82,000	4,677,000	4,759,000	—
Home equity line of credit	652,000	62,000	816,000	1,530,000	93,483,000	95,013,000	—
Consumer	104,000	63,000	121,000	288,000	14,771,000	15,059,000	121,000
Total	$2,435,000	$7,562,000	$14,220,000	$24,217,000	$841,854,000	$866,071,000	$1,019,000

Information on the past-due status of loans by class of financing receivable as of December 31, 2012, is presented in the following table:

	30-59 Days Past Due	60-89 Days Past Due	90+ Days Past Due	All Past Due	Current	Total	90+ Days & Accruing
Commercial							
Real estate	$2,172,000	$346,000	$2,380,000	$4,898,000	$246,437,000	$251,335,000	$102,000
Construction	—	29,000	35,000	64,000	22,353,000	22,417,000	—
Other	658,000	218,000	2,306,000	3,182,000	78,001,000	81,183,000	2,000
Municipal	136,000	—	—	136,000	14,568,000	14,704,000	—
Residential							
Term	2,404,000	1,082,000	9,298,000	12,784,000	366,663,000	379,447,000	363,000
Construction	188,000	—	—	188,000	6,271,000	6,459,000	—
Home equity line of credit	430,000	133,000	1,136,000	1,699,000	97,383,000	99,082,000	539,000
Consumer	101,000	70,000	45,000	216,000	14,441,000	14,657,000	45,000
Total	$6,089,000	$1,878,000	$15,200,000	$23,167,000	$846,117,000	$869,284,000	$1,051,000

Information on the past-due status of loans by class of financing receivable as of June 30, 2012, is presented in the following table:

	30-59 Days Past Due	60-89 Days Past Due	90+ Days Past Due	All Past Due	Current	Total	90+ Days & Accruing
Commercial							
Real estate	$—	$13,000	$1,858,000	$1,871,000	$251,322,000	$253,193,000	$—
Construction	119,000	—	34,000	153,000	32,919,000	33,072,000	—
Other	177,000	266,000	1,398,000	1,841,000	85,992,000	87,833,000	—
Municipal	1,560,000	—	—	1,560,000	14,529,000	16,089,000	—
Residential							
Term	2,191,000	1,000,000	7,878,000	11,069,000	357,807,000	368,876,000	—
Construction	—	—	1,336,000	1,336,000	5,113,000	6,449,000	—
Home equity line of credit	530,000	—	1,311,000	1,841,000	98,848,000	100,689,000	—
Consumer	140,000	49,000	180,000	369,000	15,244,000	15,613,000	164,000
Total	$4,717,000	1,328,000	$13,995,000	$20,040,000	$861,774,000	$881,814,000	$164,000

For all classes, loans are placed on non-accrual status when, based on current information and events, it is probable that the Company will be unable to collect all amounts due according to the contractual terms of the loan agreement or when principal and interest is 90 days or more past due unless the loan is both well secured and in the process of collection (in which case the loan may continue to accrue interest in spite of its past due status). A loan is "well secured" if it is secured (1) by collateral in the form of liens on or pledges of real or personal property, including securities, that have a realizable value sufficient to discharge the debt (including accrued interest) in full, or (2) by the guarantee of a financially responsible party. A loan is "in the process of collection" if collection of the loan is proceeding in due course either (1) through legal action, including judgment enforcement procedures, or, (2) in appropriate circumstances, through collection efforts not involving legal action which are reasonably expected to result in repayment of the debt or in its restoration to a current status in the near future.

Cash payments received on non-accrual loans, which are included in impaired loans, are applied to reduce the loan's principal balance until the remaining principal balance is deemed collectible, after which interest is recognized when collected. As a general rule, a loan may be restored to accrual status when payments are current for a substantial period of time, generally six months, and repayment of the remaining contractual amounts is expected or when it otherwise becomes well secured and in the process of collection. Information on nonaccrual loans as of June 30, 2013 and 2012 and at December 31, 2012 is presented in the following table:

	June 30, 2013	December 31, 2012	June 30, 2012
Commercial			
Real estate	$4,424,000	$4,603,000	$5,545,000
Construction	519,000	101,000	521,000
Other	2,856,000	3,459,000	2,361,000
Municipal	—	—	—
Residential			
Term	10,640,000	10,333,000	10,723,000
Construction	—	—	1,336,000
Home equity line of credit	1,046,000	654,000	1,456,000
Consumer	—	—	16,000
Total	$19,485,000	$19,150,000	$21,958,000

Impaired loans include troubled debt restructured and loans placed on non-accrual. These loans are measured at the present value of expected future cash flows discounted at the loan's effective interest rate or at the fair value of the collateral if the loan is collateral dependent. If the measure of an impaired loan is lower than the recorded investment in the loan and estimated selling costs, a specific reserve is established for the difference.

A breakdown of impaired loans by class of financing receivable as of and for the period ended June 30, 2013, is presented in the following table:

	Recorded Investment	Unpaid Principal Balance	Related Allowance	For the six months ended June 30, 2013 Average Recorded Investment	For the six months ended June 30, 2013 Recognized Interest Income	For the quarter ended June 30, 2013 Average Recorded Investment	For the quarter ended June 30, 2013 Recognized Interest Income
With No Related Allowance							
Commercial							
Real estate	$11,452,000	$11,851,000	$—	$10,621,000	$200,000	$11,083,000	$99,000
Construction	517,000	1,065,000	—	210,000	28,000	376,000	27,000
Other	4,017,000	4,325,000	—	3,726,000	59,000	3,759,000	32,000
Municipal	—	—	—	—	—	—	—
Residential							
Term	15,399,000	17,441,000	—	13,862,000	248,000	14,636,000	150,000
Construction	—	—	—	—	—	—	—
Home equity line of credit	1,655,000	1,892,000	—	1,579,000	15,000	1,665,000	7,000
Consumer	—	—	—	—	—	—	—
	$33,040,000	$36,574,000	$—	$29,998,000	$550,000	$31,519,000	$315,000
With an Allowance Recorded							
Commercial							
Real estate	$5,880,000	$6,619,000	$1,510,000	$6,688,000	$110,000	$6,577,000	$48,000
Construction	1,302,000	1,302,000	266,000	2,297,000	19,000	1,626,000	(7,000)
Other	1,773,000	1,893,000	1,005,000	2,008,000	11,000	1,920,000	2,000
Municipal	—	—	—	—	—	—	—
Residential							
Term	4,296,000	4,520,000	218,000	5,961,000	93,000	5,117,000	29,000
Construction	—	—	—	—	—	—	—
Home equity line of credit	40,000	40,000	7,000	94,000	1,000	15,000	1,000
Consumer	—	—	—	—	—	—	—
	$13,291,000	$14,374,000	$3,006,000	$17,048,000	$234,000	$15,255,000	$73,000
Total							
Commercial							
Real estate	$17,332,000	$18,470,000	$1,510,000	$17,309,000	$310,000	$17,660,000	$147,000
Construction	1,819,000	2,367,000	266,000	2,507,000	47,000	2,002,000	20,000
Other	5,790,000	6,218,000	1,005,000	5,735,000	70,000	5,679,000	34,000
Municipal	—	—	—	—	—	—	—
Residential							
Term	19,695,000	21,961,000	218,000	19,822,000	341,000	19,753,000	179,000
Construction	—	—	—	—	—	—	—
Home equity line of credit	1,695,000	1,932,000	7,000	1,673,000	16,000	1,680,000	8,000
Consumer	—	—	—	—	—	—	—
	$46,331,000	$50,948,000	$3,006,000	$47,046,000	$784,000	$46,774,000	$388,000

Substantially all interest income recognized on impaired loans for all classes of financing receivables was recognized on a cash basis as received.

A breakdown of impaired loans by class of financing receivable as of and for the year ended December 31, 2012, is presented in the following table:

	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Recognized Interest Income
With No Related Allowance					
Commercial					
Real estate	$9,386,000	$9,963,000	$—	$10,102,000	$199,000
Construction	101,000	115,000	—	2,533,000	—
Other	4,737,000	5,345,000	—	2,877,000	53,000
Municipal	—	—	—	—	—
Residential					
Term	12,747,000	14,440,000	—	9,801,000	189,000
Construction	—	—	—	560,000	—
Home equity line of credit	1,311,000	1,440,000	—	961,000	27,000
Consumer	—	—	—	3,000	—
	$28,282,000	$31,303,000	$—	$26,837,000	$468,000
With an Allowance Recorded					
Commercial					
Real estate	$6,388,000	$7,018,000	$1,523,000	$4,614,000	$211,000
Construction	3,253,000	3,253,000	969,000	1,816,000	85,000
Other	1,124,000	1,126,000	652,000	1,974,000	38,000
Municipal	—	—	—	—	—
Residential					
Term	6,697,000	6,842,000	395,000	9,066,000	237,000
Construction	—	—	—	261,000	—
Home equity line of credit	—	—	—	442,000	—
Consumer	—	—	—	9,000	—
	$17,462,000	$18,239,000	$3,539,000	$18,182,000	$571,000
Total					
Commercial					
Real estate	$15,774,000	$16,981,000	$1,523,000	$14,716,000	$410,000
Construction	3,354,000	3,368,000	969,000	4,349,000	85,000
Other	5,861,000	6,471,000	652,000	4,851,000	91,000
Municipal	—	—	—	—	—
Residential					
Term	19,444,000	21,282,000	395,000	18,867,000	426,000
Construction	—	—	—	821,000	—
Home equity line of credit	1,311,000	1,440,000	—	1,403,000	27,000
Consumer	—	—	—	12,000	—
	$45,744,000	$49,542,000	$3,539,000	$45,019,000	$1,039,000

A breakdown of impaired loans by class of financing receivable as of and for the period ended June 30, 2012, is presented in the following table:

	Recorded Investment	Unpaid Principal Balance	Related Allowance	For the six months ended June 30, 2012 Average Recorded Investment	For the six months ended June 30, 2012 Recognized Interest Income	For the quarter ended June 30, 2012 Average Recorded Investment	For the quarter ended June 30, 2012 Recognized Interest Income
With No Related Allowance							
Commercial							
Real estate	$10,313,000	$10,313,000	$—	$9,729,000	$111,000	$11,013,000	$71,000
Construction	1,464,000	1,464,000	—	2,189,000	26,000	1,395,000	13,000
Other	2,249,000	2,249,000	—	2,710,000	16,000	2,439,000	21,000
Municipal	—	—	—	—	—	—	—
Residential							
Term	8,695,000	8,695,000	—	9,662,000	71,000	9,322,000	41,000
Construction	1,002,000	1,002,000	—	880,000	—	1,042,000	—
Home equity line of credit	740,000	740,000	—	758,000	—	740,000	—
Consumer	—	—	—	6,000	—	—	—
	$24,463,000	$24,463,000	$—	$25,934,000	$224,000	$25,951,000	$146,000
With an Allowance Recorded							
Commercial							
Real estate	$3,482,000	$3,482,000	$1,133,000	$4,026,000	$16,000	$3,775,000	$6,000
Construction	2,155,000	2,155,000	787,000	1,376,000	37,000	2,155,000	37,000
Other	1,851,000	1,851,000	932,000	2,013,000	18,000	1,802,000	13,000
Municipal	—	—	—	—	—	—	—
Residential							
Term	10,357,000	10,357,000	966,000	8,487,000	127,000	9,525,000	68,000
Construction	334,000	334,000	48,000	466,000	—	334,000	—
Home equity line of credit	716,000	716,000	300,000	566,000	—	613,000	—
Consumer	16,000	16,000	11,000	15,000	—	15,000	—
	$18,911,000	$18,911,000	$4,177,000	$16,949,000	$198,000	$18,219,000	$124,000
Total							
Commercial							
Real estate	$13,795,000	$13,795,000	$1,133,000	$13,755,000	$127,000	$14,788,000	$77,000
Construction	3,619,000	3,619,000	787,000	3,565,000	63,000	3,550,000	50,000
Other	4,100,000	4,100,000	932,000	4,723,000	34,000	4,241,000	34,000
Municipal	—	—	—	—	—	—	—
Residential							
Term	19,052,000	19,052,000	966,000	18,149,000	198,000	18,847,000	109,000
Construction	1,336,000	1,336,000	48,000	1,346,000	—	1,376,000	—
Home equity line of credit	1,456,000	1,456,000	300,000	1,324,000	—	1,353,000	—
Consumer	16,000	16,000	11,000	21,000	—	15,000	—
	$43,374,000	$43,374,000	$4,177,000	$42,883,000	$422,000	$44,170,000	$270,000

Note 4. Allowance for Loan Losses

The Company provides for loan losses through the establishment of an allowance for loan losses which represents an estimated reserve for existing losses in the loan portfolio. A systematic methodology is used for determining the allowance that includes a quarterly review process, risk rating changes, and adjustments to the allowance. The loan portfolio is classified in eight classes and credit risk is evaluated separately in each class. The appropriate level of the allowance is evaluated continually based on a review of significant loans, with a particular emphasis on nonaccruing, past due, and other loans that may require special attention. Other factors include general conditions in local and national economies; loan portfolio composition and asset quality indicators; and internal factors such as changes in underwriting policies, credit administration practices, experience, ability and depth of lending management, among others. The allowance consists of four elements: (1) specific reserves for loans evaluated individually for impairment; (2) general reserves for each portfolio segment based on historical loan loss experience, (3) qualitative reserves judgmentally adjusted for local and national economic conditions, concentrations, portfolio composition, volume and severity of delinquencies and nonaccrual loans, trends of criticized and classified loans, changes in credit policies and underwriting standards, credit administration practices, and other factors as applicable for each portfolio segment; and (4) unallocated reserves. All outstanding loans are considered in evaluating the appropriateness of the allowance. A breakdown of the allowance for loan losses as of June 30, 2013, December 31, 2012, and June 30, 2012, by class of financing receivable and allowance element, is presented in the following tables:

As of June 30, 2013	Specific Reserves on Loans Evaluated Individually for Impairment	General Reserves on Loans Based on Historical Loss Experience	Reserves for Qualitative Factors	Unallocated Reserves	Total Reserves
Commercial					
Real estate	$1,510,000	$2,148,000	$2,153,000	$—	$5,811,000
Construction	266,000	162,000	163,000	—	591,000
Other	1,005,000	783,000	784,000	—	2,572,000
Municipal	—	—	18,000	—	18,000
Residential					
Term	218,000	380,000	428,000	—	1,026,000
Construction	—	4,000	5,000	—	9,000
Home equity line of credit	7,000	402,000	328,000	—	737,000
Consumer	—	408,000	223,000	—	631,000
Unallocated	—	—	—	1,275,000	1,275,000
	$3,006,000	$4,287,000	$4,102,000	$1,275,000	$12,670,000

As of December 31, 2012	Specific Reserves on Loans Evaluated Individually for Impairment	General Reserves on Loans Based on Historical Loss Experience	Reserves for Qualitative Factors	Unallocated Reserves	Total Reserves
Commercial					
Real estate	$1,523,000	$2,369,000	$1,973,000	$—	$5,865,000
Construction	969,000	213,000	177,000	—	1,359,000
Other	652,000	763,000	635,000	—	2,050,000
Municipal	—	—	18,000	—	18,000
Residential					
Term	395,000	278,000	436,000	—	1,109,000
Construction	—	4,000	7,000	—	11,000
Home equity line of credit	—	315,000	339,000	—	654,000
Consumer	—	362,000	230,000	—	592,000

Unallocated	—	—	—	842,000	842,000
	$3,539,000	$4,304,000	$3,815,000	$842,000	$12,500,000

As of June 30, 2012	Specific Reserves on Loans Evaluated Individually for Impairment	General Reserves on Loans Based on Historical Loss Experience	Reserves for Qualitative Factors	Unallocated Reserves	Total Reserves
Commercial					
Real estate	$1,133,000	$2,685,000	$1,746,000	$—	$5,564,000
Construction	787,000	355,000	231,000	—	1,373,000
Other	932,000	935,000	609,000	—	2,476,000
Municipal	—	—	19,000	—	19,000
Residential					
Term	966,000	165,000	456,000	—	1,587,000
Construction	48,000	2,000	8,000	—	58,000
Home equity line of credit	300,000	155,000	354,000	—	809,000
Consumer	11,000	351,000	241,000	—	603,000
Unallocated	—	—	—	1,895,000	1,895,000
	$4,177,000	$4,648,000	$3,664,000	$1,895,000	$14,384,000

Qualitative adjustment factors are taken into consideration when determining reserve estimates. These adjustment factors are based upon our evaluation of various current conditions, including those listed below.

- General economic conditions.
- Credit quality trends with emphasis on loan delinquencies, nonaccrual levels and classified loans.
- Recent loss experience in particular segments of the portfolio.
- Loan volumes and concentrations, including changes in mix.
- Other factors, including changes in quality of the loan origination; loan policy changes; changes in credit risk management processes; Bank regulatory and external loan review examination results.

The qualitative portion of the allowance for loan losses was 0.50% of related loans as of June 30, 2013, compared to 0.46% of related loans as of December 31, 2012. The qualitative portion increased $287,000 between December 31, 2012 and June 30, 2013 as a result of a higher level of pooled substandard commercial loans. Changes to qualitative adjustments for other major portfolio segments were not material in this period.

The unallocated portion of the allowance totaled $1,275,000 at June 30, 2013, or 10% of the total reserve. This compares to $842,000 as of December 31, 2012. The fluctuation in the unallocated component is supported by the following:

- Losses in the commercial loan portfolio have been influenced by classified levels and exacerbated by declines in real estate values, reflected in appraisal updates on collateral that secure troubled loans. Certain valuation declines have been more than expected. The unallocated portion allows some coverage for unexpected and specifically unidentified losses in pooled portfolios.
- An internal analysis completed on sales of other real estate owned found these properties sold, on average, approximately 20% below the appraised value of the property at the time of take in. Based on the analysis, Management applies a 20% additional discount factor to arrive at OREO take in amounts. This will impact the allowance as these potential additional write downs would be taken against the allowance, and the unallocated portion provides additional reserves for these adjustments.
- Watch-rated commercial loans have remained elevated after bottoming out in the third quarter of 2009. Additional losses may exist in this portfolio segment, yet are not identifiable at present. The unallocated portion provides some level of support for this.
- The present view of the economic recovery is one moving at a slow to moderate pace; consequently, caution remains appropriate at the evaluation date regarding the direction of the economy and its impact on Bank loan portfolio

quality. The spike in interest rates during the second quarter increases uncertainty in the existing loan portfolio and warrants an increase in the unallocated reserve over the six months ended June 30, 2013. Until conditions show consistent improvement, particularly with employment levels, and until the real estate markets return to some form of normalcy, losses may be higher than normal.

- The unallocated portion is also available to cover imprecision or uncertainties to incorporate the range of probable outcomes inherent in estimates used for the allowance, which may change from period to period.

Commercial loans are comprised of three major classes, commercial real estate loans, commercial construction loans and other commercial loans. Commercial real estate is primarily comprised of loans to small businesses collateralized by owner-occupied real estate, while other commercial is primarily comprised of loans to small businesses collateralized by plant and equipment, commercial fishing vessels and gear, and limited inventory-based lending. Commercial real estate loans typically have a maximum loan-to-value of 75% based upon current appraisal information at the time the loan is made. Municipal loans are comprised of loans to municipalities in Maine for capitalized expenditures, construction projects or tax-anticipation notes. All municipal loans are considered general obligations of the municipality and as such are collateralized by the taxing ability of the municipality for repayment of debt.

Construction loans, both commercial and residential, comprise a very small portion of the portfolio, and at 18.4% of capital are well under the regulatory guidance of 100.0% of capital at June 30, 2013. Construction loans and non-owner-occupied commercial real estate loans are at 74.1% of total capital, well under regulatory guidance of 300.0% of capital at June 30, 2013.

The process of establishing the allowance with respect to the commercial loan portfolio begins when a loan officer initially assigns each loan a risk rating, using established credit criteria. Approximately 50% of the outstanding loans and commitments are subject to review and validation annually by an independent consulting firm, as well as periodically by the Company's internal credit review function. The methodology employs Management's judgment as to the level of losses on existing loans based on internal review of the loan portfolio, including an analysis of a borrower's current financial position, and the consideration of current and anticipated economic conditions and their potential effects on specific borrowers and or lines of business. In determining the Company's ability to collect certain loans, Management also considers the fair value of underlying collateral. The risk rating system has eight levels, defined as follows:

1 Strong

Credits rated "1" are characterized by borrowers fully responsible for the credit with excellent capacity to pay principal and interest. Loans rated "1" may be secured with acceptable forms of liquid collateral.

2 Above Average

Credits rated "2" are characterized by borrowers that have better than average liquidity, capitalization, earnings and/or cash flow with a consistent record of solid financial performance.

3 Satisfactory

Credits rated "3" are characterized by borrowers with favorable liquidity, profitability and financial condition with adequate cash flow to pay debt service.

4 Average

Credits rated "4" are characterized by borrowers that present risk more than 1, 2 and 3 rated loans and merit an ordinary level of ongoing monitoring. Financial condition is on par or somewhat below industry averages while cash flow is generally adequate to meet debt service requirements.

5 Watch

Credits rated "5" are characterized by borrowers that warrant greater monitoring due to financial condition or unresolved and identified risk factors.

6 Other Assets Especially Mentioned (OAEM)

Loans in this category are currently protected but are potentially weak and constitute an undue and unwarranted credit risk, but not to the point of justifying a classification of substandard. OAEM have potential weaknesses which may, if not checked or corrected, weaken the asset or inadequately protect the Bank's credit position at some future date.

7 Substandard

Loans in this category are inadequately protected by the current sound worth and paying capacity of the borrower or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. Substandard loans are characterized by the distinct possibility that the Bank may sustain some loss if the deficiencies are not corrected.

8 Doubtful

Loans classified "Doubtful" have the same weaknesses as those classified substandard with the added characteristic that the weaknesses make collection or liquidation in full, based on currently existing facts, conditions, and values, highly questionable and improbable. The possibility of loss is high, but because of certain important and reasonably specific pending factors which may work to the advantage and strengthening of the asset, its classification as an estimated loss is deferred until its more exact status may be determined.

The following table summarizes the risk ratings for the Company's commercial real estate, commercial construction, commercial other, and municipal loans as of June 30, 2013:

	Commercial Real Estate	Commercial Construction	Commercial Other	Municipal Loans	All Risk-Rated Loans
1 Strong	$18,000	$—	$255,000	$1,590,000	$1,863,000
2 Above Average	12,914,000	569,000	6,135,000	7,775,000	27,393,000
3 Satisfactory	39,155,000	2,716,000	17,439,000	4,183,000	63,493,000
4 Average	102,063,000	10,963,000	33,117,000	1,337,000	147,480,000
5 Watch	39,466,000	42,000	15,716,000	—	55,224,000
6 OAEM	24,265,000	3,001,000	4,196,000	—	31,462,000
7 Substandard	33,503,000	1,350,000	14,535,000	—	49,388,000
8 Doubtful	415,000	—	—	—	415,000
Total	$251,799,000	$18,641,000	$91,393,000	$14,885,000	$376,718,000

The following table summarizes the risk ratings for the Company's commercial real estate, commercial construction, commercial other, and municipal loans as of December 31, 2012:

	Commercial Real Estate	Commercial Construction	Commercial Other	Municipal Loans	All Risk-Rated Loans
1 Strong	$19,000	$—	$271,000	$1,731,000	$2,021,000
2 Above Average	13,871,000	1,274,000	4,084,000	7,061,000	26,290,000
3 Satisfactory	34,454,000	2,312,000	14,578,000	3,487,000	54,831,000
4 Average	99,712,000	12,322,000	28,618,000	2,425,000	143,077,000
5 Watch	43,369,000	1,721,000	19,524,000	—	64,614,000
6 OAEM	26,302,000	79,000	5,300,000	—	31,681,000
7 Substandard	33,153,000	4,709,000	8,806,000	—	46,668,000
8 Doubtful	455,000	—	2,000	—	457,000
Total	$251,335,000	$22,417,000	$81,183,000	$14,704,000	$369,639,000

The following table summarizes the risk ratings for the Company's commercial real estate, commercial construction, commercial other, and municipal loans as of June 30, 2012:

	Commercial Real Estate	Commercial Construction	Commercial Other	Municipal Loans	All Risk-Rated Loans
1 Strong	$21,000	$—	$284,000	$1,822,000	$2,127,000
2 Above Average	19,319,000	170,000	4,601,000	7,933,000	32,023,000
3 Satisfactory	36,207,000	1,751,000	13,541,000	3,770,000	55,269,000
4 Average	99,855,000	20,932,000	32,700,000	2,564,000	156,051,000
5 Watch	41,089,000	1,969,000	21,147,000	—	64,205,000
6 OAEM	21,135,000	1,649,000	4,357,000	—	27,141,000
7 Substandard	34,931,000	6,601,000	11,111,000	—	52,643,000
8 Doubtful	636,000	—	92,000	—	728,000
Total	$253,193,000	$33,072,000	$87,833,000	$16,089,000	$390,187,000

Commercial loans are generally charged off when all or a portion of the principal amount is determined to be uncollectible. This determination is based on circumstances specific to a borrower including repayment ability, analysis of collateral and other factors as applicable.

Residential loans are comprised of two classes: term loans, which include traditional amortizing home mortgages, and construction loans, which include loans for owner-occupied residential construction. Residential loans typically have a 75% to 80% loan to value based upon current appraisal information at the time the loan is made. Home equity loans and lines of credit are typically written to the same underwriting standards. Consumer loans are primarily amortizing loans to individuals collateralized by automobiles, pleasure craft and recreation vehicles, typically with a maximum loan to value of 80% to 90% of the purchase price of the collateral. Consumer loans also include a small amount of unsecured short-term time notes to individuals.

Residential loans, consumer loans and home equity lines of credit are segregated into homogeneous pools with similar risk characteristics. Trends and current conditions are analyzed and historical loss experience is adjusted accordingly. Quantitative and qualitative adjustment factors for these segments are consistent with those for the commercial and municipal classes. Certain loans in the residential, home equity lines of credit and consumer classes identified as having the potential for further deterioration are analyzed individually to confirm impairment status, and to determine the need for a specific reserve; however there is no formal rating system used for these classes. Consumer loans greater than 120 days past due are generally charged off. Residential loans 90 days or more past due are placed on non-accrual status unless the loans are both well secured and in the process of collection. One- to four-family residential real estate loans and home equity loans are written down or charged-off no later than 180 days past due, or for residential real estate secured loans having a borrower in bankruptcy, within 60 days of receipt of notification of filing from the bankruptcy court, whichever is sooner. This is subject to completion of a current assessment of the value of the collateral with any outstanding loan balance in excess of the fair value of the property, less costs to sell, written down or charged-off.

There were no changes to the Company's accounting policies or methodology used to estimate the allowance for loan losses during the six months ended June 30, 2013.

The following table presents allowance for loan losses activity by class for the six-months and quarter ended June 30, 2013, and allowance for loan loss balances by class and related loan balances by class as of June 30, 2013:

	Commercial			Municipal	Residential		Home Equity Line of Credit	Consumer	Un
	Real Estate	Construction	Other		Term	Construction			
For the six months ended June 30, 2013									
Beginning balance	$5,865,000	$1,359,000	$2,050,000	$18,000	$1,109,000	$11,000	$654,000	$592,000	$84
Charge offs	61,000	930,000	521,000	—	607,000	—	431,000	252,000	—
Recoveries	—	—	144,000	—	36,000	—	2,000	90,000	—
Provision	7,000	162,000	899,000	—	488,000	(2,000)	512,000	201,000	43
Ending balance	$5,811,000	$591,000	$2,572,000	$18,000	$1,026,000	$9,000	$737,000	$631,000	$1,
For the three months ended June 30, 2013									
Beginning balance	$5,879,000	$1,064,000	$2,115,000	$18,000	$1,113,000	$9,000	$859,000	$574,000	$1,
Charge offs	7,000	527,000	233,000	—	407,000	—	69,000	125,000	—
Recoveries	—	—	41,000	—	34,000	—	1,000	42,000	—
Provision	(61,000)	54,000	649,000	—	286,000	—	(54,000)	140,000	18
Ending balance	$5,811,000	$591,000	$2,572,000	$18,000	$1,026,000	$9,000	$737,000	$631,000	$1,
Allowance for loan losses as of June 30, 2013									
Ending balance specifically evaluated for impairment	$1,510,000	$266,000	$1,005,000	$—	$218,000	$—	$7,000	$—	$—
Ending balance collectively evaluated for impairment	$4,301,000	$325,000	$1,567,000	$18,000	$808,000	$9,000	$730,000	$631,000	$1,
Related loan balances as of June 30, 2013									
Ending balance	$251,799,000	$18,641,000	$91,393,000	$14,885,000	$374,522,000	$4,759,000	$95,013,000	$15,059,000	$—
Ending balance specifically evaluated for impairment	$17,332,000	$1,819,000	$5,790,000	$—	$19,695,000	$—	$1,695,000	$—	$—
Ending balance collectively evaluated for	$234,467,000	$16,822,000	$85,603,000	$14,885,000	$354,827,000	$4,759,000	$93,318,000	$15,059,000	$—

impairment

The following table presents allowance for loan losses activity by class for the year-ended December 31, 2012 and allowance for loan loss balances by class and related loan balances by class as of December 31, 2012:

	Commercial			Municipal	Residential		Home Equity Line of Credit	Consumer	Unall
	Real Estate	Construction	Other		Term	Construction			
For the year ended December 31, 2012									
Beginning balance	$5,659,000	$658,000	$2,063,000	$19,000	$1,159,000	$255,000	$595,000	$584,000	$2,0(
Charge offs	1,394,000	928,000	3,215,000	—	1,911,000	389,000	688,000	555,000	—
Recoveries	13,000	246,000	113,000	—	110,000	54,000	1,000	208,000	—
Provision	1,587,000	1,383,000	3,089,000	(1,000)	1,751,000	91,000	746,000	355,000	(1,16
Ending balance	$5,865,000	$1,359,000	$2,050,000	$18,000	$1,109,000	$11,000	$654,000	$592,000	$842
Allowance for loan losses as of December 31, 2012									
Ending balance specifically evaluated for impairment	$1,523,000	$969,000	$652,000	$—	$395,000	$—	$—	$—	$—
Ending balance collectively evaluated for impairment	$4,342,000	$390,000	$1,398,000	$18,000	$714,000	$11,000	$654,000	$592,000	$842
Related loan balances as of December 31, 2012									
Ending balance	$251,335,000	$22,417,000	$81,183,000	$14,704,000	$379,447,000	$6,459,000	$99,082,000	$14,657,000	$—
Ending balance specifically evaluated for impairment	$15,774,000	$3,354,000	$5,861,000	$—	$19,444,000	$—	$1,311,000	$—	$—
Ending balance collectively evaluated for impairment	$235,561,000	$19,063,000	$75,322,000	$14,704,000	$360,003,000	$6,459,000	$97,771,000	$14,657,000	$—

The following table presents allowance for loan losses activity by class for the six-months and quarter ended June 30, 2012, and allowance for loan loss balances by class and related loan balances by class as of June 30, 2012:

	Commercial			Municipal	Residential		Home Equity Line of Credit	Consumer	Una
	Real Estate	Construction	Other		Term	Construction			
For the six months ended June 30, 2012									
Beginning balance	$5,659,000	$658,000	$2,063,000	$19,000	$1,159,000	$255,000	$595,000	$584,000	$2,0
Charge offs	915,000	—	2,162,000	—	375,000	118,000	49,000	276,000	—
Recoveries	1,000	246,000	11,000	—	2,000	—	—	119,000	—
Provision	819,000	469,000	2,564,000	—	801,000	(79,000)	263,000	176,000	(113
Ending balance	$5,564,000	$1,373,000	$2,476,000	$19,000	$1,587,000	$58,000	$809,000	$603,000	$1,8
For the three months ended June 30, 2012									
Beginning balance	$5,862,000	$704,000	$2,125,000	$19,000	$1,236,000	$59,000	$682,000	$568,000	$1,6
Charge offs	915,000	—	160,000	—	136,000	118,000	—	96,000	—
Recoveries	1,000	—	9,000	—	1,000	—	—	44,000	—
Provision	616,000	669,000	502,000	—	486,000	117,000	127,000	87,000	196
Ending balance	$5,564,000	$1,373,000	$2,476,000	$19,000	$1,587,000	$58,000	$809,000	$603,000	$1,8
Allowance for loan losses as of June 30, 2012									
Ending balance specifically evaluated for impairment	$1,133,000	$787,000	$932,000	$—	$966,000	$48,000	$300,000	$11,000	$—
Ending balance collectively evaluated for impairment	$4,431,000	$586,000	$1,544,000	$19,000	$621,000	$10,000	$509,000	$592,000	$1,8
Related loan balances as of June 30, 2012									
Ending balance	$253,193,000	$33,072,000	$87,833,000	$16,089,000	$368,876,000	$6,449,000	$100,689,000	$15,613,000	$—
Ending balance specifically evaluated for impairment	$13,795,000	$3,619,000	$4,100,000	$—	$19,052,000	$1,336,000	$1,456,000	$16,000	$—
Ending balance collectively evaluated for	$239,398,000	$29,453,000	$83,733,000	$16,089,000	$349,824,000	$5,113,000	$99,233,000	$15,597,000	$—

impairment

Troubled Debt Restructured

A troubled debt restructured ("TDR") constitutes a restructuring of debt if the Company, for economic or legal reasons related to the borrower's financial difficulties, grants a concession to the borrower that it would not otherwise consider. To determine whether or not a loan should be classified as a TDR, Management evaluates a loan based upon the following criteria:

- The borrower demonstrates financial difficulty; common indicators include past due status with bank obligations, substandard credit bureau reports, or an inability to refinance with another lender, and
- The Company has granted a concession; common concession types include maturity date extension, interest rate adjustments to below market pricing, and deferment of payments.

As of June 30, 2013, the Company had 105 loans with a value of $30,874,000 that have been classified as TDRs. This compares to 101 loans with a value of $29,955,000 and 82 loans with a value of $24,980,000 classified as TDRs as of December 31, 2012 and June 30, 2012, respectively. The impairment carried as a specific reserve in the allowance for loan losses is calculated by present valuing the expected cash flows on the loan at the original interest rate, or, for collateral-dependent loans, using the fair value of the collateral less costs to sell.

The following table shows TDRs by class and the specific reserve as of June 30, 2013:

	Number of Loans	Balance	Specific Reserves
Commercial			
Real estate	20	$13,593,000	$868,000
Construction	3	1,789,000	267,000
Other	23	3,491,000	607,000
Municipal	—	—	—
Residential			
Term	54	11,149,000	167,000
Construction	—	—	—
Home equity line of credit	5	852,000	7,000
Consumer	—	—	—
	105	$30,874,000	$1,916,000

The following table shows TDRs by class and the specific reserve as of December 31, 2012:

	Number of Loans	Balance	Specific Reserves
Commercial			
Real estate	18	$11,961,000	$823,000
Construction	3	3,319,000	969,000
Other	23	3,074,000	574,000
Municipal	—	—	—
Residential			
Term	53	10,945,000	224,000
Construction	—	—	—
Home equity line of credit	4	656,000	—
Consumer	—	—	—
	101	$29,955,000	$2,590,000

The following table shows TDRs by class and the specific reserve as of June 30, 2012:

	Number of Loans	Balance	Specific Reserves
Commercial			
Real estate	17	$9,216,000	$496,000
Construction	2	3,099,000	696,000
Other	15	1,984,000	590,000
Municipal	—	—	—
Residential			
Term	48	10,681,000	327,000
Construction	—	—	—
Home equity line of credit	—	—	—
Consumer	—	—	—
	82	$24,980,000	$2,109,000

As of June 30, 2013, 12 of the loans classified as TDRs with a total balance of $2,197,000 were more than 30 days past due. Of these loans, two loans with an outstanding balance of $524,000 had been placed on TDR status in the previous 12 months. The following table shows these TDRs by class and the associated specific reserves included in the allowance for loan losses as of June 30, 2013:

	Number of Loans	Balance	Specific Reserves
Commercial			
Real estate	2	$319,000	$5,000
Construction	1	423,000	—
Other	2	370,000	9,000
Municipal	—	—	—
Residential			
Term	7	1,085,000	6,000
Construction	—	—	—
Home equity line of credit	—	—	—
Consumer	—	—	—
	12	$2,197,000	$20,000

As of June 30, 2012, 13 of the loans classified as TDRs with a total balance of $2,487,000 were more than 30 days past due. Of these loans, six loans with an outstanding balance of $864,000 had been placed on TDR status in the previous 12 months. The following table shows these TDRs by class and the associated specific reserves included in the allowance for loan losses as of June 30, 2012:

	Number of Loans	Balance	Specific Reserves
Commercial			
Real estate	1	$269,000	$111,000
Construction	—	—	—
Other	3	180,000	—
Municipal	—	—	—
Residential			
Term	9	2,038,000	92,000
Construction	—	—	—
Home equity line of credit	—	—	—
Consumer	—	—	—
	13	$2,487,000	$203,000

For the six months ended June 30, 2013, ten loans were placed on TDR status with an outstanding balance of $3,890,000. This compares to 29 loans placed on TDR status with an outstanding balance of $8,107,000 for the six months ended June 30, 2012. These were considered TDRs because concessions had been granted to borrowers experiencing financial difficulties. Concessions include reductions in interest rates, principal and/or interest forbearance, payment extensions, or combinations thereof.

The following tables show loans placed on TDR status in the six months ended June 30, 2013 and 2012, by class of loan and the associated specific reserve included in the allowance for loan losses as of June 30, 2013 and 2012:

For the six months ended June 30, 2013	Number of Loans	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Specific Reserves
Commercial				
Real estate	2	$ 1,897,000	$ 1,897,000	$—
Construction	—	—	—	—
Other	5	1,164,000	1,150,000	$—
Municipal	—	—	—	—
Residential				
Term	2	625,000	475,000	—
Construction	—	—	—	—
Home equity line of credit	1	204,000	202,000	—
Consumer	—	—	—	—
	10	$ 3,890,000	$ 3,724,000	—

For the six months ended June 30, 2012	Number of Loans	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Specific Reserves
Commercial				
Real estate	12	$ 4,032,000	$ 3,845,000	$152,000
Construction	1	1,951,000	1,951,000	696,000
Other	9	713,000	712,000	544,000
Municipal	—	—	—	—
Residential				
Term	7	1,411,000	1,411,000	76,000
Construction	—	—	—	—
Home equity line of credit	—	—	—	—
Consumer	—	—	—	—
	29	$ 8,107,000	$ 7,919,000	$1,468,000

For the quarter ended June 30, 2013, three loans were placed on TDR status with an outstanding balance of $936,000. This compares to 15 loans placed on TDR status with an outstanding balance of $5,105,000 for the quarter ended June 30, 2012. These were considered TDRs because concessions had been granted to borrowers experiencing financial difficulties. Concessions include reductions in interest rates, principal and/or interest forbearance, payment extensions, or combinations thereof.

The following tables show loans placed on TDR status in the three months ended June 30, 2013 and 2012, by class of loan and the associated specific reserve included in the allowance for loan losses as of June 30, 2013 and 2012:

For the quarter ended June 30, 2013	Number of Loans	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Specific Reserves
Commercial				
Real estate	—	$ —	$ —	$—
Construction	—	—	—	—
Other	2	623,000	620,000	—
Municipal	—	—	—	—
Residential				
Term	1	313,000	163,000	$—
Construction	—	—	—	—
Home equity line of credit	—	—	—	—
Consumer	—	—	—	—
	3	$ 936,000	$ 783,000	$—

For the quarter ended June 30, 2012	Number of Loans	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Specific Reserves
Commercial				
Real estate	5	$ 1,598,000	$ 1,449,000	$152,000
Construction	1	1,951,000	1,951,000	696,000
Other	6	701,000	700,000	545,000
Municipal	—	—	—	—
Residential				
Term	3	855,000	855,000	61,000
Construction	—	—	—	—
Home equity line of credit	—	—	—	—
Consumer	—	—	—	—
	15	$ 5,105,000	$ 4,955,000	$1,454,000

As of June 30, 2013, Management is aware of ten loans classified as TDRs that are involved in bankruptcy with an outstanding balance of $970,000. There were also 23 loans with an outstanding balance of $4,027,000 that were classified as TDRs and on non-accrual status. Five loans with an outstanding balance of $450,000, that were classified as TDRs, were in the process of foreclosure.

Note 5 – Stock Options and Stock-Based Compensation

At the 2010 Annual Meeting, shareholders approved the 2010 Equity Incentive Plan (the "2010 Plan"). This reserves 400,000 shares of common stock for issuance in connection with stock options, restricted stock awards and other equity based awards to attract and retain the best available personnel, provide additional incentive to officers, employees and non-employee Directors and promote the success of our business. Such grants and awards will be structured in a manner that does not encourage the recipients to expose the Company to undue or inappropriate risk. Options issued under the 2010 Plan will qualify for treatment as incentive stock options for purposes of Section 422 of the Internal Revenue Code. Other compensation under the 2010 Plan will qualify as performance-based for purposes of Section 162(m) of the Internal Revenue Code, and will satisfy NASDAQ guidelines relating to equity compensation.

As of June 30, 2013, 46,841 shares of restricted stock had been granted under the 2010 Plan, as detailed in the following table:

Year Granted	Vesting Term (In Years)	Shares	Remaining Term (In Years)
2011	4.0	1,500	1.6
2011	5.0	5,500	2.6
2012	3.0	2,027	1.7
2012	4.0	2,704	2.7
2012	5.0	7,996	3.7
2013	2.0	8,529	1.7
2013	3.0	8,886	2.7
2013	5.0	9,699	4.7
		46,841	3.0

The compensation cost related to these restricted stock grants was $756,000 and will be recognized over the vesting terms of each grant. In the six months ended June 30, 2013, $107,000 of expense was recognized for these restricted shares, leaving $540,000 in unrecognized expense as of June 30, 2013. In the six months ended June 30, 2012, $40,000 of expense was recognized for restricted shares, leaving $240,000 in unrecognized expense as of June 30, 2012.

The Company established a shareholder-approved stock option plan in 1995 (the "1995 Plan"), under which the Company granted options to employees for 600,000 shares of common stock. Only incentive stock options were granted under the 1995 Plan. The option price of each option grant was determined by the Options Committee of the Board of Directors, and in no instance was less than the fair market value on the date of the grant. An option's maximum term was ten years from the date of grant, with 50% of the options granted vesting two years from the date of grant and the remaining 50% vesting five years from the date of grant. As of January 16, 2005, all options under the 1995 Plan had been granted. The Company applies the fair value recognition provisions of the Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") Topic 718 "Compensation – Stock Compensation", to stock-based employee compensation. As of June 30, 2013, all outstanding options were fully vested and all compensation cost for options had been recognized. A summary of the status of outstanding stock options as of June 30, 2013 and changes during the six-month period then ended, is presented below.

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (In years)	Aggregate Intrinsic Value (In thousands)
Outstanding at December 31, 2012	42,000	$18.00		
Granted in 2013	—	—		
Exercised in 2013	—	—		—
Forfeited in 2013	—	—		
Outstanding at June 30, 2013	42,000	$18.00	1.6	—
Exercisable at June 30, 2013	42,000	$18.00	1.6	—

Note 6 – Preferred and Common Stock

Preferred Stock

On January 9, 2009, the Company issued $25,000,000 in Fixed Rate Cumulative Perpetual Preferred Stock, Series A, having a liquidation preference of $1,000 per share, to the U.S. Treasury ("Treasury') under the Capital Purchase Program ("the CPP Shares"). The CPP Shares called for cumulative dividends at a rate of 5.0% per year for the first five years, and at a rate of 9.0% per year in following years, payable quarterly in arrears on February 15, May 15, August 15 and November 15 of each year.

On August 24, 2011, the Company repurchased $12,500,000 of the CPP Shares. Almost all of the repayment was made from retained earnings accumulated since the preferred stock was issued in 2009. On March 27, 2013, the Company repurchased $2,500,000 of the CPP Shares with funds from it's operating account. On May 8, 2013, the Company repurchased the remaining $10,000,000 CPP Shares using proceeds from the Company's common stock offering in the first quarter of 2013, All the repurchase transactions were approved by the Federal Reserve Bank of Boston, the Company's primary regulator.

Incident to such issuance of the CPP shares, the Company issued to the Treasury warrants (the "Warrants") to purchase up to 225,904 shares of the Company's common stock at a price per share of $16.60 (subject to adjustment). The Warrants (and any shares of common stock issuable pursuant to the Warrants) are freely transferable by Treasury to third parties and the Company has filed a registration statement with the Securities and Exchange Commission to allow for possible resale of such securities.

The Warrants have a term of ten years and could be exercised by Treasury or a subsequent holder at any time or from time to time during their term. To the extent they had not previously been exercised, the Warrants will expire after ten years. Treasury will not vote any shares of common stock it receives upon exercise of the Warrants, but that restriction would not apply to third parties to whom Treasury transferred the Warrants. The proceeds from the sale of the CPP Shares were allocated between the CPP Shares and Warrants based on their relative fair values on the issue date. The fair value of the Warrants was determined using the Black-Scholes model which includes the following assumptions: common stock price of $16.60 per share, dividend yield of 4.70%, stock price volatility of 24.43%, and a risk-free interest rate of 2.01%. The discount on the CPP Shares was based on the value that was allocated to the Warrants upon issuance, and is being accreted back to the value of the CPP Shares over a five-year period (the expected life of the shares upon issuance) on a straight-line basis. The Warrants were unchanged as a result of the CPP Shares repurchase transactions and remain outstanding.

Common Stock

On March 28, 2013, the Company consummated a fully underwritten offering for 760,771 shares of the Company's common stock, with net proceeds of $11,649,000. The Company used these proceeds to repurchase the remaining $10,000,000 of CPP Shares on May 8, 2013.

Note 7 – Earnings Per Share

The following table sets forth the computation of basic and diluted earnings per share (EPS) for the six months ended June 30, 2013 and 2012:

	Income (Numerator)	Shares (Denominator)	Per-Share Amount
For the six months ended June 30, 2013			
Net income as reported	$6,098,000		
Less dividends and amortization of premium on preferred stock	345,000		
Basic EPS: Income available to common shareholders	5,753,000	10,316,177	$0.56
Effect of dilutive securities: warrants and restricted stock		47,799	
Diluted EPS: Income available to common shareholders plus assumed conversions	$5,753,000	10,363,976	$0.56
For the six months ended June 30, 2012			
Net income as reported	$6,236,000		
Less dividends and amortization of premium on preferred stock	362,000		
Basic EPS: Income available to common shareholders	5,874,000	9,822,437	$0.60
Effect of dilutive securities: restricted stock		15,461	
Diluted EPS: Income available to common shareholders plus assumed conversions	$5,874,000	9,837,898	$0.60

The following table sets forth the computation of basic and diluted EPS for the quarters ended June 30, 2013 and 2012.

	Income (Numerator)	Shares (Denominator)	Per-Share Amount
For the quarter ended June 30, 2013			
Net income as reported	$3,242,000		
Less dividends and amortization of premium on preferred stock	164,000		
Basic EPS: Income available to common shareholders	3,078,000	10,610,615	$0.29
Effect of dilutive securities: warrants and restricted stock		47,249	
Diluted EPS: Income available to common shareholders plus assumed conversions	$3,078,000	10,657,864	$0.29
For the quarter ended June 30, 2012			
Net income as reported	$3,323,000		
Less dividends and amortization of premium on preferred stock	181,000		
Basic EPS: Income available to common shareholders	3,142,000	9,824,568	$0.32
Effect of dilutive securities: restricted stock		19,727	
Diluted EPS: Income available to common shareholders plus assumed conversions	$3,142,000	9,844,295	$0.32

All earnings per share calculations have been made using the weighted average number of shares outstanding during the period. The potentially dilutive securities are incentive stock options and unvested shares of restricted stock granted to certain key members of Management and the warrants. The number of dilutive shares is calculated using the treasury method, assuming that all options and warrants were exercisable at the end of each period. Options and warrants that are out-of-the-money are not considered in the calculation of dilutive earnings per share as the effect would be anti-dilutive.

The following table presents the number of options and warrants outstanding as of June 30, 2013 and 2012 and the amount for which the market price at period end is above or below the strike price:

	Outstanding	In-the-Money	Out-of-the-Money
As of June 30, 2013			
Incentive stock options	42,000	—	42,000
Warrants issued to Treasury	225,904	225,904	—
Total dilutive securities	267,904	225,904	42,000
As of June 30, 2012			
Incentive stock options	42,000	—	42,000
Warrants issued to Treasury	225,904	—	225,904
Total dilutive securities	267,904	—	267,904

Note 8 – Employee Benefit Plans

401(k) Plan

The Bank has a defined contribution plan available to substantially all employees who have completed 3 months of service. Employees may contribute up to Internal Revenue Service ("IRS") determined limits and the Bank may match employee contributions not to exceed 3.0% of compensation depending on contribution level. Subject to a vote of the Board of Directors, the Bank may also make a profit-sharing contribution to the Plan. Such contribution equaled 2.0% of each eligible employee's compensation in 2012. The amount for 2013 has not been established. The expense related to the 401(k) plan was $199,000 and $186,000 for the six months ended June 30, 2013 and 2012, respectively.

Supplemental Retirement Benefits

The Bank also provides unfunded, non-qualified supplemental retirement benefits for certain officers, payable in installments over 20 years upon retirement or death. The agreements consist of individual contracts with differing characteristics that, when taken together, do not constitute a postretirement plan. The costs for these benefits are recognized over the service periods of the participating officers in accordance with FASB ASC Topic 712 "Compensation – Nonretirement Postemployment Benefits". The expense of these supplemental retirement benefits was $155,000 for the six months ended June 30, 2013 and $145,000 for the same period in 2012. As of June 30, 2013, the associated accrued liability included in other liabilities in the balance sheet was $2,207,000 compared to $2,080,000 and $1,964,000 at December 31, 2012 and June 30, 2012, respectively.

Post-Retirement Benefit Plans

The Bank sponsors two post-retirement benefit plans. One plan currently provides a subsidy for health insurance premiums to certain retired employees and a future subsidy for seven active employees who were age 50 and over in 1996. These subsidies are based on years of service and range between $40 and $1,200 per month per person. The other plan provides life insurance coverage to certain retired employees and health insurance for retired directors. None of these plans are pre-funded. The Company utilizes FASB ASC Topic 712 "Compensation – Nonretirement Postemployment Benefits" to recognize the overfunded or underfunded status of a defined benefit postretirement plan as an asset or liability in its balance sheet and to recognize changes in the funded status in the year in which the changes occur through comprehensive income. The following table sets forth the accumulated postretirement benefit obligation and funded status:

	At or for the six months ended June 30,	
	2013	2012
Change in benefit obligation		
Benefit obligation at beginning of year	$1,954,000	$1,848,000
Service cost	8,000	34,000
Interest cost	52,000	56,000
Benefits paid	(68,000)	(68,000)
Benefit obligation at end of period	1,946,000	1,870,000
Funded status		
Benefit obligation at end of period	(1,946,000)	(1,870,000)
Accrued benefit cost at end of period	$(1,946,000)	$(1,870,000)

The following table sets forth the net periodic pension cost:

	For the six months ended June 30,		For the quarters ended June 30,	
	2013	2012	2013	2012
Components of net periodic benefit cost				
Service cost	$8,000	$34,000	$4,000	$17,000
Interest cost	52,000	56,000	26,000	28,000
Amortization of unrecognized transition obligation	5,000	14,000	—	7,000
Amortization of accumulated losses	4,000	6,000	4,000	3,000
Net periodic benefit cost	$69,000	$110,000	$34,000	$55,000

Amounts not yet reflected in net periodic benefit cost and included in accumulated other comprehensive income (loss) are as follows:

	June 30, 2013	December 31, 2012	June 30, 2012
Unamortized net actuarial loss	$(182,000)	$(186,000)	$(100,000)
Unrecognized transition obligation	—	(5,000)	(20,000)
	(182,000)	(191,000)	(120,000)
Deferred tax benefit at 35%	67,000	68,000	43,000
Net unrecognized postretirement benefits included in accumulated other comprehensive income (loss)	$(115,000)	$(123,000)	$(77,000)

A weighted average discount rate of 4.5% was used in determining the accumulated benefit obligation and the net periodic benefit cost. The assumed health care cost trend rate is 7.0%. The measurement date for benefit obligations was as of year-end for prior years presented. The expected benefit payments for the third quarter of 2013 are $26,000 and the expected benefit payments for all of 2013 are $102,000. Plan expense for 2013 is estimated to be $112,000. A 1% change in trend assumptions would create an approximate change in the same direction of $100,000 in the accumulated benefit obligation, $7,000 in the interest cost and $1,000 in the service cost.

Note 9 - Other Comprehensive Income (Loss)

The following table summarizes activity in the unrealized gain or loss on available for sale securities included in other comprehensive income for the six-months and quarters ended June 30, 2013 and 2012.

	For the six months ended June 30,		For the quarters ended June 30,	
	2013	2012	2013	2012
Balance at beginning of period	$7,940,000	$7,401,000	$5,474,000	$7,088,000
Unrealized gains (losses) arising during the period	(16,410,000)	2,159,000	(12,915,000)	2,118,000
Reclassification of realized gains during the period	(1,087,000)	(1,967,000)	(788,000)	(1,444,000)
Related deferred taxes	6,124,000	(67,000)	4,796,000	(236,000)
Net change	(11,373,000)	125,000	(8,907,000)	438,000
Balance at end of period	$(3,433,000)	$7,526,000	$(3,433,000)	$7,526,000

The reclassification of realized gains is included in the net securities gain line of the consolidated statements of income and comprehensive income and the tax effect is included in the income tax expense line of the same statement.
The following table summarizes activity in the unrealized gain or loss on postretirement benefits included in other comprehensive income for the six-months and quarters ended June 30, 2013 and 2012.

	For the six months ended June 30,		For the quarters ended June 30,	
	2013	2012	2013	2012
Unrecognized postretirement benefits at beginning of period	$(123,000)	$(87,000)	$(119,000)	$(82,000)
Amortization of unrecognized transition obligation	5,000	14,000	—	7,000
Change in accumulated losses	4,000	—	6,000	—
Related deferred taxes	(1,000)	(4,000)	(2,000)	(2,000)
Unrecognized postretirement benefits at end of period	$(115,000)	$(77,000)	$(115,000)	$(77,000)

The reclassification of unrecognized transition obligation is a component of net periodic benefit cost (see Note 8) and the income tax effect is included in the income tax expense line of the consolidated statements of income and comprehensive income.

Note 10 - Acquisitions and Intangible Assets

On October 26, 2012, the Bank completed the purchase of a branch at 63 Union Street in Rockland, Maine, from Camden National Bank that was formerly operated by Bank of America. As part of the transaction, the Bank acquired approximately $32,300,000 in deposits as well as a small volume of loans. On the same date, the Bank completed the purchase of a full-service bank building at 145 Exchange Street in Bangor, Maine, also from Camden National Bank, and opened a full-service branch in this building in the first quarter of 2013. The acquisition allows the Bank to expand its community banking franchise into eastern Maine and expand its presence in Rockland, Maine. The acquisition-date estimated fair values of assets acquired and liabilities assumed in Rockland and Bangor were as follows:

Assets	
Cash	$25,297,000
Loans	224,000
Bank premises and equipment	3,776,000
Accrued interest receivable and other assets	24,000
Core deposit intangible	432,000
Goodwill	2,121,000
Liabilities	
Deposits	$31,858,000
Accrued interest and other liabilities	16,000

The purchase premium of $2,600,000 was allocated to assets acquired and liabilities assumed based on estimates of fair value at the date of acquisition. The fair value of the deposit accounts assumed was compared to the carrying amounts received and the difference of $432,000 was recorded as core deposit intangible. The core deposit intangible is subject to amortization over the estimated ten-year average life of the acquired core deposit base and will be evaluated for impairment periodically. The amortization expense is included in noninterest expense in the consolidated statements of income and comprehensive income (loss) and is deductible for tax purposes. As of December 31, 2012, the amortization expense related to the core deposit intangible, absent any future impairment, is expected to be as follows:

2013	$43,000
2014	43,000
2015	43,000
2016	43,000
2017	43,000
Thereafter	217,000
Total	$432,000

The banking facilities were valued at the most recent tax assessed value, which approximates fair value. The loans acquired were recorded at fair value at the time of acquisition. The estimated fair value of the loans acquired is equal to the carrying value. The excess of the purchase price over the fair value of the assets acquired, liabilities assumed, and the amount allocated for core deposit intangible totaled $2,121,000 and was recorded as goodwill. The goodwill is not amortizable for GAAP but is amortizable for tax purposes. Management periodically assesses qualitative factors to determine whether goodwill is impaired. Management is not aware of any such events or circumstances that would cause it to conclude that the goodwill is impaired.

On January 14, 2005, the Company acquired FNB Bankshares (“FNB”) of Bar Harbor, Maine, and its subsidiary, The First National Bank of Bar Harbor. The total value of the transaction was $47,955,000, and all of the voting equity interest of FNB was acquired in the transaction. The transaction was accounted for as a purchase and the excess of purchase price over the fair value of net identifiable assets acquired equaled $27,559,000 and was recorded as goodwill, none of which was deductible for tax purposes. The portion of the purchase price related to the core deposit intangible is being amortized over its expected economic life, and goodwill is evaluated annually for possible impairment under the provisions of FASB ASC Topic 350, “Intangibles – Goodwill and Other”. As of December 31, 2012, in accordance with Topic 350, the Company completed its annual review of goodwill and determined there has been no impairment. The Bank also carries $125,000 in goodwill for a de minimus transaction in 2001.

Note 11 – Mortgage Servicing Rights

FASB ASC Topic 940 "Financial Services – Mortgage Banking" requires all separately recognized servicing assets and servicing liabilities to be initially measured at fair value, if practicable. The Company's servicing assets and servicing liabilities are reported using the amortization method and carried at the lower of amortized cost or fair value by strata. In evaluating the carrying values of mortgage servicing rights, the Company obtains third party valuations based on loan level data including note rate, type and term of the underlying loans. The model utilizes several assumptions, the most significant of which is loan prepayments, calculated using a three-month moving average of weekly prepayment data published by the Public Securities

Association (PSA) and modeled against the serviced loan portfolio, and the discount rate to discount future cash flows. As of June 30, 2013, the prepayment assumption using the PSA model was 268, which translates into an anticipated prepayment rate of 16.06%. The discount rate is the quarterly average 10 year U.S. Treasury plus 5.09%. Other assumptions include delinquency rates, foreclosure rates, servicing cost inflation, and annual unit loan cost. All assumptions are adjusted periodically to reflect current circumstances. Amortization of mortgage servicing rights, as well as write-offs due to prepayments of the related mortgage loans, are recorded as a charge against mortgage servicing fee income.

For the six months ended June 30, 2013 and 2012, servicing rights capitalized totaled $479,000 and $81,000, respectively. Servicing rights capitalized for the three-month periods ended June 30, 2013 and 2012, were $224,000 and $70,000 respectively. Servicing rights amortized for the six-month periods ended June 30, 2013 and 2012, were $265,000 and $334,000, respectively. The fair value of servicing rights was $1,757,000, $1,228,000 and $1,075,000 at June 30, 2013, December 31, 2012 and June 30, 2012, respectively. The Bank serviced loans for others totaling $212,106,000, $205,859,000 and $213,035,000 at June 30, 2013, December 31, 2012, and June 30, 2012, respectively. Mortgage servicing rights are included in other assets and detailed in the following table:

	June 30, 2013	December 31, 2012	June 30, 2012
Mortgage servicing rights	$6,909,000	$6,430,000	$6,177,000
Accumulated amortization	(5,738,000)	(5,473,000)	(5,170,000)
Impairment reserve	(18,000)	(90,000)	(177,000)
	$1,153,000	$867,000	$830,000

Note 12 – Income Taxes

FASB ASC Topic 740 "Income Taxes," defines the criteria that an individual tax position must satisfy for some or all of the benefits of that position to be recognized in a company's financial statements. Topic 740 prescribes a recognition threshold of more-likely-than-not, and a measurement attribute for all tax positions taken or expected to be taken on a tax return, in order for those tax positions to be recognized in the financial statements. The Company is currently open to audit under the statute of limitations by the IRS for the years ended December 31, 2010 through 2012.

Note 13 - Certificates of Deposit

The following table represents the breakdown of certificates of deposit at June 30, 2013 and 2012, and at December 31, 2012:

	June 30, 2013	December 31, 2012	June 30, 2012
Certificates of deposit < $100,000	$197,888,000	$199,265,000	$239,635,000
Certificates $100,000 to $250,000	334,361,000	277,571,000	313,742,000
Certificates $250,000 and over	37,160,000	28,220,000	60,501,000
	$569,409,000	$505,056,000	$613,878,000

Note 14 – Reclassifications

Certain items from the prior year were reclassified in the financial statements to conform with the current year presentation. These do not have a material impact on the consolidated balance sheet or statement of income and comprehensive income (loss) presentations.

Note 15 – Fair Value

Certain assets and liabilities are recorded at fair value to provide additional insight into the Company's quality of earnings. Some of these assets and liabilities are measured on a recurring basis while others are measured on a nonrecurring basis, with the determination based upon applicable existing accounting pronouncements. For example, securities available for sale are recorded at fair value on a recurring basis. Other assets, such as, other real estate owned and impaired loans, are recorded at fair value on a nonrecurring basis using the lower of cost or market methodology to determine impairment of individual assets. The Company groups assets and liabilities which are recorded at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. A financial instrument's level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement (with level 1 considered highest and level 3 considered lowest). A brief description of each level follows.

Level 1 - Valuation is based upon quoted prices for identical instruments in active markets.
Level 2 - Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market.
Level 3 - Valuation is generated from model-based techniques that use at least one significant assumption not observable in the market. These unobservable assumptions reflect estimates that market participants would use in pricing the asset or liability. Valuation includes use of discounted cash flow models and similar techniques.

The fair value methods and assumptions for the Company's financial instruments and other assets measured at fair value are set forth below.

Cash, Cash Equivalents and Interest-Bearing Deposits in Other Banks
The carrying values of cash equivalents, due from banks and federal funds sold approximate their relative fair values. As such, the Company classifies these financial instruments as Level 1.

Investment Securities
The fair values of investment securities are estimated by independent providers using a market approach with observable inputs. In obtaining such valuation information from third parties, the Company has evaluated their valuation methodologies used to develop the fair values in order to determine whether the valuations are representative of an exit price in the Company's principal markets. The Company's principal markets for its securities portfolios are the secondary institutional markets, with an exit price that is predominantly reflective of bid level pricing in those markets. Fair values are calculated based on the value of one unit without regard to any premium or discount that may result from concentrations of ownership of a financial instrument, possible tax ramifications, or estimated transaction costs. If these considerations had been incorporated into the fair value estimates, the aggregate fair value could have been changed. The carrying values of restricted equity securities approximate fair values. As such, the Company classifies investment securities as Level 2.

Loans Held for Sale
Loans held for sale are recorded at the lower of carrying value or market value. The fair value of mortgage loans held for sale is based on what secondary markets are currently offering for portfolios with similar characteristics. As such, the Company classifies mortgage loans held for sale as Level 2.

Loans
Fair values are estimated for portfolios of loans with similar financial characteristics. The fair values of performing loans are calculated by discounting scheduled cash flows through the estimated maturity using estimated market discount rates that reflect the credit and interest risk inherent in the loan. The estimates of maturity are based on the Company's historical experience with repayments for each loan classification, modified, as required, by an estimate of the effect of current economic and lending conditions, and the effects of estimated prepayments. Assumptions regarding credit risk, cash flows, and discount rates are judgmentally determined using available market information and specific borrower information. Management has made estimates of fair value using discount rates that it believes to be reasonable. However, because there is no market for many of these financial instruments, Management has no basis to determine whether the fair value presented above would be indicative of the value negotiated in an actual sale. As such, the Company classifies loans as Level 3, except for collateral dependent impaired loans. Fair values of impaired loans are based on estimated cash flows and are discounted using a rate commensurate with the risk associated with the estimated cash flows, or if collateral dependent, discounted to the appraised value of the collateral, less costs to sell. As such, the Company classifies collateral dependent impaired loans as Level 2 and all other impaired loans as level 3.

Other Real Estate Owned

Real estate acquired through foreclosure is initially recorded at fair value. The fair value of other real estate owned is based on property appraisals and an analysis of similar properties currently available. As such, the Company records other real estate owned as nonrecurring Level 2.

Mortgage Servicing Rights

Mortgage servicing rights represent the value associated with servicing residential mortgage loans. Servicing assets and servicing liabilities are reported using the amortization method and compared to fair value for impairment. In evaluating the fair values of mortgage servicing rights, the Company obtains third party valuations based on loan level data including note rate, type and term of the underlying loans. As such, the Company classifies mortgage servicing rights as Level 2.

Accrued Interest Receivable
The fair value estimate of this financial instrument approximates the carrying value as this financial instrument has a short maturity. It is the Company's policy to stop accruing interest on loans for which it is probable that the interest is not collectible. Therefore, this financial instrument has been adjusted for estimated credit loss. As such, the Company classifies accrued interest receivable as Level 2.

Deposits
The fair value of deposits is based on the discounted value of contractual cash flows. The discount rate is estimated using the rates currently offered for deposits of similar remaining maturities. The fair value estimates do not include the benefit that results from the low-cost funding provided by the deposits compared to the cost of borrowing funds in the market. If that value were considered, the fair value of the Company's net assets could increase. As such, the Company classifies deposits as Level 2.

Borrowed Funds
The fair value of borrowed funds is based on the discounted value of contractual cash flows. The discount rate is estimated using the rates currently available for borrowings of similar remaining maturities. As such, the Company classifies borrowed funds as Level 2.

Accrued Interest Payable
The fair value estimate approximates the carrying amount as this financial instrument has a short maturity. As such, the Company classifies accrued interest payable as Level 2.

Off-Balance-Sheet Instruments
Off-balance-sheet instruments include loan commitments. Fair values for loan commitments have not been presented as the future revenue derived from such financial instruments is not significant.

Limitations
Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial instrument. These values do not reflect any premium or discount that could result from offering for sale at one time the Company's entire holdings of a particular financial instrument. Because no market exists for a significant portion of the Company's financial instruments, fair value estimates are based on Management's judgments regarding future expected loss experience, current economic conditions, risk characteristics of various financial instruments, and other factors. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates. Fair value estimates are based on existing on- and off-balance-sheet financial instruments without attempting to estimate the value of anticipated future business and the value of assets and liabilities that are not considered financial instruments. Other significant assets and liabilities that are not considered financial instruments include the deferred tax asset, premises and equipment, and other real estate owned. In addition, tax ramifications related to the realization of the unrealized gains and losses can have a significant effect on fair value estimates and have not been considered in any of the estimates.

Assets and Liabilities Recorded at Fair Value on a Recurring Basis
The following tables present the balances of assets and liabilities that were measured at fair value on a recurring basis as of June 30, 2013, December 31, 2012 and June 30, 2012.

	At June 30, 2013			
	Level 1	Level 2	Level 3	Total
Securities available for sale				
Mortgage-backed securities	$—	$157,524,000	$—	$157,524,000

State and political subdivisions	—	128,539,000	—	128,539,000
Other equity securities	—	1,672,000	—	1,672,000
Total assets	$—	$287,735,000	$—	$287,735,000

	At December 31, 2012			
	Level 1	Level 2	Level 3	Total
Securities available for sale				
Mortgage-backed securities	$—	$169,093,000	$—	$169,093,000
State and political subdivisions	—	120,944,000	—	120,944,000
Other equity securities	—	1,577,000	—	1,577,000
Total assets	$—	$291,614,000	$—	$291,614,000
	At June 30, 2012			
	Level 1	Level 2	Level 3	Total
Securities available for sale				
Mortgage-backed securities	$—	$206,979,000	$—	$206,979,000
State and political subdivisions	—	98,593,000	—	98,593,000
Other equity securities	—	1,775,000	—	1,775,000
Total assets	$—	$307,347,000	$—	$307,347,000

Assets and Liabilities Recorded at Fair Value on a Non-Recurring Basis

The following tables include assets measured at fair value on a nonrecurring basis that have had a fair value adjustment since their initial recognition. Other real estate owned is presented net of an allowance of $547,000, $373,000 and $385,000 at June 30, 2013, December 31, 2012, and June 30, 2012, respectively. Impaired loans measured at fair value only include impaired loans with a related specific allowance for loan losses and are presented net of specific allowances of $877,000, $3,539,000 and $4,177,000 at June 30, 2013, December 31, 2012, and June 30, 2012, respectively. The December 31, 2012 and June 30, 2012 non-recurring fair value table includes all impaired loans with a related allowance. The Company refined its process for identifying impaired loans for purposes of fair value disclosures; accordingly the June 30, 2013 fair value table only includes those impaired loans for which the related allowance results in a fair value measure, as described above.

	At June 30, 2013			
	Level 1	Level 2	Level 3	Total
Other real estate owned	$—	$5,826,000	$—	$5,826,000
Impaired loans	—	3,911,000	—	3,911,000
Total assets	$—	$9,737,000	$—	$9,737,000
	At December 31, 2012			
	Level 1	Level 2	Level 3	Total
Other real estate owned	$—	$7,593,000	$—	$7,593,000
Impaired loans	—	13,923,000	—	13,923,000
Total assets	$—	$21,516,000	$—	$21,516,000
	At June 30, 2012			
	Level 1	Level 2	Level 3	Total
Other real estate owned	$—	$5,188,000	$—	$5,188,000
Impaired loans	—	14,734,000	—	14,734,000
Total assets	$—	$19,922,000	$—	$19,922,000

Fair Value of Financial Instruments

FASB ASC Topic 825 "Financial Instruments" requires disclosures of fair value information about financial instruments, whether or not recognized in the balance sheet, if the fair values can be reasonably determined. Fair value is best determined based upon quoted market prices. However, in many instances, there are no quoted market prices for the Company's various financial instruments. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques using observable inputs when available. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. Accordingly, the fair value estimates may not be realized in an immediate settlement of the instrument. Topic 825 excludes certain financial instruments and all nonfinancial instruments from its disclosure requirements. Accordingly, the aggregate fair value amounts presented may not necessarily represent the underlying fair value of the Company.

The carrying amount and estimated fair values for financial instruments as of June 30, 2013 were as follows:

	Carrying value	Estimated fair value	Level 1	Level 2	Level 3
Financial assets					
Cash and cash equivalents	$18,683,000	$18,683,000	$18,683,000	$—	$—
Interest bearing deposits in other banks	334,000	334,000	334,000	—	—
Securities available for sale	287,735,000	287,735,000	—	287,735,000	—
Securities to be held to maturity	177,264,000	174,790,000	—	174,790,000	—
Restricted equity securities	13,912,000	13,912,000	—	13,912,000	—
Loans held for sale	1,047,000	1,047,000	—	1,047,000	—
Loans (net of allowance for loan losses)					
Commercial					
Real estate	245,338,000	243,846,000	—	2,334,000	241,512,000
Construction	17,984,000	17,875,000	—	0	17,875,000
Other	88,533,000	88,601,000	—	755,000	87,846,000
Municipal	14,865,000	15,599,000	—	—	15,599,000
Residential					
Term	373,381,000	379,161,000	—	789,000	378,372,000
Construction	4,749,000	4,736,000	—	—	4,736,000
Home equity line of credit	94,194,000	93,904,000	—	33,000	93,871,000
Consumer	14,357,000	14,714,000	—	—	14,714,000
Total loans	853,401,000	858,436,000	—	3,911,000	854,525,000
Mortgage servicing rights	1,153,000	1,757,000	—	1,757,000	—
Accrued interest receivable	6,443,000	6,443,000	—	6,443,000	—
Financial liabilities					
Demand deposits	$88,540,000	$82,280,000	$—	$82,280,000	$—
NOW deposits	139,022,000	122,048,000	—	122,048,000	—
Money market deposits	87,993,000	71,120,000	—	71,120,000	—
Savings deposits	142,718,000	121,525,000	—	121,525,000	—
Local certificates of deposit	224,472,000	227,421,000	—	227,421,000	—
National certificates of deposit	344,937,000	347,693,000	—	347,693,000	—
Total deposits	1,027,682,000	972,087,000	—	972,087,000	—
Repurchase agreements	85,731,000	85,731,000	—	85,731,000	—
Federal Home Loan Bank advances	171,377,000	176,813,000	—	176,813,000	—
Total borrowed funds	257,108,000	262,544,000	—	262,544,000	—

Accrued interest payable	607,000	607,000	—	607,000	—

The carrying amounts and estimated fair values for financial instruments as of December 31, 2012 were as follows:

	Carrying value	Estimated fair value	Level 1	Level 2	Level 3
Financial assets					
Cash and cash equivalents	$14,958,000	$14,958,000	$14,958,000	$—	$—
Interest bearing deposits in other banks	1,638,000	1,638,000	1,638,000	—	—
Securities available for sale	291,614,000	291,614,000	—	291,614,000	—
Securities to be held to maturity	143,320,000	150,247,000	—	150,247,000	—
Restricted equity securities	14,448,000	14,448,000	—	14,448,000	—
Loans held for sale	1,035,000	1,035,000	—	1,035,000	—
Loans (net of allowance for loan losses)					
Commercial					
Real estate	245,046,000	244,365,000	—	4,865,000	239,500,000
Construction	20,960,000	20,902,000	—	2,284,000	18,618,000
Other	78,985,000	79,312,000	—	472,000	78,840,000
Municipal	14,685,000	16,058,000	—	—	16,058,000
Residential					
Term	378,258,000	390,223,000	—	6,302,000	383,921,000
Construction	6,447,000	6,430,000	—	—	6,430,000
Home equity line of credit	98,381,000	99,038,000	—	—	99,038,000
Consumer	14,022,000	14,392,000	—	—	14,392,000
Total loans	856,784,000	870,720,000	—	13,923,000	856,797,000
Mortgage servicing rights	867,000	1,228,000	—	1,228,000	—
Accrued interest receivable	4,912,000	4,912,000	—	4,912,000	—
Financial liabilities					
Demand deposits	$90,252,000	$91,544,000	$—	$91,544,000	$—
NOW deposits	147,309,000	141,436,000	—	141,436,000	—
Money market deposits	80,983,000	71,799,000	—	71,799,000	—
Savings deposits	135,250,000	126,142,000	—	126,142,000	—
Local certificates of deposit	218,571,000	223,748,000	—	223,748,000	—
National certificates of deposit	286,485,000	290,457,000	—	290,457,000	—
Total deposits	958,850,000	945,126,000	—	945,126,000	—
Repurchase agreements	101,504,000	101,504,000	—	101,504,000	—
Federal Home Loan Bank advances	181,401,000	189,321,000	—	189,321,000	—
Total borrowed funds	282,905,000	290,825,000	—	290,825,000	—
Accrued interest payable	619,000	619,000	—	619,000	—

The carrying amount and estimated fair values for financial instruments as of June 30, 2012 were as follows:

	Carrying value	Estimated fair value	Level 1	Level 2	Level 3
Financial assets					
Cash and cash equivalents	$14,192,000	$14,192,000	$14,192,000	$—	$—
Interest bearing deposits in other banks	—	—	—	—	—
Securities available for sale	307,347,000	307,347,000	—	307,347,000	—
Securities to be held to maturity	135,775,000	143,628,000	—	143,628,000	—
Restricted equity securities	14,448,000	14,448,000	—	14,448,000	—
Loans held for sale	378,000	378,000	—	378,000	—
Loans (net of allowance for loan losses)					
Commercial					
Real estate	246,597,000	247,044,000	—	2,349,000	244,695,000
Construction	31,507,000	31,564,000	—	1,368,000	30,196,000
Other	84,952,000	85,322,000	—	919,000	84,403,000
Municipal	16,068,000	17,640,000	—	—	17,640,000
Residential					
Term	367,152,000	380,115,000	—	9,391,000	370,724,000
Construction	6,386,000	6,380,000	—	286,000	6,094,000
Home equity line of credit	99,810,000	100,546,000	—	416,000	100,130,000
Consumer	14,958,000	15,868,000	—	5,000	15,863,000
Total loans	867,430,000	884,479,000	—	14,734,000	869,745,000
Mortgage servicing rights	830,000	1,075,000	—	1,075,000	—
Accrued interest receivable	6,024,000	6,024,000	—	6,024,000	—
Financial liabilities					
Demand deposits	$77,019,000	$77,250,000	$—	$77,250,000	$—
NOW deposits	123,897,000	117,571,000	—	117,571,000	—
Money market deposits	71,009,000	62,251,000	—	62,251,000	—
Savings deposits	119,471,000	110,169,000	—	110,169,000	—
Local certificates of deposit	212,845,000	218,300,000	—	218,300,000	—
National certificates of deposit	401,033,000	405,539,000	—	405,539,000	—
Total deposits	1,005,274,000	991,080,000	—	991,080,000	—
Repurchase agreements	90,537,000	90,537,000	—	90,537,000	—
Federal Home Loan Bank advances	158,389,000	166,535,000	—	166,535,000	—
Total borrowed funds	248,926,000	257,072,000	—		