BCB BANCORP INC
Form 10-Q
August 12, 2011

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2011.

Or

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

For the transition period from to

Commission File Number: 0-50275

BCB Bancorp, Inc.
(Exact name of registrant as specified in its charter)

New Jersey	26-0065262
(State or other jurisdiction of incorporation or organization)	(IRS Employer I.D. No.)

104-110 Avenue C Bayonne, New Jersey	07002
(Address of principal executive offices)	(Zip Code)

(201) 823-0700
(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year if changed since last report)

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

Large Accelerated Filer	o	Accelerated Filer	o
Non-Accelerated Filer	o	Smaller Reporting Company	ý

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

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

APPLICABLE ONLY TO CORPORATE ISSUERS:

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date. As of August 1, 2011, BCB Bancorp, Inc., had 9,263,032 shares of common stock, no par value, outstanding.

BCB BANCORP INC. AND SUBSIDIARIES

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PART I. FINANCIAL INFORMATION

ITEM I. FINANCIAL STATEMENTS

BCB BANCORP INC. AND SUBSIDIARIES
Consolidated Statements of Financial Condition
(In Thousands, Except Share and Per Share Data, Unaudited)

	June 30, 2011	December 31, 2010
ASSETS		
Cash and amounts due from depository institutions	$ 10,655	$ 22,065
Interest-earning deposits	63,485	99,062
Total Cash and Cash equivalents	74,140	121,127
Securities available for sale	1,314	1,098
Securities held to maturity, fair value $221,719 and $166,785; respectively	217,983	165,572
Loans held for sale	2,147	5,572
Loans receivable, net of allowance for loan losses of $8,716 and $8,417; respectively	764,980	773,101
Premises and equipment	12,784	11,359
Property held for sale	1,017	1,017
Federal Home Loan Bank of New York stock	6,678	6,723
Interest receivable	5,387	5,203
Real estate owned	4,190	3,602
Deferred income taxes	5,925	5,785
Other assets	3,800	6,729
Total Assets	$ 1,100,345	$ 1,106,888
LIABILITIES AND STOCKHOLDERS' EQUITY		
LIABILITIES		
Non-interest bearing deposits	$ 69,966	$ 69,471
Interest bearing deposits	807,647	816,817
Total deposits	877,613	886,288
Long-term debt	114,124	114,124
Other Liabilities	9,096	7,502
Total Liabilities	1,000,833	1,007,914

STOCKHOLDERS' EQUITY		
Preferred stock; $0.01 par value; 10,000,000 shares authorized; none issued and outstanding	-	-
Common stock, stated value $0.064; 20,000,000 shares authorized, 10,170,411 and 10,144,830 shares respectively, issued; 9,278,642 shares and 9,383,695 shares, respectively, outstanding	650	649
Additional paid-in capital	85,533	85,327
Treasury stock, at cost, 891,769 and 761,135 shares, respectively	(12,178)	(10,760)
Retained Earnings	25,372	23,753
Accumulated other comprehensive income, net of taxes	135	5
Total Stockholders' equity	99,512	98,974
Total Liabilities and Stockholders' equity	$ 1,100,345	$ 1,106,888

See accompanying notes to consolidated financial statements.

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BCB BANCORP INC. AND SUBSIDIARIES
Consolidated Statements of Income
(In Thousands, except for per share amounts, Unaudited)

	Three Months Ended June 30, 2011	Three Months Ended June 30, 2010	Six Months Ended June 30, 2011	Six Months Ended June 30, 2010
Interest income:				
Loans	$11,090	$ 6,369	$ 22,351	$ 12,806
Investments, taxable	2,129	1,328	3,882	2,832
Investment, non-taxable	13	-	25	-
Other interest-earning assets	18	21	46	40
Total interest income	13,250	7,718	26,304	15,678
Interest expense:				
Deposits:				
Demand	222	176	447	388
Savings and club	275	238	544	510
Certificates of deposit	1,638	1,380	3,305	2,893
	2,135	1,794	4,296	3,791
Borrowed money	1,233	1,233	2,454	2,454
Total interest expense	3,368	3,027	6,750	6,245
Net interest income	9,882	4,691	19,554	9,433
Provision for loan losses	450	300	800	750
Net interest income after provision for loan losses	9,432	4,391	18,754	8,683
Non-interest income:				
Fees and service charges	243	240	462	400
Gain on sales of loans originated for sale	226	56	404	128
Loss on sale of real estate owned	(80)	-	(136)	-
Gain on sale of securities	18	-	18	-
Other	22	8	158	17
Total non-interest income	429	304	906	545

Non-interest expense:				
Salaries and employee benefits	2,900	1,403	5,907	2,770
Occupancy expense of premises	723	273	1,502	560
Equipment	1,068	536	2,091	1,090
Professional Fees	258	61	461	193
Director Fees	180	108	299	214
Regulatory Assessments	355	189	793	362
Advertising	106	71	178	138
Merger related expenses	256	144	256	344
Other	711	394	1,723	777
Total non-interest expense	6,557	3,179	13,210	6,448
Income before income tax provision	3,304	1,516	6,450	2,780
Income tax provision	1,352	594	2,577	1,140
Net Income	$1,952	$ 922	$ 3,873	$ 1,640

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Net Income per common share				
Basic:	$ 0.21	$ 0.20	$ 0.41	$ 0.35
Diluted	$ 0.21	$ 0.20	$ 0.41	$ 0.35
Weighted average number of common shares outstanding:				
Basic	9,356	4,663	9,375	4,662
Diluted	9,374	4,678	9,394	4,678

See accompanying notes to consolidated financial statements.

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BCB BANCORP INC. AND SUBSIDIARIES
Consolidated Statement of Changes in Stockholders' Equity
(In Thousands, except share and per share data, Unaudited)

	Common Stock	Additional Paid-In Capital	Treasury Stock	Retained Earnings	Accumulated Other Comprehensive Income	Total
Beginning Balance at December 31, 2010	$ 649	$ 85,327	$ (10,760)	$ 23,753	$ 5	$ 98,974
Exercise of Stock Options (25,581 shares)	1	206	—	—	—	207
Treasury Stock Purchases (130,634 shares)	—	—	(1,418)	—	—	(1,418)
Cash dividends ($0.24 per share) declared	—	—	—	(2,254)	—	(2,254)
Net income for the six months ended June 30, 2011	—	—	—	3,873	—	3,873
Unrealized gain on securities available for sale, net of deferred income tax of $(86)	—	—	—	—	130	130
Total Comprehensive income	—	—	—	—	—	4,003
Ending Balance at June 30, 2011	$ 650	$ 85,533	$ (12,178)	$ 25,372	$ 135	$ 99,512

See accompanying notes to consolidated financial statements.

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BCB BANCORP INC. AND SUBSIDIARIES
Consolidated Statements of Cash Flows
(In Thousands, Unaudited)

	Six Months Ended June 30, 2011	Six Months Ended June 30, 2010
Cash flows from operating activities:		
Net Income	$ 3,873	$ 1,640
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation of premises and equipment	505	185
Amortization and accretion, net	767	651
Provision for loan losses	800	750
Deferred income tax benefit	(226)	(62)
Loans originated for sale	(10,143)	(10,881)
Proceeds from sale of loans originated for sale	12,447	11,817
Gain on sale of loans originated for sale	(404)	(128)
Loss on sales of real estate owned	136	-
Gain on sales of securities held to maturity	(18)	-
(Increase) decrease in interest receivable	(184)	233
Decrease (increase) in other assets	2,929	(231)
(Decrease) in accrued interest payable	(34)	(84)
Increase (decrease) in other liabilities	1,628	(619)
Net cash provided by operating activities	12,076	3,271
Cash flows from investing activities:		
Redemption of Federal Home Loan Bank of New York stock	45	12
Proceeds from calls of securities held to maturity	17,322	66,470
Purchases of securities held to maturity	(90,552)	(54,921)
Proceeds from repayments on securities held to maturity	17,509	4,808
Proceeds from sales of securities held to maturity	2.438	-
Proceeds from sales of participation interest in loans	2,437	-
Proceeds from sales of real estate owned	656	494
Purchases of loans	(847)	-
Net decrease in loans receivable	6,004	13,253
Improvements to other real estate owned	(5)	(20)
Additions to premises and equipment	(1,930)	(185)
Net cash (used in) provided by investing activities	(46,923)	29,911
Cash flows from financing activities:		
Net (Decrease) increase in deposits	(8,675)	20,354
Purchases of treasury stock	(1,418)	(12)
Cash dividend paid	(2,254)	(1,120)
Exercise of stock options	207	31

Net cash (used in) provided by financing activities	(12,140)	19,253
Net (Decrease) increase in cash and cash equivalents	(46,987)	52,435
Cash and cash equivalents-beginning	121,127	67,347
Cash and cash equivalents-ending	$ 74,140	$ 119,782
Supplemental disclosure of cash flow information:		
Cash paid during the year for:		
Income taxes	$ 54	$ 1,487
Interest	$ 6,784	$ 6,329
Non-cash items:		
Transfer of loans to other real estate owned	$ 2,316	$ 1,193
Loans to facilitate sale of other real estate owned	$ 942	$ -
Reclassification of loans originated for sale to held to maturity	$ 1,524	$ 2,151

See accompanying notes to consolidated financial statements.

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BCB Bancorp Inc. and Subsidiaries
Notes to Unaudited Consolidated Financial Statements

Note 1 – Basis of Presentation

The accompanying unaudited consolidated financial statements include the accounts of BCB Bancorp, Inc. (the "Company") and the Company's wholly owned subsidiaries, BCB Community Bank (the "Bank"), BCB Holding Company Investment Company, and Pamrapo Service Corporation. The Company's business is conducted principally through the Bank. All significant intercompany accounts and transactions have been eliminated in consolidation.

The accompanying unaudited consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and Regulation S-X and, therefore, do not necessarily include all information that would be included in audited financial statements. The information furnished reflects all adjustments that are, in the opinion of management, necessary for a fair presentation of consolidated financial condition and results of operations. All such adjustments are of a normal recurring nature. The results of operations for the three and six months ended June 30, 2011 are not necessarily indicative of the results to be expected for the fiscal year ending December 31, 2011 or any other future interim period. The preparation of the consolidated financial statements in conformity with accounting principles generally accepted in the United States of America ("GAAP") requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reported periods. Actual results could differ from these estimates.

These unaudited consolidated financial statements should be read in conjunction with the Company's audited consolidated financial statements and related notes for the year ended December 31, 2010, which are included in the Company's Annual Report on Form 10-K as filed with the Securities and Exchange Commission.

In preparing these consolidated financial statements, BCB Bancorp, Inc., evaluated the events and transactions that occurred between June 30, 2011, and the date these consolidated financial statements were issued.

Note 2 – Acquisition

Allegiance Community Bank

On April 5, 2011, BCB Bancorp, Inc. (the Company), its wholly owned New Jersey Bank subsidiary, BCB Community Bank and Allegiance Community Bank ("Allegiance"), headquartered in South Orange, New Jersey, jointly announced the signing of an agreement and plan of merger, dated as of April 4, 2011 (the "merger agreement") pursuant to which Allegiance will merge with and into BCB Community Bank. At December 31, 2010, Allegiance had total assets of approximately $121.3 million, including $84.2 million in loans, and deposits of approximately $100.1 million in two branches in South Orange and Woodbridge, New Jersey. Under the terms of the merger agreement, each outstanding share of Allegiance common stock will be converted into the right to receive 0.35 shares of common stock of the Company, subject to adjustment as disclosed in the merger agreement. The merger is expected to close sometime in the second half of 2011, pending regulatory approvals, approval of the merger agreement by shareholders of Allegiance and the satisfaction of other customary closing conditions.

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Note 3 – Pension and Other Postretirement Plans

The Company acquired, through the merger with Pamrapo Bancorp, Inc., a non-contributory defined benefit pension plan covering all eligible employees of Pamrapo Savings Bank. Effective January 1, 2010, the defined benefit pension plan (“Pension Plan”), was frozen by Pamrapo Savings Bank. All benefits for eligible participants accrued in the “Pension Plan” to the freeze date have been retained. Accordingly, no employees are permitted to commence participation in the Pension Plan and future salary increases and future years of credited service are not considered when computing an employee’s benefits under the Pension Plan. The Pension Plan is funded in conformity with the funding requirements of applicable government regulations. The Company also acquired through the merger with Pamrapo Bancorp, Inc. a supplemental executive retirement plan (“SERP”) in which certain former employees of Pamrapo Savings Bank are covered. A SERP is an unfunded non-qualified deferred retirement plan. Participants who retire at the age of 65 (the “Normal Retirement Age”), are entitled to an annual retirement benefit equal to 75% of compensation reduced by their retirement plan annual benefits. Participants retiring before the Normal Retirement Age receive the same benefits reduced by a percentage based on years of service to the Company and the number of years prior to the Normal Retirement Age that participants retire.

Periodic pension and SERP cost, which is recorded as part of salaries and employee benefits expense in our Consolidated Statements of Income, is comprised of the following, (In Thousands):

	Three months ended June 30		Six Months ended June 30	
	2011	2010	2011	2010
Pension plan:				
Interest cost	$ 117	$ -	$ 234	$ -
Expected return on plan assets	(94)	-	(188)	-
Net periodic pension cost	$ 23	$ -	$ 46	$ -
SERP plan:				
Interest cost	$ 7	$ -	$ 14	$ -
Net periodic postretirement cost	$ 7	$ -	$ 14	$ -

Stock-Based Compensation Plan

The Company, under the plan approved by its shareholders on April 28, 2011 (“2011 Stock Plan”), authorized the issuance of up to 900,000 shares of common stock of BCB Bancorp, Inc. pursuant to grants of stock options. Employees and directors of BCB Bancorp, Inc. and BCB Community Bank are eligible to participate in the 2011 Stock Plan. All stock options will be granted in the form of either "incentive" stock options or "non-qualified" stock options. Incentive stock options have certain tax advantages that must comply with the requirements of Section 422 of the Internal Revenue Code. Only employees are permitted to receive incentive stock options. No grants of stock options have been issued under the 2011 Stock Plan.

Note 4 – Earnings Per Share

Basic net income per common share is computed by dividing net income by the weighted average number of shares of common stock outstanding. The diluted net income per common share is computed by adjusting the weighted average number of shares of common stock outstanding to include the effects of outstanding stock options, if dilutive, using the treasury stock method. For the three and six months ended June 30, 2011 and 2010, the weighted average of outstanding options considered to be anti-dilutive were 180,684 and 230,264, respectively, and were therefore, excluded from diluted net income per common share calculation.

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Note 5 – Securities Available for Sale

	June 30, 2011			
	Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(In Thousands)			
Equity Securities-Financial Institutions	$ 1,097	$ 217	$ -	$ 1,314

	December 31, 2010			
	Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(In Thousands)			
Equity Securities-Financial Institutions	$ 1,097	$ 32	$ 31	$ 1,098

There were no sales of securities available for sale for the six months ended June 30, 2011 and 2010.

The unrealized losses, categorized by the length of time of continuous loss position, and fair value of related securities available for sale were as follows:

	Less than 12 Months		More than 12 Months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	(In Thousands)					
June 30, 2011						
Equity Securities-Financial Institutions	$ —	$ —	$ —	$ —	$ —	$ —
December 31, 2010						

Equity Securities-Financial Institutions	$	65	$	31	$	—	$	—	$	65	$	31

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Note 6 – Securities Held to Maturity

	June 30, 2011			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(In Thousands)			
U.S. Government Agencies:				
Due within one year	$ 3,315	$ 113	$ -	$ 3,428
Due after ten years	25,495	179	19	25,655
	28,810	292	19	29,083
Residential mortgage-backed securities:				
Due within one year	$ 12	$ -	$ –-	$ 12
Due after one year through five years	910	36	-	946
Due after five years through ten years	44,217	563	22	44,758
Due after ten years	136,258	2,981	110	139,129
	181,397	3,580	132	184,845
Subordinated notes:				
Due within one year	$ 6,000	$ -	$ -	$ 6,000
Municipal obligations:				
Due after ten years	1,373	10	-	1,383
Trust originated preferred security:				
Due after ten years	403	5	-	408
	7,776	15	-	7,791
	$ 217,983	$ 3,887	$ 151	$221,719

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Note 6 – Securities Held to Maturity (Continued)

	December 31, 2010			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(In Thousands)			
U.S. Government Agencies:				
Due after one through five years	$ 3,315	$ 180	$ —	$ 3,495
Due after ten years	27,523	14	62	27,475
	30,838	194	62	30,970
Residential mortgage-backed securities:				
Due within one year	$ 6	$ —	$ —	$ 6
Due after one year through five years	775	24	1	798
Due after five years through ten years	54,629	374	357	54,646
Due after ten years	71,545	1,552	493	72,604
	126,955	1,950	851	128,054
Subordinated notes:				
Due within one year	$ 6,000	$ —	$ —	$ 6,000
Municipal obligations:				
Due after ten years	1,376	—	21	1,355
Trust originated preferred security:				
Due after ten years	403	3	—	406
	$ 165,572	$ 2,147	$ 934	$ 166,785

The amortized cost and carrying values shown above are by contractual final maturity. Actual maturities will differ from contractual final maturities due to scheduled monthly payments related to mortgage–backed securities and due to the borrowers having the right to prepay obligations with or without prepayment penalties. At June 30, 2011 and December 31, 2010, all residential mortgage backed securities held in the portfolio were Government Sponsored Enterprise securities.

During the second quarter of 2011, management decided to sell its collateralized mortgage obligations that were issued by the Federal National Mortgage Association (“FNMA”) and the Federal Home Loan Mortgage Corporation (“FHLMC”). While these securities were classified as held to maturity, ASC 320 (formerly FAS 115) allows sales of securities so designated, provided that a substantial portion (at least 85%) of the principal balance has been amortized prior to the sale. During the three and six months ended June 30, 2011, proceeds from sales of securities held to maturity totaled approximately $2,438,000 and resulted in gross gains of approximately $25,000 and gross losses of approximately $7,000.

There were no sales of securities held to maturity for the six months ended June 30, 2010.

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Note 6 – Securities Held to Maturity (Continued)

The unrealized losses, categorized by the length of time of continuous loss position, and fair value of related securities held to maturity were as follows:

	Less than 12 Months		More than 12 Months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	(In Thousands)					
June 30, 2011						
U.S. Government Agencies	$ 2,981	$ 19	$ —	$ —	$ 2,981	$ 19
Residential mortgage-backed securities	20,823	132	—	—	20,823	132
	$ 23,804	$ 151	$ —	$ —	$ 23,804	$ 151
December 31, 2010						
U.S. Government Agencies	$ 20,328	$ 62	$ —	$ —	$ 20,328	$ 62
Residential mortgage-backed securities	74,899	851	—	—	74,899	851
Municipal obligations	1,355	21	—	—	1,355	21
	$ 96,582	$ 934	$ —	$ —	$ 96,582	$ 934

Management does not believe that any of the unrealized losses at June 30, 2011, (which are related to one U.S. Government Agency bonds and thirteen residential mortgage-backed securities) represent an other-than-temporary impairment as they are primarily related to market interest rates and not related to the underlying credit quality of the issuers of the securities as all these securities were issued by U.S. Agencies. Additionally, the Company has the ability, and management has the intent, to hold such securities for the time necessary to recover cost and does not have the intent to sell the securities, and it is more likely than not that it will not have to sell the securities before recovery of their cost.

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Note 7 - Loans Receivable and Allowance for Loan Losses

The following table presents the recorded investment in Loans receivable at June 30, 2011 and December 31, 2010.

	June 30, 2011	December 31, 2010
	(In Thousands)	
Real estate mortgage:		
Residential	$224,896	$ 234,435
Commercial and multi-family	406,866	410,212
Construction	14,266	17,848
	646,028	662,495
Commercial:		
Business loans	23,383	13,932
Lines of credit	45,489	40,228
	68,872	54,160
Consumer:		
Passbook or certificate	889	1,004
Home equity lines of credit	9,948	10,228
Home equity	47,873	53,375
Automobile	140	178
Personal	437	554
	59,287	65,339
Deposit overdrafts	75	80
Total Loans	774,262	782,074
Deferred loan fees, net	(566)	(556)
Allowance for loan losses	(8,716)	(8,417)
	(9,282)	(8,973)
	$764,980	$ 773,101

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Allowance for Loan Losses

Management reviews the adequacy of the allowance on at least a quarterly basis to ensure that the provision for loan losses has been charged against earnings in an amount necessary to maintain the allowance at a level that is adequate based on management's assessment of probable estimated losses. The Company's methodology for assessing the adequacy of the allowance for loan losses consists of several key elements. These elements include a general allocated reserve for impaired loans, a specific reserve for impaired loans and an unallocated portion.

The Company consistently applies the following comprehensive methodology. During the quarterly review of the allowance for loan losses, the Company considers a variety of factors that include:

General economic conditions.

Trends in charge-offs.

Trends and levels of delinquent loans.

Trends and levels of non-performing loans, including loans over 90 days delinquent.

Trends in volume and terms of loans.

Levels of allowance for specific classified loans.

Credit concentrations.

The methodology includes the segregation of the loan portfolio by loans that are performing and loans that are impaired. Loans which are performing are evaluated collectively by loan class or loan type. The allowance for performing loans is evaluated based on historical loan loss experience, including consideration of peer loss analysis, with an adjustment for qualitative factors due to economic conditions in the market. Impaired loans are loans which are 60 days or more delinquent or troubled debt restructured. These loans are individually evaluated for loan loss either by current appraisal, estimated economic factor, or net present value. Management reviews the overall estimate for reasonableness and bases the loan loss provision accordingly.

The portfolio of performing loans is segmented into the following loan types, where the risk level for each type is analyzed when determining the allowance for these loans:

Residential single family real estate loans involve certain risks such as interest rate risk and risk of non-repayment. Adjustable-rate residential family real estate loans decreases the interest rate risk to the Bank that is associated with changes in interest rates but involve other risks, primarily because as interest rates rise, the payment by the borrower rises to the extent permitted by the terms of the loan, thereby increasing the potential for default. At the same time, the marketability of the underlying property may be adversely affected by higher interest rates. Repayment risk can be affected by job loss, divorce, illness and personal bankruptcy of the borrower.

Construction lending is generally considered to involve a high risk due to the concentration of principal in a limited number of loans and borrowers and the effects of the general economic conditions on developers and builders.

Moreover, a construction loan can involve additional risks because of the inherent difficulty in estimating both a property's value at completion of the project and the estimated cost (including interest) of the project. The nature of these loans is such that they are generally difficult to evaluate and monitor. In addition, speculative construction loans to a builder are not necessarily pre-sold and thus pose a greater potential risk to the Bank than construction loans to individuals on their personal residence.

Commercial and multi-family real estate lending entails significant additional risks as compared with residential family property lending. Such loans typically involve large loan balances to single borrowers or groups of related borrowers. The payment experience on such loans is typically dependent on the successful operation of the real estate project. The success of such projects is sensitive to changes in supply and demand conditions in the market for commercial real estate as well as economic conditions generally.

Commercial business lending is generally considered higher risk due to the concentration of principal in a limited number of loans and borrowers and the effects of general economic conditions on the business. Commercial business loans are primarily secured by inventories and other business assets. In most cases, any repossessed collateral for a defaulted commercial business loans will not provide an adequate source of repayment of the outstanding loan balance.

Home equity lending entails certain risks such as interest rate risk and risk of non-repayment. The marketability of the underlying property may be adversely affected by higher interest rates, decreasing the collateral securing the loan. Repayment risk can be affected by job loss, divorce, illness and personal bankruptcy of the borrower.

Home equity line of credit lending entails securing an equity interest in the borrower's home. The risk associated with this type of lending is the marketability of the underlying property may be adversely affected by higher interest rates. Repayment risk can be affected by job loss, divorce, illness and personal bankruptcy of the borrower. This type of lending is often priced on an adjustable rate basis with the rate set at or above a predefined index. Adjustable-rate loans decreases the interest rate risk to the Bank that is associated with changes in interest rates but involve other risks, primarily because as interest rates rise, the payment by the borrower rises to the extent permitted by the terms of the loan, thereby increasing the potential for default

Consumer loans generally have more credit risk because of the type and nature of the collateral and, in certain cases, the absence of collateral. Consumer loans generally have shorter terms and higher interest rates than other lending. In addition, consumer lending collections are dependent on the borrower's continuing financial stability, and thus are more likely to be adversely effected by job loss, divorce, illness and personal bankruptcy. In most cases, any repossessed collateral for a defaulted consumer loan will not provide and adequate source of repayment of the outstanding loan.

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The Company also maintains an unallocated allowance. The unallocated allowance is used to cover any factors or conditions which may cause a potential loan loss but are not specifically identifiable. It is prudent to maintain an unallocated portion of the allowance because no matter how detailed an analysis of potential loan losses is performed, these estimates lack some element of precision. Management must make estima