BERKSHIRE BANCORP INC /DE/
Form 10-K
June 10, 2010

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

FORM 10-K

x ANNUAL REPORT PURSUANT TO SECTION 13 or 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2009

OR

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

For the transition period from to

Commission File Number 0-13649

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

Delaware (State or other jurisdiction of incorporation or organization)	94-2563513 (I.R.S. employer identification number)
160 Broadway, New York, New York (Address of principal executive offices)	10038 (Zip Code)

Registrant's telephone number, including area code: (212) 791-5362

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Traded
Common Stock, par value $.10 per share	The NASDAQ Stock Market LLC (The NASDAQ Global Market)

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the Registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ¨ No x

Indicate by check mark if the Registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ¨ No x

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (232.405 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 ¨ No ¨

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of the Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. x

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

Large accelerated filer ¨	Accelerated filer ¨
Non-accelerated filer ¨ (Do not check if a smaller reporting company)	Smaller reporting company x

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

Aggregate market value of voting and non-voting common stock held by non-affiliates of the Registrant as of June 30, 2009: $17,656,792.

Number of shares of Common Stock outstanding as of June 2, 2010: 7,054,183.

DOCUMENTS INCORPORATED BY REFERENCE: None

Forward-Looking Statements. Statements in this Annual Report on Form 10-K that are not based on historical fact may be "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. Words such as "believe", "may", "will", "expect", "estimate", "anticipate", "continue" or similar terms identify forward-looking statements. A wide variety of factors could cause the actual results and experiences of Berkshire Bancorp Inc. (the "Company") to differ materially from the results expressed or implied by the Company's forward-looking statements. Some of the risks and uncertainties that may affect operations, performance, results of the Company's business, the interest rate sensitivity of its assets and liabilities, and the adequacy of its loan loss allowance, include, but are not limited to: (i) deterioration in local, regional, national or global economic conditions which could result, among other things, in an increase in loan delinquencies, a decrease in property values, or a change in the housing turnover rate; (ii) changes in market interest rates or changes in the speed at which market interest rates change; (iii) changes in laws and regulations affecting the financial services industry; (iv) changes in competition; (v) changes in consumer preferences, (vi) changes in banking technology; (vii) ability to maintain key members of management, (viii) possible disruptions in the Company's operations at its banking facilities, (ix) cost of compliance with new corporate governance requirements, and other factors referred to in the sections of this Annual Report entitled "Business", "Risk Factors" and "Management's Discussion and Analysis of Financial Condition and Results of Operations."

Certain information customarily disclosed by financial institutions, such as estimates of interest rate sensitivity and the adequacy of the loan loss allowance, are inherently forward-looking statements because, by their nature, they represent attempts to estimate what will occur in the future.

The Company cautions readers not to place undue reliance upon any forward-looking statement contained in this Annual Report. Forward-looking statements speak only as of the date they were made and the Company assumes no obligation to update or revise any such statements upon any change in applicable circumstances.

PART I

ITEM 1. Business

General. Berkshire Bancorp Inc., a Delaware corporation, is a bank holding company registered under the Bank Holding Company Act of 1956. References herein to "Berkshire", the "Company" or "we" and similar pronouns shall be deemed to refer to Berkshire Bancorp Inc. and its wholly-owned consolidated subsidiaries unless the context otherwise requires. Berkshire's principal activity is the ownership and management of its indirect wholly-owned subsidiary, The Berkshire Bank (the "Bank"), a New York State chartered commercial bank. The Bank is owned through Berkshire's wholly-owned subsidiary, Greater American Finance Group, Inc. ("GAFG").

We file annual, quarterly and current reports, proxy statements and other information with the Securities and Exchange Commission (the "SEC"). You may read and copy our reports or other filings made with the SEC at the SEC's Public Reference Room, located at 100 F Street, N.E., Washington, DC 20549. You may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. You can also access information that we file electronically on the SEC's website at WWW.SEC.GOV.

We do not presently have a website. However, as soon as practicable after filing with or furnishing to the SEC, we will provide at no cost, paper or electronic copies of our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to those reports. Requests should be directed to:

Berkshire Bancorp Inc.
Investor Relations
160 Broadway, First Floor
New York, NY 10038

Series A Preferred Shares. On October 31, 2008, the Company sold an aggregate of 60,000 shares of its 8% Non-Cumulative Mandatorily Convertible Perpetual Series A Preferred Stock (the "Series A Preferred Shares") at $1,000 per share, or $60 million in the aggregate, to the Company's Chairman of the Board and majority stockholder, and two non-affiliated investors. Each Series A Preferred Share bears non-cumulative cash dividends at the rate of 8% per annum, payable quarterly, is mandatorily convertible into 123.153 shares of our Common Stock on October 31, 2011, unless previously redeemed, and is redeemable at the option of the Company between April 30, 2009 and November 1, 2010 at a redemption price of $1,100. So long as any share of Series A Preferred Shares remains outstanding, unless the full dividends for the most recent dividend payment date have been paid or declared, no dividends may be paid or declared on the Company's Common Stock. No Series A Preferred Shares have been redeemed to date.

Business of the Bank - General. The Bank's principal business consists of gathering deposits from the general public and investing those deposits primarily in loans, debt obligations issued by the U.S. Government and its agencies, debt obligations of business corporations, and mortgage-backed securities. The Bank currently operates from seven deposit-taking offices in New York City, four deposit-taking offices in Orange and Sullivan Counties, New York and deposit taking offices in Ridgefield and Teaneck, NJ.

Branch Locations of The Berkshire Bank
December 31, 2009

4 East 39th Street New York, NY	2 South Church Street Goshen, NY
5 Broadway New York, NY	214 Harriman Drive Goshen, NY
5010 13th Avenue Brooklyn, NY	80 Route 17M Harriman, NY
1421 Kings Highway Brooklyn, NY	60 Main Street Bloomingburg, NY
4917 16th Avenue Brooklyn, NY	1119 Avenue J Brooklyn, NY
600 Broad Avenue Ridgefield, NJ	210 Pinehurst Avenue New York, NY 10033
517 Cedar Lane Teaneck, NJ	

Principal Loan Types. The Bank's principal loan types are residential and commercial mortgage loans and commercial non-mortgage loans, both unsecured and secured by personal property. The Bank's revenues come principally from interest on loans and investment securities. The Bank's primary sources of funds are deposits, borrowings and proceeds from principal and interest payments on loans and investment securities.

Operating Plan. The Bank's operating plan concentrates on obtaining deposits from a variety of businesses, professionals and retail customers and investing those funds in conservatively underwritten loans. Due to the Bank's underwriting criteria, its deposits have significantly exceeded the level of satisfactory loans available for investment in recent years. Hence, the Bank has invested a portion of its available funds in investment, mortgage-backed and auction rate securities.

Market Area. The Bank draws its customers principally from the New York City metropolitan area and the Villages of Goshen and Harriman, New York and their surrounding communities, representing most of Orange County, NY. The Bank also has a branch in Bloomingburg, New York, just over the border between Orange and Sullivan Counties. Predominantly rural with numerous small towns, many residents of Orange and Sullivan Counties work in New York City. Consequently, the health of the economy in the New York City metropolitan area has, and will continue to have a direct effect on the economic well being of residents and businesses in these counties. From time to time, the Bank may make loans or accept deposits from outside these areas, but such transactions generally represent extensions of existing local customer relationships.

Competition. The Bank's principal competitors for deposits are other commercial banks, savings banks, savings and loan associations and credit unions in the Bank's market areas, as well as money market mutual funds, insurance companies, securities brokerage firms and other financial institutions, many of which are substantially larger in size than the Bank. The Bank's competition for loans comes principally from commercial banks, savings banks, savings and loan associations, mortgage bankers, finance companies and other institutional lenders. Many of the institutions which compete with the Bank have much greater financial and marketing resources than the Bank. The Bank's principal methods of competition include loan and deposit pricing, maintaining close ties with its local communities, the quality of the personal service it provides, the types of business services it provides, and other marketing programs.

Operations of the Bank. Reference is made to the information set forth in Item 7 herein ("Management's Discussion and Analysis of Financial Condition and Results of Operations") for information as to various aspects of the Bank's operations, activities and conditions.

Subsidiary Activities. The Bank is permitted under New York State law and federal law to own subsidiaries for certain limited purposes, generally to engage in activities which are permissible for a subsidiary of a national bank. The Bank has two subsidiaries, Berkshire Agency, Inc., a company engaged in the title insurance agency business, and Berkshire 1031, a company that acts as a qualified intermediary in connection with tax free exchanges under Section 1031 of the Internal Revenue Code of 1986.

Regulation. The Company is a bank holding company under federal law and registered as such with the Federal Reserve. The Bank is a commercial bank chartered under the laws of New York State. It is subject to regulation at the state level by the New York Superintendent of Banks and the New York Banking Board, while at the federal level its primary regulator is the Federal Deposit Insurance Corporation (the "FDIC").

Both the Company and the Bank are subject to extensive state and federal regulation of their activities. The following discussion summarizes certain banking laws and regulations that affect Berkshire and the Bank. Proposals to change these laws and regulations are frequently proposed in Congress, in the New York State legislature, and before state and federal bank regulatory agencies. The likelihood and timing of any changes and the impact such changes might have on the Company are impossible to determine with any certainty. A change in applicable laws or regulations, or a change in the way such laws or regulations are interpreted by regulatory agencies or courts, may have a material impact on the business, operations and earnings of the Company, the nature and effect of which cannot be predicted.

Supervisory Actions. The Bank is subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can prompt certain mandatory, and possibly additional discretionary, actions by regulators that, if undertaken, could have a direct material effect on the Company's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of the Bank's assets, liabilities, and certain off-balance-sheet items as calculated under regulatory accounting practices. The Bank's capital amounts and classification are also subject to qualitative judgments by the regulators involving factors such as the risk weights assigned to assets and what items may be counted as capital. Regulators also have broad discretion to require any institution to maintain higher capital levels than otherwise required by statute or regulation, even institutions that are considered "well-capitalized" under applicable regulations.

Bank Holding Company Regulation. The Federal Reserve is authorized to make regular examinations of the Company and its nonbank subsidiaries. Under federal law and Federal Reserve regulations, the activities in which the Company and its nonbank subsidiaries may engage are limited. The Company may not acquire direct or indirect ownership or control of more than 5% of the voting shares of any company, including a bank, without the prior approval of the Federal Reserve, except as specifically authorized under federal law and Federal Reserve regulations. The Company, subject to the approval of the Federal Reserve, may acquire more than 5% of the voting shares of non-banking corporations if those corporations engage in activities which the Federal Reserve deems to be so closely related to banking or managing or controlling banks as to be a proper incident thereto. These limitations also apply to activities in which the Company engages directly rather than through a subsidiary.

The Federal Reserve has enforcement powers over the Company and its non-bank subsidiaries. This allows the Federal Reserve, among other things, to stop activities that represent unsafe or unsound practices or constitute violations of law, rules, regulations, administrative orders or written agreements with a federal bank regulator. These powers may be exercised through the issuance of cease-and-desist orders, the imposition of civil money penalties or other actions.

Federal Reserve Capital Requirements. The Federal Reserve requires that the Company, as a bank holding company, must maintain certain minimum ratios of capital to assets. The Federal Reserve's regulations divide capital into two categories. Primary capital includes common equity, surplus, undivided profits, perpetual preferred stock, mandatory convertible instruments, the allowance for loan and lease losses, contingency and other capital reserves, and minority interests in equity accounts of consolidated subsidiaries. Secondary capital includes limited-life preferred stock, subordinated notes and debentures and certain unsecured long term debt.

The Federal Reserve requires that bank holding companies maintain a minimum ratio of primary capital to total assets of 5.5% and a minimum level of total capital (primary plus secondary capital) equal to 6% of total assets. In calculating capital ratios, the allowance for loan losses, which is a component of primary capital, is added back in determining total assets. Certain capital components, such as debt and perpetual preferred stock, are includable as capital only if they satisfy certain definitional tests.

The Company must also meet a risk-based capital standard. Capital, for the risk-based capital requirement, is divided into Tier I capital and Supplementary capital, determined as discussed below in connection with the FDIC capital requirements imposed on the Bank. The Federal Reserve requires that the Bank maintain a ratio of total capital (defined as Tier I plus Supplementary capital) to risk-weighted assets of at least 8%, of which at least 4% must be Tier I capital. Risk weighted assets are also determined in a manner comparable to the determination of risk-weighted assets under FDIC regulations as discussed below.

At December 31, 2009 and 2008, the Company met the definition of a "well capitalized" bank holding company.

Inter-state Banking. Bank holding companies may generally acquire banks in any state. Federal law also permits a bank to merge with an out-of-state bank and convert any offices into branches of the resulting bank if both states have not opted out of interstate branching; permits a bank to acquire branches from an out-of-state bank if the law of the state where the branches are located permits the interstate branch acquisition; and permits banks to establish and operate new interstate branches whenever the host state opts-in to that authority. Bank holding companies and banks that want to engage in such activities must be adequately capitalized and managed.

The New York Banking Law generally authorizes interstate branching in New York as a result of a merger, purchase of assets or similar transaction. An out of state bank may not first enter New York by opening a new branch in New York,
but once a branch is acquired as described in the preceding sentence, additional new branches may be opened state wide.

Regulation of the Bank. In general, the powers of the Bank are limited to the express powers described in the New York Banking Law and powers incidental to the exercise of those express powers. The Bank is generally authorized to accept deposits and make loans on terms and conditions determined to be acceptable to the Bank. Loans may be unsecured, secured by real estate, or secured by personal property. The Bank may also invest assets in bonds, notes or other debt securities which are not in default and certain limited classes of equity securities including certain publicly traded equity securities in an amount aggregating not more than 2% of assets or 20% of capital. The Bank may also engage in a variety of other traditional activities for commercial banks, such as the issuance of letters of credit.

The exercise of these state-authorized powers is limited by FDIC regulations and other federal laws and regulations. In particular, FDIC regulations limit the investment activities of state-chartered, FDIC-insured banks such as the Bank.

Under FDIC regulations, the Bank generally may not directly or indirectly acquire or retain any equity investment that is not permissible for a national bank. In addition, the Bank may not directly or indirectly through a subsidiary, engage as "principal" in any activity that is not permissible for a national bank unless the FDIC has determined that such activities would pose no risk to the applicable FDIC insurance fund and the Bank is in compliance with applicable regulatory capital requirements. FDIC regulations permit real estate investments under certain circumstances. The Bank does not engage in real estate investing activity.

In May 2009, in connection with the Bank's examination by the Federal Deposit Insurance Corporation (the "FDIC") the Bank received a Joint Memorandum of Understanding (the "MOU") from the FDIC and the New York State Banking Department (the "NYSBD"), which the Bank executed. The MOU sets forth an informal understanding among the Bank, the FDIC and the NYSBD addressing asset quality, loan review, underwriting and administration and certain other concerns identified in the examination. The Bank's board has appointed a committee comprised of three directors to monitor the Bank's compliance. We do not believe that compliance with the MOU will have a material adverse effect on our results of operations or financial condition. As set forth in "Management's Discussion and Analysis of Financial Condition And Results of Operations - Capital Adequacy" and Note O to the Company's consolidated financial statements, the Bank is well capitalized for regulatory purposes as of December 31, 2009.

Loans to One Borrower. With certain exceptions, the Bank may not make loans or other extensions of credit to a single borrower, or certain related groups of borrowers, in an aggregate amount in excess of 15% of the Bank's net worth, plus an additional 10% of the Bank's net worth if such amount is secured by certain types of readily marketable collateral. In addition, the Bank is not permitted to make a mortgage loan in excess of 15% of capital stock, surplus fund and undivided profits.

FDIC Capital Requirements. The FDIC requires that the Bank maintain certain minimum ratios of capital to assets. The FDIC's regulations divide capital into two tiers. The first tier ("Tier I") includes common equity, retained earnings, certain non-cumulative perpetual preferred stock (excluding auction rate issues) and minority interests in equity accounts of consolidated subsidiaries, minus goodwill and other intangible assets (except mortgage servicing rights and purchased credit card relationships subject to certain limitations). Supplementary ("Tier II") capital includes, among other items, cumulative perpetual and long-term limited-life preferred stock, mandatorily convertible securities, certain hybrid capital instruments, term subordinated debt and the allowance for loan losses, subject to certain limitations, less required deductions.

The FDIC requires that the highest rated banks maintain a Tier I leverage ratio (Tier I capital to adjusted total assets) of at least 3.0%. All other banks subject to FDIC capital requirements must maintain a Tier I leverage ratio of 4.0% to 5.0% or more. As of December 31, 2009 and 2008, the Bank's Tier I leverage capital ratio was 9.4% and 8.9%, respectively.

The Bank must also meet a risk-based capital standard. The risk-based standard requires the Bank to maintain total capital (defined as Tier I and Tier II capital) to risk-weighted assets of at least 8%, of which at least 4% must be Tier I capital. In determining the amount of risk-weighted assets, all assets, plus certain off-balance sheet assets, are multiplied by a risk-weight of 0% to 100%, based on the risks the FDIC believes are inherent in the type of asset. As of December 31, 2009 and 2008, the Bank maintained a 15.6% and 12.2% Tier I risk-based capital ratio and a 16.9% and 13.4% total risk-based capital ratio, respectively.

In addition to the foregoing regulatory capital requirements, the FDIC Improvements Act of 1991 created a "prompt corrective action" framework, under which decreases in a depository institution's capital category trigger various supervisory actions. Pursuant to implementing regulations adopted by the FDIC, for purposes of the prompt corrective action provisions, a state-chartered, nonmember bank, such as the Bank, is deemed to be well capitalized if it has: a total risk-based capital ratio of 10% or greater; a Tier I risk-based capital ratio of 6% or greater; and a leverage ratio of 5% or greater. As of December 31, 2009 and 2008, the Bank met the definition of a "well capitalized" financial institution.

Community Reinvestment Act. The Bank must, under federal law, meet the credit needs of its community, including low and moderate income segments of its community. The FDIC is required, in connection with its examination of the Bank, to assess whether the Bank has satisfied this requirement. Failure to satisfy this requirement could adversely affect certain applications which the Bank may make, such as branch applications, merger applications, and applications for permission to purchase branches. In the case of Berkshire, the Federal Reserve will assess the record of each subsidiary bank in considering certain applications by Berkshire. The New York Banking Law contains similar provisions applicable to the Bank. As of the most recent Community Reinvestment Act examinations by the FDIC and the New York State Banking Department, the Bank received "satisfactory" ratings.

Dividends From the Bank to the Company. One source of funds for Berkshire to pay dividends to its stockholders is dividends from the Bank to Berkshire. Under the New York Banking Law, the Bank may pay dividends to Berkshire, without regulatory approval, equal to its net profits for the year in which the payment is made, plus retained net profits for the two previous years, subject to certain limits not generally relevant. The Bank's retained net profits in fiscal 2009 was $7.64 million. The Bank's aggregate retained net loss for the 2007 and 2008 fiscal years totaled approximately $74.55 million. Therefore, the Bank may not pay dividends to Berkshire without obtaining regulatory approval.

Under federal law, the Bank may not make any capital distribution to Berkshire, including any dividend or repurchase of the Bank's stock, if, after making such distribution, the Bank fails to meet the required minimum capital ratio requirements discussed above. The FDIC may prohibit the Bank from paying dividends if, in its opinion, the payment of dividends would constitute an unsafe or unsound practice.

Transactions With Related Parties. The Company, its direct non-banking subsidiaries and other companies controlled by stockholders who control the Company are affiliates, within the meaning of the Federal Reserve Act, of the Bank and its subsidiaries. The Bank's authority to engage in transactions with its "affiliates" is limited by Sections 23A and 23B of the Federal Reserve Act. Section 23A limits the aggregate amount of transactions with any individual affiliate to 10% of the capital and surplus of the Bank and also limits the aggregate amount of transactions with all affiliates to 20% of the Bank's capital and surplus. Extensions of credit to affiliates must be secured by certain specified collateral, and the purchase of low quality assets from affiliates is generally prohibited. Section 23B provides that certain transactions with affiliates, including loans and asset purchases, must be on terms and under circumstances, including credit standards, that are at least as favorable to the Bank as those prevailing at the time for comparable transactions with non-affiliated companies. In the absence of comparable transactions, such transactions may only occur under terms and circumstances, including credit standards, that in good faith would be offered to or would apply to non-affiliated companies.

In accordance with banking regulations, the Bank may make loans to its and the Company's directors, executive officers, and 10% stockholders, as well as to entities controlled by them, subject to specific federal and state limits. Among other things, these loans must (a) be made on terms that are substantially the same as, and follow credit underwriting procedures that are not less stringent than, those prevailing for comparable transactions with unaffiliated persons and that do not involve more than the normal risk of repayment or present other unfavorable features and (b) not exceed certain limitations on the amount of credit extended to such persons, individually and in the aggregate, which limits are based, in part, on the amount of the Bank's capital. In addition, extensions of credit in excess of certain limits must be approved by the Bank's Board of Directors. However, the Bank may make loans to executive officers, directors and principal stockholders on preferential terms, provided the extension of credit is made pursuant to a benefit or compensation program of the Bank that is widely available to employees of the Bank or its affiliates and does not give preference to any insider over other employees of the Bank or affiliates. The Bank has no such benefit or compensation programs.

Enforcement. The FDIC and the Banking Department have enforcement authority over the Bank. The Superintendent of the Banking Department (the "Superintendent") may order the Bank to appear and explain an apparent violation of law, to discontinue unauthorized or unsafe practices and to keep prescribed books and accounts. If any director or officer of the Bank has violated any law, or has continued unauthorized or unsafe practices in conducting the business of the Bank after having been notified by the Superintendent to discontinue such practices, the New York Banking Board may remove the individual from office after notice and an opportunity to be heard. The Superintendent also may take over control of the Bank under specified statutory criteria.

The FDIC's enforcement authority includes, among other things, the ability to assess civil money penalties, to issue cease and desist orders and to remove directors and officers. As indicated above, the FDIC is required to take prompt action to correct deficiencies in banks which do not satisfy specified FDIC capital ratio requirements. Dividends, other capital distributions or the payment of management fees to any controlling person are prohibited if, following such distribution or payment, a bank would be undercapitalized. An undercapitalized bank must file a plan to restore its capital within 45 days after being notified that it is undercapitalized. Undercapitalized, significantly undercapitalized and critically undercapitalized institutions are subject to increasing prohibitions on permitted activities, and increasing levels of regulatory supervision, based upon the severity of their capital problems. The FDIC is required to monitor closely the condition of an undercapitalized bank. Enforcement action taken by the FDIC can escalate to the appointment of a conservator or receiver of a critically undercapitalized bank.

Insurance of Accounts. Deposit insurance premiums payable to the FDIC are based upon the perceived risk of the institution to the FDIC insurance fund. The FDIC assigns an institution to one of three capital categories: (a) well capitalized, (b) adequately capitalized or (c) undercapitalized. The FDIC also assigns an institution to one of three supervisory categories based on an evaluation by the institution's primary federal regulator and information that the FDIC considers relevant to the institution's financial condition and the risk posed to the deposit insurance funds. At present, the Bank pays no deposit insurance premium based upon its risk-based categorization.

The FDIC has raised insurance premiums to cover substantial losses incurred by the Deposit Insurance Fund ("DIF") due to recent bank failures of 2009 and 2008. As a result, we expect deposit insurance premiums may be higher for the foreseeable future than they have been in the recent past. The Bank's FDIC assessments increased by 79% to $1.93 million in fiscal 2009 from $1.08 million in fiscal 2008. The increased assessment is a result of the FDIC's anticipation of greater demands on the Bank Insurance Fund in the future in response to the current unrest in the banking industry. In June 2009, the Bank paid a special assessment charged by the FDIC in the amount of $453,000.

In November 2009, the FDIC adopted a final rule imposing a 13 quarter prepayment of FDIC premiums. The Bank's prepayment amount totaled $5.59 million and was paid in December 2009. This was an estimated prepayment for the fourth quarter of 2009 through the fourth quarter of 2012. The prepayment amount will be used to offset future FDIC insurance premiums beginning in March 2010.

Reserve Requirements. The Bank must maintain non-interest-earning reserves against its transaction accounts (primarily NOW and regular checking accounts). The Bank is generally able to satisfy reserve requirements with cash on hand and other non-interest bearing deposits which it maintains for other purposes, so the reserve requirements do not impose a material financial burden on the Bank.

Governmental Policies. Our earnings are significantly affected by the monetary and fiscal policies of governmental authorities, including the Federal Reserve. Among the instruments of monetary policy used by the Federal Reserve to implement these objectives are open-market operations in U.S. Government securities and Federal funds, changes in the discount rate on member bank borrowings and changes in reserve requirements against member bank deposits. These instruments of monetary policy are used in varying combinations to influence the overall level of bank loans, investments and deposits, and the interest rates charged on loans and paid for deposits. The Federal Reserve frequently uses these instruments of monetary policy, especially its open-market operations and the discount rate, to influence the level of interest rates and to affect the strength of the economy, the level of inflation or the price of the dollar in foreign exchange markets. The monetary policies of the Federal Reserve have had a significant effect on the operating results of banking institutions in the past and are expected to continue to do so in the future. It is not possible to predict the nature of future changes in monetary and fiscal policies, or the effect which they may have on our business and earnings.

Personal Holding Company Status. For the fiscal years ended December 31, 2009, 2008 and 2007, the Company has been deemed to be a Personal Holding Company (a "PHC"), as defined in the Internal Revenue Code. As a PHC, we may be required to pay an additional income tax or issue a dividend to our stockholders in an amount based upon the PHC Internal Revenue Code formulas, which is primarily based upon net income. No such dividend was required to be paid in fiscal 2009, 2008 and 2007. (See Dividends in Item 5).

Employees. On March 31, 2010, the Company had one full time employee and the Bank employed 112 full time and 4 part time employees. The Bank's employees are not represented by a collective bargaining unit, and the Bank considers its relationship with its employees to be good.

ITEM 1A. Risk Factors.

Our business faces significant risks. These risks include those described below and may include additional risks and uncertainties not presently known to us or that we currently deem immaterial. Our business, financial condition and results of operations could be materially adversely affected by any of these risks, and the trading price of our common stock could decline.

Our future success depends on our ability to compete effectively in a highly competitive market and geographic area.

Our ability to return to and maintain profitability may depend in part on our ability to expand our scope of available financial services as needed to meet the needs and demands of our customers. Our business model focuses on using superior customer service to provide traditional banking services to a growing customer base. However, we face substantial competition in all phases of our operations from a variety of different competitors. We encounter competition from other commercial banks, savings and loan associations, mutual savings banks, credit unions and other financial institutions. Our competitors, including credit unions, consumer finance companies, factors, insurance companies and money market mutual funds, compete with lending and deposit-gathering services offered by us. In addition, our competitors now include securities dealers, brokers, mortgage bankers, investment advisors and finance and insurance companies who seek to offer one-stop financial services to their customers that may include services that we have not been able or allowed to offer to our customers in the past. This increasingly competitive environment is primarily a result of changes in regulation, changes in technology and product delivery systems and the accelerating pace of consolidation among financial services providers. There is very strong competition for financial services in the New York state areas in which we currently conduct our business. This geographic area includes offices of many of the largest financial institutions in the world. Many of those competing institutions have much greater financial and marketing resources than we have. Due to their size, many competitors can achieve larger economies of scale and as a result may offer a broader range of products and services than we do. If we are unable to offer competitive products and services, our earnings may be negatively affected. Some of the financial services organizations with which we compete are not subject to the same degree of regulation as is imposed on bank holding companies like ourselves and on federally insured financial institutions like our banking subsidiary, The Berkshire Bank. As a result, these nonbank competitors have certain advantages over us in accessing funding and in providing various services. The banking business in our current primary market area is very competitive, and the level of competition we face may increase further, which may limit our asset growth and profitability.

Economic conditions either nationally or locally in areas in which our operations are concentrated may be less favorable than expected.

Deterioration in local, regional, national or global economic conditions could result in, among other things, an increase in loan delinquencies, a decrease in property values, a change in housing turnover rate or a reduction in the level of bank deposits. Particularly, a weakening of the real estate or employment market in our primary market areas could result in an increase in the number of borrowers who default on their loans and a reduction in the value of the collateral securing their loans, which in turn could have an adverse effect on our profitability. Substantially all of our real estate loans are collateralized by properties located in these market areas, and substantially all of our loans are made to borrowers who live in and conduct business in these market areas. Any material economic deterioration in these market areas could
have an adverse impact on our profitability.

Much of the Bank's lending is in New York City and upstate New York. As a result of this geographic concentration, a significant broad-based deterioration in economic conditions in the New York City metropolitan area and upstate New York could have a material adverse impact on the quality of the Bank's loan portfolio, and accordingly, our results of operations. Such a decline in economic conditions could restrict borrowers' ability to pay outstanding principal and interest on loans when due, and, consequently, adversely affect the cash flows of our business.

The Bank's loan portfolio is largely secured by real estate collateral. Conditions in real estate markets in which the collateral for the Bank's loans are located strongly influence the level of the Bank's non-performing loans and results of operations. A decline in the New York City metropolitan area and upstate New York real estate markets, as well as other external factors, could adversely affect the Bank's loan portfolio.

Recent negative developments in the financial services industry and U.S. and global credit markets may adversely impact our operations and results.

Negative developments in the capital markets during the latter half of 2007, throughout 2008 and 2009, and during 2010 to date have resulted in uncertainty in the financial markets in general with the expectation of the general economic downturn continuing for the remainder of 2010 and possibly beyond. Loan portfolio performances have deteriorated at many institutions, including the Bank, resulting from, among other factors, a weak economy and a decline in the value of the collateral supporting their loans. The competition for our deposits has increased significantly due to liquidity concerns at many of these same institutions. Stock prices of bank holding companies like ours have been negatively affected by the current condition of the financial markets, as has our ability, if needed, to raise capital or borrow in the debt markets compared to recent years. As a result, there is a potential for new federal or state laws and regulations regarding lending and funding practices and liquidity standards, and financial institution regulatory agencies are expected to be very aggressive in responding to concerns and trends identified in examinations. Negative developments in the financial services industry and the impact of new legislation in response to those developments could negatively impact our operations by restricting our business operations, including our ability to originate or sell loans, and adversely impact our financial performance.

Changes in interest rates could reduce our income and cash flows.

Our income and cash flow and the value of our assets and liabilities depend to a great extent on the difference between the interest rates earned on interest-earning assets such as loans and investment securities, and the interest rates paid on interest-bearing liabilities such as deposits and borrowings. These rates are highly sensitive to many factors which are beyond our control, including general economic conditions and policies of various governmental and regulatory agencies, in particular, the Board of Governors of the Federal Reserve System. Changes in monetary policy, including changes in interest rates, will influence the origination of loans, the returns on our portfolio of investment securities and the amounts paid on deposits. If the rate of interest we pay on deposits and other borrowings increases more than the rate of interest we earn on loans and other investments, our net interest income, and therefore our earnings, could be adversely affected. In addition, there is a risk that certain deposits would not be renewed. Our earnings could also be adversely affected if the rates on our loans and other investments fall more quickly than those on our deposits and other borrowings. During 2009, interest rates continued at historic lows, a situation which has negatively affected and continues to negatively affect the yield we achieve on interest-earning assets.

Due to the recent downturn in the market, certain of the marketable securities we own may take longer to auction than initially anticipated, if at all.

Our portfolio of investment securities includes auction rate securities. From the first quarter of 2008 to the present, our balance of auction rate securities failed to auction due to sell orders exceeding buy orders. Unless we hold these securities to maturity, these funds will not be available to us until a successful auction occurs or a buyer is found outside the auction process. During 2009, we recorded approximately $2.0 million in OTTI charges related to Freddie Mac auction rate securities. In fiscal 2008 approximately $101 million of auction rate securities, at cost, were written down to approximately $63 million, based on our analysis, as an unrealized temporary decrease in fair value, which is reflected as a component of accumulated other comprehensive loss in the stockholders' equity section of our consolidated balance sheet. This is in addition to the other than temporary impairment charge recognized on auction rate securities which have preferred shares of the Federal National Mortgage Association ("Fannie Mae") and the Federal Home Loan Mortgage Corporation ("Freddie Mac") as the underlying collateral, as described elsewhere in this Report. Further discussion of the auction rate securities may also be found elsewhere in this Report under "Investment Activities."

Declines in value may adversely impact the investment portfolio.

As of December 31, 2009, we had approximately $357.5 million and $340,000 in available for sale and held to maturity investment securities, respectively. We may be required to record other-than-temporary impairment ("OTTI") charges on our investment securities if they suffer a decline in value that is related to the credit quality of the issue. Numerous factors, including lack of liquidity for re-sales of certain investment securities, absence of reliable pricing information for investment securities, adverse changes in business climate, adverse actions by regulators, or unanticipated changes in the competitive environment, could have a negative effect on our investment portfolio in future periods. In 2009 and 2008, impairment charges on investment securities were $17.4 million and $94.3 million, respectively. There can be no assurances that further impairment charges will not have to be recognized. In addition, as noted in Part II Item 9A(T) - Controls and Procedures, we identified a material weakness related to our method of identification and valuation of securities for other than temporary impairment and related tax accounting. Management has revised the relevant controls and procedures with respect to these matters which, if not properly corrected, could have a negative effect on our investment portfolio in future periods.

We operate in a highly regulated environment; changes in laws and regulations and accounting principles may adversely affect us.

We are subject to extensive state and federal regulation, supervision, and legislation which govern almost all aspects of our operations. These laws may change from time to time and are primarily intended for the protection of customers, depositors, and the deposit insurance funds. The impact of any changes to these laws may negatively impact our ability to expand our services and to increase the value of our business. Regulatory authorities have extensive discretion in the exercise of their supervisory and enforcement powers. They may, among other things, impose restrictions on the operation of a banking institution, the classification of assets by such institution and such institution's allowance for loan losses. Regulatory and law enforcement authorities also have wide discretion and extensive enforcement powers under various consumer protection, civil rights and other laws, including the Gramm-Leach-Blilely Act, the Bank Secrecy Act, the Truth-in-Lending Act, the Equal Credit Opportunity Act, the Fair Housing Act and the Real Estate Settlement Procedures Act. These laws also permit private individual and class action lawsuits and provide for the recovery of attorneys fees in certain instances. Any changes to these laws or any applicable accounting principles may negatively impact our results of operations and financial condition. We are currently analyzing the Restoring American Financial Stability Act, passed by the United States Senate on May 10, 2010, and the effects such act would have on the Company's operations and financial condition if it were to become law. While we cannot predict what effect any presently contemplated or future changes in the laws or regulations or their interpretations would have, these changes could be materially adverse to our investors and stockholders.

In May 2009, in connection with the Bank's examination by the Federal Deposit Insurance Corporation (the "FDIC") the Bank received a Joint Memorandum of Understanding (the "MOU") from the FDIC and the New York State Banking Department (the "NYSBD"), which the Bank executed. The MOU sets forth an informal understanding among the Bank, the FDIC and the NYSBD addressing asset quality, loan review, underwriting and administration and certain other concerns identified in the examination. The Bank's board has appointed a committee comprised of three directors to monitor the Bank's compliance. We do not believe that compliance with the MOU will have a material adverse effect on our results of operations or financial condition. As set forth in "Management's Discussion and Analysis of Financial Condition And Results of Operations - Capital Adequacy" and Note O to the Company's consolidated financial statements, the Bank is well capitalized for regulatory purposes as of December 31, 2009.

We are required to maintain an allowance for loan losses. These reserves are based on management's judgment and may have to be adjusted in the future. Any adjustment to the allowance for loan losses, whether due to regulatory changes, economic conditions or other factors, may affect our financial condition and earnings.

We maintain an allowance for loan losses at a level believed adequate by management to absorb losses specifically identifiable and inherent in the loan portfolio. In conjunction with an internal loan review function that operates independently of the lending function, management monitors the loan portfolio to identify risks on a timely basis so that an appropriate allowance can be maintained. Based on an evaluation of the loan portfolio, management presents a periodic review of the loan loss reserve to the board of directors of the Bank, indicating any changes in the reserve since the last review and any recommendations as to adjustments in the reserve. In making its evaluation, in addition to the factors discussed below, management considers the results of recent regulatory examinations, which typically include a review of the allowance for loan losses as an integral part of the examination process.

In establishing the allowance, management evaluates individual large classified loans and nonaccrual loans, and determines an aggregate reserve for those loans based on that review. An allowance for the remainder of the loan portfolio is also determined based on historical loss experience within the components of the portfolio. These allocations may be modified if current conditions indicate that loan losses may differ from historical experience, based on economic factors and changes in portfolio mix and volume.

In addition, a portion of the allowance is established for losses inherent in the loan portfolio which have not been identified by the more quantitative processes described above. This determination inherently involves a higher degree of subjectivity, and considers risk factors that may not have yet manifested themselves in historical loss experience. Those factors include changes in levels and trends of charge-offs, delinquencies, and nonaccrual loans, trends in volume and terms of loans, changes in underwriting standards and practices, portfolio mix, tenure of loan officers and management, entrance into new geographic markets, changes in credit concentrations, and national and local economic trends and conditions. While the allowance for loan losses is maintained at a level believed to be adequate by management for estimated losses in the loan portfolio, determination of the allowance is inherently subjective, as it requires estimates, all of which may be susceptible to significant change. Changes in these estimates may impact the provisions charged to expense in future periods. Federal and state regulatory authorities, as an integral part of their examination process, review our loans and allowance for loan losses. We cannot assure you that we will not increase the allowance for loan losses or the regulators will not require us to increase this allowance. Either of these occurrences could negatively impact Berkshire Bancorp's results of operations.

We may be adversely affected by the soundness of other financial institutions.

Financial services institutions are interrelated as a result of trading, clearing, counterparty, or other relationships. We have exposure to many different industries and counterparties, and routinely execute transactions with counterparties in the financial service industry, including the Federal Home Loan Bank of New York (the "FHLBNY"), commercial banks, brokers and dealers, investment banks, and other institutional clients. Many of these transactions expose us to credit risk in the event of a default by a counterparty or client. In addition, our credit risk may be exacerbated when the collateral held by us cannot be realized or is liquidated at prices not sufficient to recover the full amount due to us. Any such losses could have a material adverse effect on our financial condition and results of operations.

It may be difficult for a third party to acquire us and this could depress our common stock price.

Under our amended and restated certificate of incorporation, we have authorized 2,000,000 shares of preferred stock, of which 60,000 shares have been designated as Series A Preferred Stock, and of which the remaining 1,940,000 shares may be issued by the board of directors with terms, rights, preferences and designations as the board of directors may determine and without any vote of the stockholders, unless otherwise required by law. Issuing the preferred stock, depending upon the rights, preferences and designations set by the board of directors, may delay, deter, or prevent a change in control of the Company.

In addition, federal and state banking laws may restrict the ability of the stockholders to approve a merger or business combination or obtain control of the Company. This may tend to make it more difficult for stockholders to replace existing management or may prevent stockholders from receiving a premium for their shares of our common stock.

Issuance of Common Stock Upon Conversion of Series A Preferred Stock and Other Factors Could Depress our Common Stock Price.

At December 31, 2009, there are 60,000 shares of preferred stock outstanding which have been issued to the Company's majority stockholder and two unaffiliated entities. The preferred stock may be redeemed by the Company between April 30, 2009 and November 1, 2010 at $1,100 per share. Each preferred share is mandatorily convertible into 123.153 shares of common stock on October 31, 2011 unless previously redeemed. The availability of additional shares for sale in the market could depress our common stock price.

In addition, we have authorized 25,000,000 shares of common stock of which approximately 7,000,000 shares are issued and outstanding. The price of our common stock may be volatile at times since our common stock is thinly traded and one individual owns or controls more than 50% of our outstanding shares. It may be difficult for a stockholder to sell a significant number of shares at a time and at a price of their choosing or for a third party to purchase sufficient shares on the open market to cause a change in control of the Company, all of which could depress the price of the Company's common stock.

Our stock is not insured by any governmental agency and, therefore, investment in them involves risk.

Our securities are not deposit accounts or other obligation of any bank, and are not insured by the FDIC, or any other governmental agency, and are subject to investment risk, including the possible loss of principal.

Our Series A Preferred Shares impact net income available to our common stockholders and our earnings per share.

As long as there are Series A Preferred Shares outstanding, no dividends may be paid on our Common Stock unless all dividends on the Series A Preferred Shares have been paid in full. The dividends declared on our fixed rate Series A Preferred Shares will reduce the net income available to holders of our Common Stock and our earnings per share of Common Stock. The Series A Preferred Shares will also receive preferential treatment in the event of liquidation, dissolution or winding up of the Company.

Moreover, holders of our Common Stock are entitled to receive dividends only when, as and if declared by our board of directors. We have temporarily ceased paying a dividend on our Common Stock. The absence of cash dividends on our Common Stock could adversely affect the market price.

The Financial Sector Is Experiencing An Economic Downturn. An Increase In The Number of Non-performing Loans Will Have An Adverse Effect On Our Operations.

Virtually all of our real estate loans are secured by real estate in New York. At December 31, 2009, loans secured by real estate, including home equity loans and lines of credit, represented 88% of our total loans. Both nationally and in the State of New York, we are experiencing an economic downturn that is having a significant impact on the prices of real estate and related assets. The residential and commercial real estate sectors have been adversely affected by weakening economic conditions and may negatively impact our loan portfolio. While we believe that our total non-performing loans as a percentage of total assets are relatively low by industry standards, if loans that are currently performing become non-performing, we may need to increase our allowance for loan losses, which would have an adverse impact on our financial condition and results of operations. We added approximately $9.30 million and $4.90 million to the allowance for loan losses during the fiscal years ended December 31, 2009 and 2008, respectively.

Our FDIC Premium Could Be Substantially Higher In The Future, Which Would Have An Adverse Effect On Our Future Earnings.

Our FDIC insurance assessment was $1.93 million for 2009 compared to $1.08 million for 2008. See "Insurance of Accounts."

ITEM 1B. Unresolved Staff Comments.

Not Applicable

ITEM 2. Properties.

The following are Berkshire's and the Bank's principal facilities as of March 31, 2010:

Location	Operations	Approximate Floor Area (Sq. Ft.)	Approximate Annual Lease Rent		Expiration
New York, NY	Executive Offices	1,500	$	18,000	(1)(3)
New York, NY	Main Bank Office and Bank Branch	9,729	Owned		March 2013
Brooklyn, NY	Bank Branch	4,500	$	229,029	March 2013
Brooklyn, NY	Bank Branch	2,866	$	83,898	March 2013
Brooklyn, NY	Bank Branch	2,592	$	118,245	December 2012
Brooklyn, NY	Bank Branch	1,640	$	79,433	June 2015

New York, NY	Bank Branch	9,924	$	353,315	June 2010 (2)(3)
New York, NY	Bank Branch	3,300	$	63,263	November 2016 (2)(3)
Goshen, NY	Bank Branch	10,680	Owned		
Harriman, NY	Bank Branch	1,623	Owned		
Bloomingburg, NY	Bank Branch	1,530	$	22,806	August 2010
Ridgefield, NJ	Bank Branch	6,120	Owned		
Teaneck, NJ	Bank Branch	2,200	$	44,000	June 2014

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(1) Rented on a month to month basis from a company affiliated with Mr. Moses Marx, a director of the Company.
(2) Leased from a company affiliated with Mr. Marx, a director of the Company.
(3) Management believes the annual rent paid is comparable to the annual rent that would be paid to non-affiliated parties in a similar commercial transaction for similar commercial space.

ITEM 3. Legal Proceedings.

In the ordinary course of operations, the Bank is a party to routine litigation involving claims incidental to its banking business. Management believes that no current litigation, threatened or pending, to which we or our assets are a party, poses a substantial likelihood of potential loss or exposure which would have a material adverse effect on the financial condition or results of our operations.

ITEM 4. (Reserved)

PART II

ITEM 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.

The Company's Common Stock trades on the Nasdaq Global Market under the symbol BERK. The following table sets forth, for the periods indicated, the high and low sales prices for the Company's Common Stock as reported by NASDAQ.

Fiscal Year Ended December 31, 2008	High	Low
January 1, 2008 to March 31, 2008	$ 16.94	$ 13.52
April 1, 2008 to June 30, 2008	15.98	12.05
July 1, 2008 to September 30, 2008	14.71	4.71
October 1, 2008 to December 31, 2008	8.99	4.16

Fiscal Year Ended December 31, 2009	High	Low
January 1, 2009 to March 31, 2009	$ 5.00	$ 3.30
April 1, 2009 to June 30, 2009	6.00	4.00
July 1, 2009 to September 30, 2009	8.98	4.86
October 1, 2009 to December 31, 2009	7.78	5.23

As of the close of business on June 4, 2010, there were 902 holders of record of the Company's Common Stock.

Dividends

For the fiscal years ended December 31, 2009, 2008 and 2007, the Company has been deemed to be a PHC, as defined in the Internal Revenue Code. As a PHC, we may be required to pay an additional income tax or issue a dividend to our stockholders in an amount based upon applicable Internal Revenue Code formulas, which is primarily based upon net income. No such dividend was required to be paid in fiscal 2009, 2008 or 2007.

On March 23, 1999, the Board of Directors adopted a policy of paying regular cash dividends in respect of the Common Stock of the Company, payable in equal semi-annual installments. Pursuant to said policy, the Board of Directors declared and the Company paid cash dividends on its Common Stock as follows:

Declaration Date	Record Date	Payment Date	Per Share Amount
April 2, 2007	April 18, 2007	April 26, 2007	$ .09
October 3, 2007	October 18, 2007	October 25, 2007	$ .09
April 2, 2008	April 18, 2008	April 28, 2008	$ .10
October 8, 2008	October 23, 2008	October 30, 2008	$ .10

On March 31, 2009, the Company announced that it would temporarily suspend its previously announced Common Stock dividend policy and not declare or pay a semi-annual dividend in April 2009. Subsequently, the Board of Directors deemed it appropriate to continue the suspension and did not declare or pay a cash dividend in October 2009.

The declaration, payment and amount of such dividends in the future are within the discretion of the Board of Directors and will depend upon our earnings, capital requirements, financial condition and other relevant factors. So long as any Series A Preferred Shares remain outstanding, unless the full dividends for the most recent dividend payment date have been paid or declared, no dividends may be paid or declared on the Company's Common Stock.

On May 15, 2003, The Company's Board of Directors authorized the purchase of up to 450,000 shares of its Common Stock in the open market, from time to time, depending upon prevailing market conditions, thereby increasing the maximum number of shares which may be purchased by the Company from 1,950,000 shares of Common Stock to 2,400,000 shares of Common Stock. From 1990 through December 31, 2006, the Company has purchased a total of 1,898,909 shares of its Common Stock. During fiscal years 2007, 2008 and 2009 we did not purchase any shares, and at December 31, 2009 there were 501,091 shares of Common Stock which may yet be purchased under our stock repurchase plan.

Equity Compensation Plans

See Part III, Item 12 for information concerning the Company's equity compensation plans.

ITEM 6. Selected Financial Data

Not Applicable

ITEM 7. Managements' Discussion and Analysis of Financial Condition and Results of Operations.

The following discussion and analysis is intended to provide a better understanding of the consolidated financial condition and results of operations of Berkshire Bancorp Inc. and subsidiaries for the fiscal years ended December 31, 2009, 2008 and 2007. All references to earnings (loss) per share, unless stated otherwise, refer to loss per basic shares for the 2009 and 2008 fiscal years, and earnings per diluted shares for the 2007 fiscal year. The discussion should be read in conjunction with the consolidated financial statements and related notes (Notes located in Item 8 herein). Reference is also made to Part I, Item 1 "Business" herein.

Segments

Management has determined that the Company through its wholly owned bank subsidiary, the Bank, operates in one business segment, community banking. The Bank's principal business activity consists of gathering deposits from the general public and investing those deposits in residential and commercial mortgage loans and commercial non-mortgage loans, both unsecured and secured by personal property. In addition, the Bank invests those deposits in debt obligations issued by the U.S. Government, its agencies, business corporations and mortgage-backed securities.

Series A Preferred Shares

On October 31, 2008, the Company sold an aggregate of 60,000 Series A Preferred Shares at $1,000 per share, or $60 million in the aggregate, to the Company's Chairman of the Board and majority stockholder, and two non-affiliated investors. Each Series A Preferred Share bears non-cumulative cash dividends at the rate of 8% per annum, payable quarterly, is mandatorily convertible into 123.153 shares of our Common Stock on October 31, 2011, unless previously redeemed, and is redeemable at the option of the Company between April 30, 2009 and November 1, 2010 at a redemption price of $1,100. No Series A Preferred Shares have been redeemed to date. So long as any share of Series A Preferred Shares remains outstanding, unless the full dividends for the most recent dividend payment date have been paid or declared, no dividends may be paid or declared on the Company's Common Stock. (See Note A of Notes to Consolidated Financial Statements for further discussion of Series A Preferred Shares).

Critical Accounting Policies, Judgments and Estimates

The accounting and reporting policies of the Company conform with accounting principles generally accepted in the United States of America ("U.S. GAAP") and general practices within the financial services industry. The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and the accompanying notes. Actual results could differ from those estimates.

The Company considers that the determination of the allowance for loan losses involves a higher degree of judgment and complexity than any of its other significant accounting estimates. The allowance for loan losses is calculated with the objective of maintaining a reserve level believed by management to be sufficient to absorb estimated credit losses. Management's determination of the adequacy of the allowance is based on periodic evaluations of the loan portfolio and other relevant factors. However, this evaluation is inherently subjective as it requires material estimates, including, among others, expected default probabilities, loss given default, the amounts and timing of expected future cash flows on impaired loans, mortgages, and general amounts for historical loss experience. The process also considers economic conditions, uncertainties in estimating losses and inherent risks in the loan portfolio. All of these factors may be susceptible to significant change. To the extent actual outcomes differ from management estimates, additional provisions for loan losses may be required that would adversely impact earnings in future periods. See further discussion of the allowance for loan losses in "Provision for Loan Losses."

In accordance with Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") 350, "Intangibles-Goodwill and Other", the Company discontinued the amortization of goodwill resulting from acquisitions. Goodwill is subject to impairment testing at least annually to determine whether write-downs of the recorded balances are necessary. The Company tests for impairment based on the goodwill maintained at the Bank. A fair value is determined for each reporting unit based on at least one of three various market valuation methodologies. If the fair value of the reporting units exceed the book value, no write-down of recorded goodwill is necessary. If the fair value of the reporting unit is less, an expense may be required on the Company's books to write down the related goodwill to the carrying value. As of December 31, 2009, the goodwill was evaluated for impairment with no recognition of impairment considered necessary. The fair value of the reporting unit was substantially greater than the carrying value. However, there can be no guarantees that impairment will not be recognized in future periods.

The Company recognizes deferred tax assets and liabilities for the future tax effects of temporary differences, net operating loss carryforwards and tax credits. Deferred tax assets are subject to management's judgment based upon available evidence that future realization is more likely than not. If management determines that the Company may be unable to realize all or part of net deferred tax assets in the future, a direct charge to income tax expense may be required to reduce the recorded value of the net deferred tax asset to the expected realizable amount.

The Company evaluates unrealized losses on securities to determine if any reduction in the fair value is other than temporary. This amount will continue to be dependent on market conditions, the occurrence of certain events or changes in circumstances of the issuer of the security, and the Company's intent and ability to hold impaired investments at the time the valuation is made. If management determines that an impairment in the investment's value is other than temporary, earnings would be charged.

The Company is required to disclose the estimated fair value of its assets and liabilities considered to be financial instruments. For the Company, as for most financial institutions, the majority of its assets and liabilities are considered financial instruments. The Company values those financial assets and financial liabilities in accordance with ASC Topic 820 "Fair Value Measurements and Disclosures." ASC Topic 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, establishes a framework for measuring fair value, and expands disclosures about fair value measurement.

Financial assets and financial liabilities reported at fair value are required to be measured based on the following alternatives: (1) quoted prices in active markets for identical financial instruments (level 1), (2) significant other observable inputs (level 2), or (3) significant unobservable inputs (level 3). Judgement is required in selecting the appropriate level to be used to determine fair value. The majority of the investments classified as Available for Sale, were measured using level 2 inputs, which requires judgement to determine the fair value. The auction rate securities held in the investment portfolio, were measured using level 3 inputs due to the inactive market for these securities.

Discussion of Financial Condition and Results of Operations

Overview

Fiscal Year Ended December 31, 2009 Compared to Fiscal Year Ended December 31, 2008. Net loss allocated to common stockholders for the fiscal year ended December 31, 2009 was $7.0 million, or $1.00 per common share, compared to a net loss allocated to common stockholders of $79.9 million, or $11.45 per common share for the fiscal year ended December 31, 2008. Net loans decreased by approximately 8%. Investment securities increased by approximately 20% and total assets decreased by approximately 4%.

	As of and for the Fiscal Year Ended December 31,		
	2009	2008	% Inc/(Dec)
	(In millions, except per share data and percentages and bank branch information)		
Total Assets	$ 909.3	$ 943.7	(4)%
Loans, net	418.9	457.5	(8)%
Investment Securities	357.8	297.9	20%
Total Liabilities	824.0	877.8	(6)%
Deposits	713.4	726.1	(2)%
Borrowings	103.7	127.5	(19)%
Stockholders' Equity	85.2	66.0	29%
Total Income	46.1	60.3	(24)%
Interest Income	45.9	59.6	(23)%
Total Expense	61.6	146.0	(58)%
Interest Expense	17.1	30.5	(44)%
Net Interest Income	28.8	29.1	(1)%
Net (Loss)	(7.0)	(79.9)	(91)%
(Loss) Per Common Share	(1.00)	(11.45)	(91)%
Bank Branches	13	12	-

Fiscal Year Ended December 31, 2008 Compared to Fiscal Year Ended December 31, 2007. Net loss allocated to common stockholders for the fiscal year ended December 31, 2008 was $79.9 million, or $11.45 per common share, compared to net income of $5.4 million, or $.76 per diluted common share, for the fiscal year ended December 31, 2007. Net loans increased by approximately 6%. Investment securities and total assets decreased by approximately 50% and 16%, respectively.

	As of and for the Fiscal Year Ended December 31,		
	2008	2007	% Inc/(Dec)
	(In millions, except per share data and percentages and bank branch information)		
Total Income	60.3	60.2	0%
Interest Income	59.6	58.5	2%
Total Expense	146.0	52.5	178%
Interest Expense	30.5	37.8	(19)%
Net Interest Income	29.1	20.7	41%
Net Income (Loss)	(79.9)	5.4	(1,580)%
Diluted Income (Loss) Per Share	(11.45)	.76	(1,607)%
Bank Branches	12	12	-

The Company's average balances, interest, and average yields are set forth on the following table (in thousands, except percentages):

	Twelve Months Ended December 31, 2009			Twelve Months Ended December 31, 2008			Twelve Months Ended December 31, 2007		
	Average Balance	Interest and Dividends	Average Yield/Rate	Average Balance	Interest and Dividends	Average Yield/Rate	Average Balance	Interest and Dividends	Average Yield/Rate
INTEREST-EARNING ASSETS:									
Loans (1)	$ 448,394	$ 29,777	6.63%	$ 461,678	$ 32,754	7.09%	$ 389,520	$ 29,804	7.65%
Investment securities	312,966	15,506	4.95	464,927	25,456	5.48	558,742	27,178	4.86
Other (2)(5)	61,496	639	1.04	54,157	1,380	2.55	31,678	1,553	4.90
Total interest-earning assets	822,856	45,922	5.58	980,762	59,590	6.08	979,940	58,535	5.97
Noninterest-earning assets	58,828			55,244			46,070		
Total Assets	$ 881,684			$ 1,036,006			$ 1,026,010		
INTEREST-BEARING LIABILITIES:									
Interest bearing deposits	204,629	2,316	1.13	287,772	7,645	2.66	291,049	10,338	3.55
Time deposits	426,892	9,921	2.32	456,803	17,323	3.79	449,754	21,745	4.83
Other borrowings	115,869	4,866	4.20	127,343	5,555	4.36	103,112	5,710	5.54
Total interest-bearing liabilities	747,390	17,103	2.29	871,918	30,523	3.50	843,915	37,793	4.48
Demand deposits	56,544			54,452			50,647		
Noninterest-bearing liabilities	8,701			9,077			12,285		
Stockholders' equity (5)	69,049			100,559			119,163		
Total liabilities and stockholders' equity	$ 881,684			$ 1,036,006			$ 1,026,010		
Net interest income		$ 28,819			$ 29,067			$ 20,742	
Interest-rate spread (3)			3.29%			2.58%			1.49%
Net interest margin (4)			3.50%			2.96%			2.12%
Ratio of average interest-earning assets to average interest bearing liabilities	1.10			1.12			1.16		

(1) Includes nonaccrual loans.
(2) Includes interest-bearing deposits, federal funds sold and securities purchased under agreements to resell.
(3) Interest-rate spread represents the difference between the average yield on interest-earning assets and the average cost of interest bearing liabilities.
(4) Net interest margin is net interest income as a percentage of average interest-earning assets.
(5) Average balances for Berkshire Bancorp Inc. (parent only) have been calculated on a monthly basis.

Changes in net interest income may also be analyzed by segregating the volume and rate components of interest income and interest expense. The following tables set forth certain information regarding changes in interest income and interest expense of the Company for the years indicated. For each category of interest-earning assets and interest-bearing liabilities, information is provided on changes attributable to (1) changes in rate (change in rate multiplied by prior volume), (2) changes in volume (changes in volume multiplied by prior rate) and (3) changes in rate-volume (change in rate multiplied by change in volume) (in thousands):

	Twelve Months Ended December 31, 2009 Versus Twelve Months Ended December 31, 2008 Increase (Decrease) Due To		
	Rate	Volume	Total
Interest-earning assets:			
Loans	$ (2,124)	$ (853)	$ (2,977)
Investment securities	(2,464)	(7,486)	(9,950)
Other	(818)	77	(741)
Total	(5,406)	(8,262)	(13,668)
Interest-bearing liabilities:			
Deposit accounts:			
Interest bearing deposits	(4,403)	(926)	(5,329)
Time deposits	(6,715)	(687)	(7,402)
Other borrowings	(204)	(485)	(689)
Total	(11,322)	(2,098)	(13,420)
Net interest income	$ 5,916	$ (6,164)	$ (248)

	Twelve Months Ended December 31, 2008 Versus Twelve Months Ended December 31, 2007 Increase (Decrease) Due To		
	Rate	Volume	Total
Interest-earning assets:			
Loans	$ (2,181)	$ 5,131	$ 2,950
Investment securities	3,464	(5,186)	(1,722)
Other	(744)	571	(173)
Total	539	516	1,055
Interest-bearing liabilities:			
Deposit accounts:			
Interest bearing deposits	(2,590)	(103)	(2,693)
Time deposits	(4,677)	255	(4,422)
Other borrowings	(1,217)	1,062	(155)
Total	(8,484)	1,214	(7,270)
Net interest income	$ 9,023	$ (698)	$ 8,325

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Provision for Loan Losses.

The allowance for loan losses is the estimated amount considered necessary to cover credit losses inherent in the loan portfolio at the balance sheet date. The allowance is established through the provision for loan losses that is charged against income. In determining the allowance for loan losses, management makes significant estimates which involve a high degree of judgment, subjectivity of the assumptions utilized, and potential for changes in the economic environment that could result in changes to the amount of the recorded allowance for loan losses.

The allowance for loan losses has been determined in accordance with U.S. GAAP, principally FASB ASC 450, "Contingencies", ("ASC 450") and FASB ASC 310, "Receivables", ("ASC 310"). Under the above accounting principles, we are required to maintain an allowance for probable losses at the balance sheet date. We are responsible for the timely and periodic determination of the amount of the allowance required. Management believes that the allowance for loan losses is adequate to cover specifically identifiable losses, as well as estimated losses inherent in our portfolio for which certain losses are probable but not specifically identifiable.

Management performs a monthly evaluation of the adequacy of the allowance for loan losses. The analysis of the allowance for loan losses has two components: specific and general allocations. Specific allocations are made for loans determined to be impaired. Impairment is measured by determining the present value of expected future cash flows or, as a practical expedient for collateral-dependent loans, the fair value of the collateral adjusted for market conditions and selling expenses. The Bank considers its investment in one-to-four family real estate loans and consumer loans to be smaller balance homogeneous loans and therefore excluded from separate identification for evaluation of impairment. These homogeneous loan groups are evaluated for impairment on a collective basis under FASB ASC 310.

The general allocation is determined by segregating the remaining loans by type of loan, risk weighting (if applicable) and payment history. Management also analyzes historical loss experience, delinquency trends, general economic conditions, geographic concentrations, and industry and peer comparisons. This analysis establishes factors that are applied to the loan segments to determine the amount of the general allocations. This evaluation is inherently subjective as it requires material estimates that may be susceptible to significant revisions based upon changes in economic and real estate market conditions. Actual loan losses may be significantly more than the allowance for loan losses management has established which could have a material negative effect on the Company's financial results.

On a monthly basis, the Bank's management committee reviews the current status of various loan assets in order to evaluate the adequacy of the allowance for loan losses. In this evaluation process, specific loans are analyzed to determine their potential risk of loss. This process includes all loans, concentrating on non-accrual and classified loans. Each non-accrual or classified loan is evaluated for potential loss exposure. Any shortfall results in a recommendation of a specific allowance if the likelihood of loss is evaluated as probable. To determine the adequacy of collateral on a particular loan, an estimate of the fair market value of the collateral is based on the most current appraised value available. This appraised value is then reduced to reflect estimated liquidation expenses.

As a substantial amount of our loan portfolio is collateralized by real estate, appraisals of the underlying value of property securing loans are critical in determining the amount of the allowance required for specific loans. Assumptions for appraisal valuations are instrumental in determining the value of properties. Overly optimistic assumptions or negative changes to assumptions could significantly impact the valuation of a property securing a loan and the related allowance determined. The assumptions supporting such appraisals are carefully reviewed by management to determine that the resulting values reasonably reflect amounts realizable on the related loans. Based on the composition of our loan portfolio, management believes the primary risks are increases in interest rates, a decline in the economy, generally, and a decline in real estate market values in the New York metropolitan area. Any one or combination of these events may adversely affect our loan portfolio resulting in increased delinquencies, loan losses and future levels of loan loss provisions. Management believes the allowance for loan losses reflects the inherent credit risk in our portfolio, the level of our non-performing loans and our charge-off experience.

A loan is considered nonperforming when it becomes delinquent ninety days or when other adverse factors become known to us. We generally order updated appraisals from independent third party licensed appraisers at the time the loan is identified as nonperforming. Depending upon the property type, we receive appraisals within thirty to ninety days from the date the appraisals are ordered. Upon receipt of the appraisal, which is discounted by us to take account of estimated selling and other holding costs, we compare the adjusted appraisal amount to the carrying amount of the real estate dependent loan and record any impairment through the allowance for loan loss at that time.

As the majority of our real estate dependent loans are concentrated in the New York City metropolitan area, we do not make adjustments to the appraisals for this concentration. We do not increase the appraised value of any property. Any adjustments we make to the appraisals are to decrease the appraised value due to selling and other holding costs.

Although management believes that we have established and maintained the allowance for loan losses at adequate levels, additions may be necessary if future economic and other conditions differ substantially from the current operating environment. Although management uses what it believes is the best information available, the level of the allowance for loan losses remains an estimate that is subject to significant judgment and short-term change. In addition, the Federal Deposit Insurance Corporation, New York State Banking Department, and other regulatory bodies, as an integral part of their examination process, will periodically review our allowance for loan losses. Such agencies may require us to recognize adjustments to the allowance based on its judgments about information available to them at the time of their examination.

Results of Operations Fiscal Year Ended December 31, 2009 Compared to Fiscal Year Ended December 31, 2008.

Net Loss Allocated to Common Stockholders. Net loss allocated to common stockholders for the fiscal year ended December 31, 2009 was $7.0 million, or $1.00 per common share, as compared to a net loss of $79.9 million, or $11.45 per common share, for the fiscal year ended December 31, 2008. The net loss allocated to common stockholders in fiscal 2009 was primarily due to the other than temporary impairment ("OTTI") charges on securities of $17.4 million, or $2.47 per common share, and dividends on our Series A Preferred Stock of $4.8 million, or $.68 per common share, partially offset by the benefit for income taxes of $13.2 million, or, $1.87 per common share.

The net loss in fiscal 2008 was primarily due to the OTTI charges on securities of $94.3 million or $13.37 per common share. The OTTI charge was due to our investment, directly and indirectly through auction rate securities, in preferred shares of Fannie Mae and Freddie Mac. These government sponsored agencies were placed into conservatorship by the federal government in September 2008 resulting in, among other things, the suspension of dividend payments.

In January 2009, the Bank filed an arbitration proceeding with the Financial Industry Regulatory Authority against the issuing financial institution of the auction rate securities in our investment portfolio. The outcome of the arbitration process, postponed from a scheduled date in March 2010 and rescheduled for the fall of 2010 and the amount we may recover, if any, is uncertain at this time.

The Company's net income is largely dependent on interest rate levels, the demand for the Company's loan and deposit products and the strategies employed to manage the interest rate and other risks inherent in the banking business.

Interest Income. Total interest income for the fiscal year ended December 31, 2009 decreased by $13.7 million to $45.9 million from $59.6 million for the fiscal year ended December 31, 2008. The decrease in total interest income in fiscal 2009 was primarily due to the $157.9 million decrease in the average amounts of interest-earning assets to $822.9 million from $980.8 million during fiscal 2008 and the 50 basis point decrease in the average yields earned on such assets to 5.58% from 6.08% during fiscal years 2009 and 2008, respectively.

The following table presents the composition of interest income for the indicated periods:

	Fiscal 2009		Fiscal 2008	
	Interest Income	% of Total	Interest Income	% of Total
	(In thousands, except percentages)			
Loans	$ 29,777	64.84%	$ 32,754	54.96%
Investment Securities	15,506	33.77	25,456	42.72
Other	639	1.39	1,380	2.32
Total Interest Income	$ 45,922	100.00%	$ 59,590	100.00%

Loans, which are inherently risky and therefore command a higher return than our portfolio of investment securities and other interest-earning assets, increased to 54.49% of total average interest-earning assets during fiscal 2009 from 47.07% of total interest-earning assets during fiscal 2008. The average amounts of investment securities decreased to 38.03% of total average interest-earning assets during fiscal 2009 from 47.40% of total interest-earning assets during fiscal 2008. While we actively seek to originate new loans with qualified borrowers who meet the Bank's underwriting standards, our strategy has been to maintain those standards, sacrificing some current income to avoid possible large future losses in the loan portfolio.

At December 31, 2009, our portfolio of investment securities included approximately $78.9 million at cost of auction rate securities and approximately $26.5 million at cost of corporate notes, including single issuer and pooled trust preferred securities, for which an OTTI charge has not been recorded in our financial statements. The fair value of these securities, presently $66.9 million and $18.9 million, respectively, could be negatively impacted in the future. Were this to occur, we may be required to reflect a write down of certain of our securities in future periods as a charge to earnings if any of these securities are deemed to be other than temporarily impaired. Such impairment charge could be material to our results of operations.

As required by FASB ASC 320, "Investments-Debt and Equity Securities", securities are classified into three categories: trading, held-to-maturity and available-for-sale. Securities that are bought and held principally for the purpose of selling them in the near term are classified as trading securities and are reported at fair value with unrealized gains and losses included in trading account activities in the statement of income. Securities that the Bank has the positive intent and ability to hold to maturity are classified as held-to-maturity and reported at amortized cost. All other securities are classified as available-for-sale. Available-for-sale securities are reported at fair value with unrealized gains and losses included, on an after-tax basis, as a separate component of stockholders' equity. The Company does not have a trading securities portfolio and has no current plans to maintain such a portfolio in the future. The Company generally classifies all newly purchased debt securities as available for sale in order to maintain the flexibility to sell those securities if the need arises. The Bank has a limited portfolio of securities classified as held to maturity, represented principally by securities purchased a number of years ago.

Federal Home Loan Bank Stock. The Bank owns stock of the FHLBNY which is necessary for it to be a member of the FHLBNY. Membership requires the purchase of stock equal to 0.20% of the Bank's mortgage related assets (investments and loans) plus 4.5% of the outstanding borrowings. The stock is redeemable at par, therefore, its cost is equivalent to its redemption value. The Bank's ability to redeem FHLBNY shares is dependent upon the redemption practices of the FHLBNY. At December 31, 2009, the FHLBNY neither placed restrictions on redemption of shares in excess of a member's required investment in stock, nor stated that it will cease paying dividends. The Bank did not consider this asset impaired at either December 31, 2009 or 2008.

The following table presents the composition of interest-earning assets for the indicated periods:

	Fiscal 2009		Fiscal 2008	
	Average Amount	% of Total	Average Amount	% of Total
	(In thousands, except percentages)			
Loans	$ 448,394	54.50%	$ 461,678	47.08%
Investment Securities	312,966	38.03	464,927	47.40
Other	61,496	7.47	54,157	5.52
Total Interest-Earning Assets	$ 822,856	100.00%	$ 980,762	100.00%

Interest Expense. Total interest expense for the fiscal year ended December 31, 2009 deceased by $13.4 million to $17.1 million from $30.5 million for the fiscal year ended December 31, 2008. The decrease in total interest expense was due to the $124.5 million decrease in the average amounts of interest-bearing liabilities to $747.4 million during fiscal 2009 from $871.9 million during fiscal 2008 and the 121 basis point decrease in the average rates paid on such liabilities to 2.29% from 3.50% during fiscal years 2009 and 2008, respectively.

The following table presents the composition of interest expense for the indicated periods:

	Fiscal 2009		Fiscal 2008	
	Interest Expense	% of Total	Interest Expense	% of Total
	(In thousands, except percentages)			
Interest-Bearing Deposits	$ 2,316	13.54%	$ 7,645	25.05%
Time Deposits	9,921	58.01	17,323	56.75
Other Borrowings	4,866	28.45	5,555	18.20
Total Interest Expense	$ 17,103	100.00%	$ 30,523	100.00%

The following table presents the composition of interest-bearing liabilities for the indicated periods:

	Fiscal 2009		Fiscal 2008	
	Average Amount	% of Total	Average Amount	% of Total
	(In thousands, except percentages)			
Interest-Bearing Deposits	$ 204,629	27.38%	$ 287,772	33.00%
Time Deposits	426,892	57.12	456,803	52.40
Other Borrowings	115,869	15.50	127,343	14.60
Total Interest-Bearing Liabilities	$ 747,390	100.00%	$ 871,918	100.00%

Net Interest Income. The Company's primary source of revenue is net interest income, or the difference between interest income earned on interest-earning assets, such as loans and investment securities, and interest expense on interest-bearing liabilities such as deposits and borrowings. The amount of interest income is dependent upon many factors including: (i) the amount of interest-earning assets that the Company can maintain based upon its funding sources; (ii) the relative amounts of interest-earning assets versus interest-bearing liabilities; and (iii) the difference between the yields earned on those assets and the rates paid on those liabilities. Non-performing loans adversely affect net interest income because they must still be funded by interest-bearing liabilities, but they do not provide interest income. Furthermore, when we designate an asset as non-performing, all interest which has been accrued but not actually received is deducted from current period income, further reducing net interest income.

For the fiscal year ended December 31, 2009, net interest income decreased by approximately $250,000 to $28.8 million from $29.1 million for the fiscal year ended December 31, 2008. The decrease in net interest income was due to the decrease in the average amounts of interest-earning assets to $822.9 million during fiscal year 2009 from $980.8 million during fiscal year 2008 and the decrease in the average yields earned on such assets to 5.58% from 6.08% during fiscal years 2009 and 2008, respectively. The decrease in net interest income was substantially offset by the decrease in the average amounts of interest-bearing liabilities to $747.4 million during fiscal year 2009 from $871.9 million during fiscal year 2008 and the decrease in the average rates paid on such liabilities to 2.29% from 3.50% during fiscal years 2009 and 2008, respectively. The Company's interest-rate spread, the difference between the average yield on interest-earning assets and the average cost of interest-bearing liabilities, increased by 71 basis points to 3.29% during fiscal 2009 from 2.58% during fiscal 2008.

Net Interest Margin. Net interest margin, or net interest income as a percentage of average interest-earning assets, increased by 54 basis points to 3.50% during fiscal 2009 from 2.96% during fiscal 2008. We seek to secure and retain customer deposits with competitive products and rates, while making strategic use of the prevailing interest rate environment to borrow funds at what we believe to be attractive rates. We invest such deposits and borrowed funds in what we believe to be a prudent mix of fixed and adjustable rate loans, investment securities and short-term interest-earning assets. The increase in net interest margin during fiscal 2009 was primarily due to the increase in the average amounts of higher yielding loans as a percentage of our total mix of interest-earning assets.

Non-Interest Income. Non-interest income consists primarily of realized gains on sales of marketable securities and service fee income. For the fiscal year ended December 31, 2009, total non-interest income decreased by $561,000 to $197,000 from $758,000 for the fiscal year ended December 31, 2008.

The following table presents the composition of non-interest income for the indicated periods:

	Fiscal 2009		Fiscal 2008	
	Non-Interest Income	% of Total	Non-Interest Income	% of Total
	(In thousands, except percentages)			
Service Charges on Deposits	$ 490	248.73%	$ 585	77.18%
Investment Securities Losses	(860)	(436.55)	(685)	(90.37)
Other	567	287.82	858	113.19
Total Non-Interest Income	$ 197	100.00%	$ 758	100.00%

Non-Interest Expense. Non-interest expense includes salaries and employee benefits, occupancy and equipment expenses, legal and professional fees, other operating expenses associated with the day-to-day operations of the Company and OTTI charges on investment securities. Total non-interest expense for the fiscal years ended December 31, 2009 and 2008 was $35.2 million and $110.6 million, respectively, including OTTI charges on investment securities of $17.4 million and $94.3 million, respectively. Excluding the OTTI charges, total non-interest expense during fiscal 2009 increased by $1.4 million to $17.7 million from $16.3 million during fiscal 2008. This increase was primarily due to the increase of $846,000 in our FDIC assessment and expenses related to the opening of a new bank branch.

The following table presents the composition of non-interest expense for the indicated period.

	Fiscal 2009		Fiscal 2008	
	Non-Interest Expense	% of Total	Non-Interest Expense	% of Total
	(In thousands, except percentages)			
Salaries and Employee Benefits	$ 9,517	27.06%	$ 9,366	8.46%
Net Occupancy Expense	2,150	6.11	2,079	1.88
Equipment Expense	378	1.07	386	0.35
FDIC Assessment	1,928	5.48	1,082	0.98
Data Processing Expense	452	1.29	442	0.40
Other than temporary impairment charges on securities	17,435	49.58	94,346	85.29
Other	3,311	9.41	2,915	2.64
Total Non-Interest Expense	$ 35,171	100.00%	$ 110,616	100.00%

Provision for Income Tax. For the fiscal year ended December 31, 2009, the Company recorded a benefit for income taxes of $13.2 million compared to a benefit for income taxes of $5.8 million for the fiscal year ended December 31, 2008. The tax benefit in fiscal 2009 includes the benefit from the actual losses realized on sales of investment securities.

The recorded tax benefits in 2008 relates to the OTTI charge related to the Lehman Brothers corporate note which was treated as an ordinary loss under the current federal tax code when Lehman Brothers filed for bankruptcy in September 2008. The OTTI charge related to Fannie Mae and Freddie Mac securities, both direct investments and through auction rate securities, were considered capital losses under the federal tax code. A valuation allowance was recorded on the amount of capital losses in excess of available capital gains. With the passage by the U.S. Congress of the Emergency Economic Stabilization Act in October 2008, the nature of the Fannie Mae and Freddie Mac capital losses were changed to ordinary losses. Due to this change in the tax law, we carried back as much loss as could be utilized and recognized a deferred tax benefit for the remainder.

Results of Operations Fiscal Year Ended December 31, 2008 Compared to Fiscal Year Ended December 31, 2007.

Net Income (Loss). Net loss for the fiscal year ended December 31, 2008 was $79.9 million, or $11.45 per share, as compared to net income of $5.4 million, or $.76 per share, for the fiscal year ended December 31, 2007. The net loss in fiscal 2008 was primarily due to the other than temporary impairment charges on securities of $94.3 million or $13.37 per share. The other than temporary impairment charge was due to our investment, directly and indirectly through auction rate securities, in preferred shares of Fannie Mae and Freddie Mac. These government sponsored agencies were placed into conservatorship by the federal government in September 2008 resulting in, among other things, the suspension of dividend payments on our common stock.

Interest Income. Total interest income for the fiscal year ended December 31, 2008 increased by $1.1 million to $59.6 million from $58.5 million for the fiscal year ended December 31, 2007. The increase in interest income in fiscal 2008 was primarily due to the increase in the average amount of higher yielding loans and the decrease in lower yielding investment securities as a percentage of our total interest-earning assets.

The following table presents the composition of interest income for the indicated periods:

	Fiscal 2008		Fiscal 2007	
	Interest Income	% of Total	Interest Income	% of Total
	(In thousands, except percentages)			
Loans	$ 32,754	54.96%	$ 29,804	50.92%
Investment Securities	25,456	42.72	27,178	46.43
Other	1,380	2.32	1,553	2.65
Total Interest Income	$ 59,590	100.00%	$ 58,535	100.00%

Loans grew to 54.96% of our total average interest-earning assets in fiscal 2008 from 50.92% in fiscal 2007. While we actively seek to originate new loans with qualified borrowers who meet the Bank's underwriting standards, our long-term strategy has been to maintain those standards, sacrificing some current income to avoid possible large future losses in the loan portfolio.

The following table presents the composition of interest-earning assets for the indicated periods:

	Fiscal 2008			Fiscal 2007		
		Average Amount	% of Total		Average Amount	% of Total
	(In thousands, except percentages)					
Loans	$	461,678	47.08%	$	389,520	39.75%
Investment Securities		464,927	47.40		558,742	57.02
Other		54,157	5.52		31,678	3.23
Total Interest-Earning Assets	$	980,762	100.00%	$	979,940	100.00%

Interest Expense. Total interest expense for the fiscal year ended December 31, 2008 decreased by $7.3 million to $30.5 million from $37.8 million for the fiscal year ended December 31, 2007. The decrease in interest expense was due to the decrease in the average rates paid on such liabilities, 3.50% and 4.48% in fiscal years 2008 and 2007, respectively, partially offset by the $28.0 million increase in the average amount of total interest-bearing liabilities during fiscal year 2008.

The following table presents the composition of interest expense for the indicated periods:

	Fiscal 2008			Fiscal 2007		
		Interest Expense	% of Total		Interest Expense	% of Total
	(In thousands, except percentages)					
Interest-Bearing Deposits	$	7,645	25.05%	$	10,338	27.35%
Time Deposits		17,323	56.75		21,745	57.54
Other Borrowings		5,555	18.20		5,710	15.11
Total Interest Expense	$	30,523	100.00%	$	37,793	100.00%

The following table presents the composition of interest-bearing liabilities for the indicated periods:

	Fiscal 2008		Fiscal 2007	
	Average Amount	% of Total	Average Amount	% of Total
	(In thousands, except percentages)			
Interest-Bearing Deposits	$ 287,772	33.00%	$ 291,049	34.49%
Time Deposits	456,803	52.40	449,754	53.29
Other Borrowings	127,343	14.60	103,112	12.22
Total Interest-Bearing Liabilities	$ 871,918	100.00%	$ 843,915	100.00%

Net Interest Income. The Company's primary source of revenue is net interest income, or the difference between interest income on earning assets, such as loans and investment securities, and interest expense on interest-bearing liabilities such as deposits and borrowings.

For the fiscal year ended December 31, 2008, net interest income increased by approximately $8.3 million to $29.1 million from $20.7 million for the fiscal year ended December 31, 2007. The year over year increase in net interest income was the result of the 98 basis point decrease in the average rates paid on the average amount of total interest-bearing liabilities and the 11 basis point increase in the average yields earned on the average amount of total interest-earning assets. The Company's interest-rate spread, the difference between the average yield on interest-earning assets and the average cost of interest-bearing liabilities, widened by 109 basis points to 2.58% during fiscal 2008 from 1.49% during fiscal 2007.

Net Interest Margin. Net interest margin, or net interest income as a percentage of average interest-earning assets, increased by 84 basis points to 2.96% during fiscal 2008 from 2.12% during fiscal 2007. We seek to secure and retain customer deposits with competitive products and rates, and to make strategic use of the prevailing interest rate environment to borrow funds at what we believe to be attractive rates. We invest such deposits and borrowed funds in a prudent mix of fixed rate and adjustable rate loans, investment securities and short-term interest-earning assets which provided an aggregate average yield of 6.08% and 5.97% in fiscal 2008 and 2007, respectively.

The average amount of loans increased by $72.2 million to $461.7 million during fiscal 2008 from $389.5 million during fiscal 2007, though the average yield on such loans decreased by 56 basis points to 7.09% in fiscal 2008 from 7.65% in fiscal 2007. The average amount of investment securities decreased by $93.8 million to $464.9 million in fiscal 2008 from $558.7 million in fiscal 2007 and the average yield on investment securities improved by 62 basis points, to 5.48% in 2008 from 4.86% in 2007. The average amount of other interest-earning assets, primarily cash and short-term investments, increased by $22.5 million to $54.2 million in 2008 from $31.7 million in 2007 and returned an average yield of 2.55% and 4.90% during the fiscal years ended December 31, 2008 and 2007, respectively.

Non-Interest Income. Non-interest income consists primarily of realized gains on sales of marketable securities and service fee income. For the fiscal year ended December 31, 2008, total non-interest income decreased by $901,000 to $758,000 from $1.66 million for the fiscal year ended December 31, 2007. The decrease is primarily due to realized loss of $685,000 on sales of investment securities during fiscal 2008.

The following table presents the composition of non-interest income for the indicated periods:

	Fiscal 2008		Fiscal 2007	
	Non-Interest Income	% of Total	Non-Interest Income	% of Total
	(In thousands, except percentages)			
Service Charges on Deposits	$ 585	77.18%	$ 658	39.66%
Investment Securities (Losses) Gains	(685)	(90.37)	86	5.18
Other	858	113.19	915	55.16
Total Non-Interest Income	$ 758	100.00%	$ 1,659	100.00%

Non-Interest Expense. Non-interest expense includes salaries and employee benefits, occupancy and equipment expenses, legal and professional fees and other operating expenses associated with the day-to-day operations of the Company. Total non-interest expense for the fiscal year ended December 31, 2008, including the other than temporary impairment charges on securities of $94.3 million, increased by $96.3 million to $110.6 million from $14.3 million for the fiscal year ended December 31, 2007. Excluding the other than temporary impairment charges, total non-interest expense for fiscal 2008 increased by $2.0 million to $16.3 million. This increase was primarily due to the increase of approximately $1.0 million in our FDIC assessment.

The following table presents the composition of non-interest expense for the indicated period.

	Fiscal 2008		Fiscal 2007	
	Non-Interest Expense	% of Total	Non-Interest Expense	% of Total
	(In thousands, except percentages)			
Salaries and Employee Benefits	$ 9,366	8.46%	$ 8,971	62.66%
Net Occupancy Expense	2,079	1.88	2,050	14.32
Equipment Expense	386	0.35	80	0.56
FDIC Assessment	1,082	0.98	86	0.60
Data Processing Expense	442	0.40	417	2.91
Other than temporary impairment charges on securities	94,346	85.29	—	
Other	2,915	2.64	2,714	18.95
Total Non-Interest Expense	$ 110,616	100.00%	$ 14,318	100.00%

Provision for Income Tax. For the fiscal year ended December 31, 2008, the Company recorded an income tax benefit of $5.8 million as compared to income tax expense of $2.4 million for the fiscal year ended December 31, 2007. The tax benefit recorded in fiscal 2008 relates to the other than temporary impairment charge on securities, including (i) a Lehman Brothers corporate note, (ii) direct investments in Fannie Mae and Freddie Mac securities, and (iii) indirect investments in Fannie Mae and Freddie Mac securities through our investments in certain auction rate securities and is a carryback claim. The Emergency Economic Stabilization Act of 2008 (the "EESA"), enacted on October 3, 2008, provides for, among other things, the characterization of the losses on direct and indirect investments in Fannie Mae and Freddie Mac securities as ordinary losses which may be used to offset income taxes on ordinary income.

Investment Activities

General. The investment policy of the Bank is designed primarily to provide satisfactory yields while maintaining adequate liquidity, a balance of high quality, diversified investments, and minimal risk. The Bank does not, as a rule, invest in equity securities, however, the Company does invest in some equity securities. The largest component of the Bank's investments, representing more than 50% of total investment securities, are debt securities issued by U.S. Government agencies including Freddie Mac, Fannie Mae or the Government National Mortgage Association ("Ginnie Mae"). The remainder of the Bank's debt securities investments are primarily short term debt securities issued by the United States or its agencies. The Bank maintains a portfolio of high-yield corporate debt securities. Recognizing the higher credit risks of these securities, the Bank underwrites these securities in a manner similar to its loan underwriting procedures.

The following is a summary of held to maturity investment securities:

	December 31, 2009			
	Amortized Cost	Gross unrealized gains	Gross unrealized losses	Fair value
	(In thousands)			
U.S. Government Agencies	$ 340	$ —	$ (3)	$ 337

	December 31, 2008			
	Amortized Cost	Gross unrealized gains	Gross unrealized losses	Fair value
	(In thousands)			
U.S. Government Agencies	$ 360	$ 3	$ (1)	$ 362

The following is a summary of available-for-sale investment securities:

	December 31, 2009			
	Amortized Cost	Gross unrealized gains	Gross unrealized losses	Fair value
	(In thousands)			
U.S. Treasury Notes	$ 50,236	$ 35	$ (65)	$ 50,206
U.S. Government Agencies	76,259	59	(793)	75,525
Mortgage-backed securities	134,810	1,943	(710)	136,043
Corporate notes	19,029	1,011	(2,311)	17,729
Single Issuer Trust Preferred CDO	1,021	—	—	1,021
Pooled Trust Preferred CDO	6,463	—	(6,313)	150
Municipal securities	1,973	198	—	2,171
Auction rate securities	78,895	—	(11,953)	66,942
Marketable equity securities and other	7,648	69	(26)	7,691
Totals	$ 376,334	$ 3,315	$ (22,171)	$ 357,478

	December 31, 2008			
	Amortized Cost	Gross unrealized gains	Gross unrealized losses	Fair value
	(In thousands)			
U.S. Government Agencies	$ 91,429	$ 72	$ (380)	$ 91,121
Mortgage-backed securities	83,882	1,037	(1,061)	83,858
Corporate notes	51,150	112	(13,138)	38,124
Single Issuer Trust Preferred CDO	3,000	—	(1,794)	1,206
Pooled Trust Preferred CDO	10,000	—	(7,006)	2,994
Municipal securities	1,973	125	(495)	1,603
Auction rate securities	101,110	—	(38,030)	63,080
Marketable equity securities and other	16,708	80	(1,238)	15,550
Totals	$ 359,252	$ 1,426	$ (63,142)	$ 297,536

Management uses a multi-factor approach to determine whether each investment security in an unrealized loss position is other-than-temporarily impaired ("OTTI"). An unrealized loss position exists when the current fair value of an investment is less than its amortized cost basis. The valuation factors utilized by management incorporate the ideas and concepts outlined in relevant accounting guidance. These include such factors as:

*The length of time and the extent to which the market value has been less than cost;

*The financial condition of the issuer of the security as well as the near and long-term prospect for the issuer;

*The rating of the security by a national rating agency;

*Historical volatility and movement in the fair market value of the security; and

*Adverse conditions relative to the security, issuer or industry.

The following table shows the outstanding auction rate securities at December 31, 2009 and 2008:

	2009		2008	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
	(In thousands)			
Federal National Mortgage Association Preferred Shares	$ —	$ —	$ 2,223	$ 728
Federal Home Loan Mortgage Corporation Preferred Shares	1,895	1,895	3,904	704
Preferred Shares of Money Center Banks	65,000	53,767	65,000	32,789
Other Assets of Money Center Banks	10,000	9,280	10,000	8,876
Public Utility Debt and Equity Securities	2,000	2,000	15,000	15,000
Other	-	—	4,983	4,983
Totals	$ 78,895	$ 66,942	$ 101,110	$ 63,080

The fair value of the auction rate securities is determined by Management using a discounted cash flow analysis and by valuing the underlying security. The auction rate securities allow for conversion to the underlying preferred security after two failed auctions. As of December 31, 2009, there have been more than two failed auctions for all outstanding auction rate securities. Because of the lack of liquidity in the market for the auction rate securities as compared to the market for the underlying preferred shares and as there is a possibility of an orderly transaction and market for the underlying preferred shares without significant adjustment to their carrying value, we considered the market value of the underlying preferred shares to be more objective and relevant. For the public utility debt and equity securities, the security is collateralized by a mutual fund in which the majority of the investments are public utility debt and equity securities. As this fund, as well as other mutual funds for public utilities, has not been severely impacted by the market dislocation, these funds, and consequently our auction rate securities, have continued to perform. The final market sector, noted above as "other", is collateralized by long term debt of a seasoned issuer that deals in business machinery.

In determining whether there is an OTTI, Management considers the factors noted above. The financial performance indicators we review include, but are not limited to, net earnings, change in liquidity, and change in cash from operating activities, and, for money center banks, the regulatory capital ratios and the allowance for loan losses to the nonperforming loans. Through December 31, 2009, the auction rate securities have continued to pay interest at the highest rate as stipulated in the original prospectus, except for the Federal Home Loan Mortgage Corporation ("Freddie Mac").

In addition to valuing the auction rate securities (ARS) by valuing the collateral, we completed discounted cash flow analyses. In determining the appropriate cash flow analysis for our auction rate securities, the Company reviewed multiple factors and prepared multiple discounted cash flow analyses. The four main factors affecting our cash flow analysis for each ARS were: the expected future interest rate of the ARS, the expected holding period, the expected principal to be received at the end of the holding period, and an assumed discount rate.

In determining the expected future interest rate, we used the current ARS rate at December 31, 2009 and kept the rate constant for future cash flow estimates. The current rates being paid on the majority of these securities are the maximum penalty rate and we believe that these rates will not change significantly in the future. In addition, if the rates do increase or decrease in future periods, we believe that this would increase or decrease the risk profile of these securities which would cause a corresponding change in the discount rate assumption so the discounted cash flow analysis would not be significantly affected by interest rate changes.

In determining the expected holding period of each security using discounted cash flow analysis, we ran several scenarios. These scenarios included holding the security until the trust dissolution date (maturity date), and a five year scenario, inasmuch as we believe five years from December 31, 2009 would be the earliest that the ARS market may resume the normal auction process.

The expected principal that we would receive in the discounted cash flow analysis was based upon two scenarios. These scenarios included receiving par at the maturity date and at the five-year assumed recovery date and receiving the market value of the underlying preferred shares at the maturity date and at the five-year assumed recovery date. Under the terms of the ARS agreements, we would receive the assets of the Trust at the trust dissolution date which would constitute a conversion to the underlying preferred shares.

Finally, in determining the discount rate, we reviewed numerous industry rates and determined a separate discount rate for each ARS as follows: We obtained the 10 year credit default swap spread for each of the underlying issuers (we believed that this was the most readily available information that would most closely represent an equivalent yield). We then adjusted this rate by 50 - 100 basis points depending on how far out the actual maturity date was in excess of 10 years (maturity dates range from 16.5 years to 25 years). We then added the 15-year swap rate at December 31, 2009, and finally added 50 or 100 basis points for the illiquidity and other market risks. The liquidity factor applied to these securities was based on the credit rating of the security (50 basis points for securities above investment grade and 100 basis points for securities slightly below investment grade). The final discount rates ranged from 4.4% - 6.9%.

For the Freddie Mac securities that we are holding as of December 31, 2009, we did not perform a discounted cash flow analysis. These securities are no longer paying interest so a discounted cash flow analysis would show a value far less than what would be an appropriate fair value. We believe that for these securities an analysis of the underlying value of the preferred shares is the best way to value these securities.

Based on these analyses, the discounted cash flows ranged from a total of approximately $62.5 million to $73.3 million. We believe that of these scenarios, the most likely scenario as of December 31, 2009 is that we will hold these securities to the maturity based on the high interest rates and will receive par. However, we also verified the reasonableness of the value by analyzing receipt of the fair value of the underlying preferred securities at maturity. The calculated fair values using the par value approach was $65.6 million as compared to $62.5 million using the underlying preferred securities. The current fair value that the Bank has recorded for the ARS portfolio based on the value of the underlying securities is approximately $67 million. As our current fair value falls within the range of the discounted cash flows analyses performed and higher than the most likely scenarios, we believe that our current fair value is an appropriate representation of what a willing market participant would pay for these securities and is an accurate estimate of our ARS fair value at December 31, 2009.

Based upon our methodology for determining the fair value of the auction rate securities, we recorded an OTTI charge totaling $2.0 million related to the Freddie Mac auction rate securities for the year ended December 31, 2009. We concluded that, as of December 31, 2009, the unrealized loss for the remainder of the auction rate securities is due to the market interest volatility, the continued illiquidity of the auction rate markets, and uncertainty in the financial markets as there has not been a deterioration in the credit quality of the issuer of the auction rate securities or a downgrade of the auction rate security from investment grade. It is not more likely than not that the Company would be required to sell the auction rate securities prior to recovery of the unrealized loss, nor does the Company intend to sell the security at the present time.
At December 31, 2009, we had six auction rate securities totaling $25.9 million which were below investment grade. At December 31, 2008, we had four auction rate securities totaling $6.1 million which were below investment grade.

During the year ended December 31, 2009, approximately $18.0 million of auction rate securities were redeemed with no gain or loss recognized. During the year ended December 31, 2009, $2.2 million of Federal National Mortgage Association (Fannie Mae) auction rate securities were converted into the underlying preferred shares and simultaneously sold recognizing a loss totaling $1.4 million in addition to the OTTI charge recognized in 2008.

For the year ended December 31, 2008, we valued the auction rate securities by valuing the underlying collateral. During the year ended December 31, 2008, the Federal government placed Fannie Mae and Freddie Mac into receivership and suspended dividend payments. As a result of placing Fannie Mae and Freddie Mac into receivership, we considered the auction rate securities collateralized by these quasi-government agencies as impaired and recognized a credit related impairment charge totaling $80.2 million. The OTTI charge was calculated based upon the fair market value of the underlying preferred shares. We concluded that any further decline in the market value as of December 31, 2008 was caused by market interest volatility, a significant widening of credit spreads across markets for these securities, and illiquidity and uncertainty in the financial markets.

At both December 31, 2009 and 2008, we had a trust preferred security issued by a non-registrant regional bank with an amortized cost of $1.0 million (after OTTI charges) and $2.9 million, respectively, and a fair value of $1.0 million and $1.2 million, respectively. There are no tranches associated with this security. When this asset was acquired it was an investment grade security but has subsequently deteriorated to a non-rated security. The issuer of this security is experiencing deterioration of its loan portfolio and net losses, but appears to be prepared to rectify these adverse conditions as the controlling family recently contributed an amount to ensure this institution remains well capitalized. This security has not defaulted nor deferred any interest payments as all interest has been paid as contractually stipulated. Based on an evaluation of the OTTI factors (as fully described above) during the year ended December 31, 2009, the Company recorded a credit related OTTI charge of $1.9 million. The OTTI charge was determined using a price quote from an independent broker (Level 2) as compared to the amortized cost as of December 31, 2009.

At both December 31, 2009 and 2008, we had one pooled trust preferred CDO ("TPCDO") with an amortized cost of $6.5 million (after OTTI charges) and $10.0 million, respectively, and a fair value of $150,000 and $3.0 million, respectively. We own a Class B tranche of the TPCDO, which was considered below investment grade at both December 31, 2009 and 2008. During the year ended December 31, 2009, we recognized a credit related impairment charge totaling $3.5 million to reduce the amortized cost to $6.5 million. For the period ended September 30, 2009, an independent third party analyzed the collateral waterfall. Based upon this analysis, the Company recognized an impairment charge of $3.0 million. At December 31, 2009, we obtained discounted cash flow scenarios from independent third parties. We used the most conservative result in order to value our TPCDO, which we believe also reflects the most likely expected cash flow. The factors used to value the TPCDO were a discount rate of 1.9%, a prepayment speed of 0.00%, and default ratios based upon the Texas ratios as noted.

Historically, there have been no prepayments on this security but the issuers into the TPCDO can prepay at their discretion after January 2008. We used prepayment speed range of 0% to 1% in the cash flow analyses. The cash flow analysis that we utilized in valuing the TPCDO used a 0% prepayment speed for the next two years. As there have been no prepayments and we continue to expect the underlying issuers in the TPCDO to focus on improving capital and liquidity, we expect prepayments to be minimal on this security. We factored in a nominal prepayment assumption into our cash flow analysis as the underlying issuers have the right to prepay.

The discount rate used in our analysis was the effective interest rate implicit in the security at the date of acquisition.

For purposes of completing the cash flow analysis, defaults and deferrals are treated in the same manner. At December 31, 2009, there are five institutions in deferral status which were excluded from the discounted cash flow analysis. In order to estimate potential defaults and deferrals we segregated the underlying issuers by the Texas ratio. This ratio is a key indicator of the health of the institution and the likelihood of failure. The underlying issuers were pooled based upon their Texas ratio as if the underlying issuer had already defaulted. There was one underlying issuer with a Texas ratio greater than 100% for which it was assumed to default at the next scheduled payment date. This security was included with the deferred issuers in the cash flow analysis. The second pool of underlying issuers were those institutions with a Texas ratio of 75.00% to 99.99%. The rate of deferral for these institutions was 35%. The third pool of underlying issuers was those institutions that had a Texas ratio between 50.00% and 74.99%. The rate of deferral for these institutions was 20%. The 35% and 20% rates were used as they are representative of current industry statistics of bank failures. The final group of underlying issuers is comprised of those with a Texas ratio of less than 49.99%, and a money center bank with a ratio slightly above 50.00%. As these banks are considered healthy, we concluded that there is minimal risk of default and assigned a zero default assumption in the cash flow analyses.

Based upon the discounted cash flow analysis, an additional credit related OTTI charge totaling $529,000 was recognized during the quarter ended December 31, 2009, resulting in a total credit related impairment charge of $3.5 million for this security for the year ended December 31, 2009.

The table below reflects the number and amount of single issue debt securities below investment grade and the lowest rating by security type at December 31, 2009 (in thousands):

	Amortized Cost	Fair Value	Unrealized Gain (Loss)	Lowest Credit Rating
Single Issuer Corporate Bonds:				
Airline #1	$ 1,597	$ 1,594	$ (3)	Ba2
Airline #2	552	552	—	No rating
Automobile	800	1,506	706	D
Commercial	495	435	(60)	No rating
Student Lender	5,000	3,920	(1,080)	Ba1
Trust Preferred Security	1,021	1,021	—	No rating
Auction Rate Securities:				
Federal Home Loan Bank Corporation	1,895	1,895	—	Ca
Money Center Banks	24,000	17,537	(6,463)	Ba3
Pooled Issuers:				
TPCDO	6,463	150	(6,313)	No rating

The below investment grade Federal Home Loan Mortgage Corporation auction rate securities are comprised of two securities. The below investment grade auction rate securities collateralized by preferred shares of money center banks consists of four securities, from two original issuers. In the first quarter of 2009, one of the issuers was acquired by the other.

The below investment grade for the student lender was one factor evaluated in determining whether it was appropriate to recognize an OTTI. We also considered and evaluated analysis prepared by two independent third party analysts and the financial data of the issuer. The financial factors we evaluated included but are not limited to, net income, return on assets, increased cash and cash equivalents, increased originations, and the amount of debt included in current liabilities. We also considered the effects of the student loan overhaul included in the Health Care legislation signed by President Obama in March 2010 which will eliminate the student lender's ability to originate new student loans. Management believes this security has a fair value below cost due to the weak economic environment, high unemployment, slow salary growth, and high consumer debt which has adversely affected income generation of the borrowers. As a result, student loans have exhibited increased delinquency and defaults. The student lender bond the Company owns was purchased in 2004 prior to the current credit crisis and for which the underlying loans are guaranteed by the Federal Government at 98%. Based upon the entirety of the evidence of the student lender corporate bond outlined above, management concluded that OTTI was not appropriate and that the unrealized loss was due to market factors.

At December 31, 2009, all other single issuer debt securities had a credit rating of investment grade.

During the year ended December 31, 2009, the Company recorded OTTI charges related to four single issuer corporate bonds totaling $9.1 million. The Company evaluated the length of time and extent the amortized cost exceeded fair value and the credit rating of the issuer. During 2009, two issuers filed for bankruptcy which resulted in a credit related OTTI charge of $7.2 million. The Company concluded that the financial deterioration of these two issuers resulted in a credit loss. The preponderance of the remainder of the loss was due to an airline company bond. The airline company issuer had not shown improved earnings and operations since a merger in the fourth quarter of 2008. Since there was no improvement, the Company concluded full receipt of the principal was unlikely and recorded a credit related OTTI. The amounts of the OTTI charges were determined based upon broker quotes (Level 2).

At December 31, 2009 and 2008, the Company owned preferred and common stock (collectively "equities"). The fair value of the equities was determined by quoted market prices; unrealized loss was determined by comparing the cost of the equity to its fair value. In order to determine whether OTTI should be recognized, we evaluated the length of time and the extent to which the fair value was below cost, the financial condition and near term prospects of the issuer, and the Company's intent and ability to retain the equity security to allow for recovery. Based upon the length of time these securities were in an unrealized loss position, the amount by which the cost exceeded fair value, and the financial prospects of the issuer, we recorded a $0.8 million OTTI charge during the fiscal year ended December 31, 2009.

The table below details certain information related to the equity securities as of December 31, 2009 (in thousands):

	Industry	Cost	Fair Value	Unrealized Gain (Loss)
Common	Telecommunications	$ 91	$ 94	$ 3
	Airline	862	862	—
Preferred	Airline	61	61	—
	Flooring and other	35	34	(1)
	Mining	27	91	64
	Money Center Banks	2,008	1,984	(24)

The Company has investments in certain debt securities, as noted in the table below, that have unrealized losses or may be otherwise impaired, but OTTI has not been recognized in the financial statements as management believes the decline is due to the credit markets coupled with the interest rate environment. In addition, these securities are making payments in accordance with the terms of the instruments.

The following table indicates the length of time individual securities that we consider temporarily impaired have been in a continuous unrealized loss position at December 31, 2009 (in thousands):

	Less than 12 months		12 months or longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Description of Securities						
U.S. Treasury Notes	$ 30,048	$ 65	$ —	$ —	$ 30,048	$ 65
U.S. Government Agencies	40,518	748	19,948	45	60,466	793
Mortgage-backed securities	7,932	43	15,661	667	23,593	710
Corporate notes	1,613	13	7,522	2,298	9,135	2,311
Pooled Trust Preferred CDO	—	—	150	6,313	150	6,313
Auction rate securities	—	—	58,047	11,953	58,047	11,953
Subtotal, debt securities	80,111	869	101,328	21,276	181,439	22,145
Marketable equity securities and other	—	—	1,044	26	1,044	26
Total temporarily impaired securities	$ 80,111	$ 869	$ 102,372	$ 21,302	$ 182,483	$ 22,171

The Company had a total of 52 debt securities with a fair market value of $123.4 million which were temporarily impaired at December 31, 2009. The total unrealized loss on these securities was $10.2 million, which is attributable to the market interest volatility, the continued illiquidity of the debt markets, and uncertainty in the financial markets. The remaining unrealized loss of $12.0 million is on 10 auction rate securities which have declined in value due to auction failures beginning in February 2008. It is not more likely than not that we would sell these securities before maturity, and we have the intent to hold all of these securities to maturity and will not be required to sell these securities, due to our ratio of cash and cash equivalents of approximately 6.2% of total assets at December 31, 2009. Therefore, the unrealized losses associated with these securities are not considered to be other than temporary.

The Company also had 2 equity securities with an aggregate fair market value of $1.0 million which were temporarily impaired at December 31, 2009. The total unrealized loss on these securities was $26,000. The preponderance of the unrealized loss for marketable equity securities and other is a $24,000 unrealized loss at December 31, 2009 on one money center bank preferred issue. As the stock market declined in the first and second quarter of 2009, especially related to the financial sector, the Company's investments decreased in value. At March 31, 2009, the unrealized loss totaled $348,000. subsequent to March 31, 2009, the fair value of this security has rebounded to an unrealized position of $24,000 at December 31, 2009. The issuer of this preferred equity security has raised sufficient capital to repay the Troubled Asset Relief Program ("TARP") funds, continue to pay its dividend, maintain its credit rating and remain well-capitalized. Based upon these factors, coupled with the increasing stock market prices, especially in the financial sector, the Company does not believe an OTTI charge is warranted at December 31, 2009.

The following table indicates the length of time individual securities have been in a continuous unrealized loss position at December 31, 2008 (in thousands):

	Less than 12 months		12 months or longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Description of Securities						
U.S. Government Agencies	$ 71,241	$ 378	$ 5,072	$ 2	$ 76,313	$ 380
Mortgage-backed securities	6,135	58	21,769	1,003	27,904	1,061
Corporate notes	14,480	3,407	4,100	9,731	18,580	13,138
Single Issuer Trust Preferred CDO	—	—	1,149	1,794	1,149	1,794
Pooled Trust Preferred CDO	—	—	2,981	7,006	2,981	7,006
Municipal securities	—	—	1,478	495	1,478	495
Auction rate securities	38,098	38,030	—	—	38,098	38,030
Subtotal, debt securities	129,954	41,873	36,549	20,031	166,503	61,904
Marketable equity securities and other	1,681	332	900	906	2,581	1,238
Total temporarily impaired securities	$ 131,635	$ 42,205	$ 37,449	$ 20,937	$ 169,084	$ 63,142

The Company had a total of 63 debt securities with an aggregate fair market value of $128.4 million which were temporarily impaired at December 31, 2008. The total unrealized loss on these securities was $23.9 million, which is attributable to market interest volatility, the continued illiquidity of the debt markets, and uncertainty in the financial markets which have decreased the market value of these securities. The remaining unrealized loss of $38.0 million is on 14 auction rate securities which have declined in value due to auction failures beginning in February 2008. We have the intent to hold these securities to maturity and will not be required to sell these securities, due to our ratio of cash and cash equivalents to total assets of approximately 10.85% of total assets at December 31, 2008. Therefore, the unrealized losses associated with these securities are not considered to be other than temporary.

The Company also had 10 equity securities with an aggregate fair market value of $2.6 million which were temporarily impaired at December 31, 2008. The total unrealized loss on these securities was $1.2 million.

The amortized cost and fair value of investment securities available for sale and held to maturity, by contractual maturity, at December 31, 2009 are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	December 31, 2009			
	Available for Sale		Held to Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
	(In thousands)			
Due in one year or less	$ 23,070	$ 23,153	$ —	$ —
Due after one through five years	56,766	56,101	—	—
Due after five through ten years	21,857	21,784	—	—
Due after ten years	188,098	181,807	340	337
Auction rate securities	78,895	66,942	—	—
Marketable equity securities and other	7,648	7,691	—	—
Totals	$ 376,334	$ 357,478	$ 340	$ 337

Gross gains realized on the sales of investment securities for the years ended December 31, 2009 and 2008 were approximately $553,000 and $313,000, respectively. Gross losses were approximately $1,413,000 and $998,000 for the years ended December 31, 2009 and 2008, respectively. During the year ended December 31, 2009, we sold the Fannie Mae auction rate securities and certain corporate notes. During the year ended December 31, 2008, we sold our preferred shares in Fannie Mae and Freddie Mac, the corporate note for which we took an OTTI charge, U.S. Treasuries, U.S. Agencies and certain corporate notes.

As of December 31, 2009 and 2008, securities sold under agreements to repurchase with a book value of approximately $50.0 million and $59.5 million, respectively, were outstanding. The book value of the securities pledged for these repurchase agreements was $55.60 million and $69.60 million, respectively. As of December 31, 2009 and 2008, the Company did not own investment securities of any one issuer where the carrying value exceeded 10% of stockholders' equity.

The following table sets forth the cost and fair value of available-for-sale and held-to-maturity securities as of the dates indicated:

	December 31,					
	2009		2008		2007	
	Cost	Fair Value	Cost	Fair Value	Cost	Fair Value
	(In thousands)					
Available-For-Sale						
U.S. Treasury Notes	$ 50,236	$ 50,206	$ —	$ —	$ —	$ —
U.S. Government Agencies	76,259	75,525	91,466	91,158	272,789	272,318
Mortgage-backed securities	134,810	136,043	83,845	83,821	53,886	53,057
Corporate notes	19,029	17,729	51,150	38,124	71,147	67,601
Single Issuer Trust Preferred CDO	1,021	1,021	3,000	1,206		
Pooled Trust Preferred CDO	6,463	150	10,000	2,994		
Municipal securities	1,973	2,171	1,973	1,603	1,973	3,004
Auction rate securities	78,895	66,942	101,110	63,080	184,597	184,597
Marketable equity securities and other	7,648	7,691	16,708	15,550	18,698	18,384
Total	$ 376,334	$ 357,478	$ 359,252	$ 297,536	$ 603,090	$ 598,961
Held-To-Maturity						
U.S. Government Agencies	$ 340	$ 337	$ 360	$ 362	$ 395	$ 405

The following tables summarize the Company's available-for-sale and held- to-maturity securities:

	December 31, 2009		
	Weighted Average Yield	Cost	Fair Value
	(Dollars in thousands)		
Available-For-Sale			
U.S. Treasury Notes			
Due within one year	1.93%	$ 20,123	$ 20,158
Due after one through five years	0.91	30,113	30,048
		50,236	50,206
U.S. Government Agencies Obligations			
Due after one year through five years	3.26	9,973	10,028
Due after five years through ten years	4.38	20,567	20,526
Due after ten years	6.02	45,719	44,971
		76,259	75,525
Municipal Obligations			
Due after ten years	9.41	1,973	2,171
		1,973	2,171
Mortgage-backed securities			
Due after one year through five years	4.43	6,768	6,946
Due after five years through ten years	4.82	654	689
Due after ten years	5.64	127,388	128,408
		134,810	136,043
Corporate Notes (1)			
Due within one year	3.38	3,442	3,430
Due after one year through five years	5.70	9,912	9,079
Due after five years through ten years	8.45	1,188	1,122
Due after ten years	8.53	11,971	5,269
		26,513	18,900
Auction rate and other securities			
Common Stocks	0.11	953	956
Preferred Stocks	6.77	2,131	2,170
Auction Rate Securities	4.90	78,895	66,942
Money market funds	0.31	2,250	2,250
Federal Home Loan Bank Stock	7.43	2,314	2,315
		86,543	74,633
		$ 376,334	$ 357,478
Held-To-Maturity			
U.S. Government Agencies Obligations			
Due after ten years	6.58	340	337
		$ 340	$ 337

(1) Includes Single Issuer Trust Preferred CDO and Pooled Trust Preferred CDO

Federal Home Loan Bank Stock. The Bank owns stock of the FHLBNY which is necessary for it to be a member of the FHLBNY. Membership requires the purchase of stock equal to 0.20% of the Bank's mortgage related assets (investments and loans) plus 4.5% of the outstanding borrowings. The stock is redeemable at par, therefore, its cost is equivalent to its redemption value. The Bank's ability to redeem FHLBNY shares is dependent upon the redemption practices of the FHLBNY. At December 31, 2009, the FHLBNY neither placed restrictions on redemption of shares in excess of a member's required investment in stock, nor stated that it will cease paying dividends. The Bank did not consider this asset impaired at either December 31, 2009 or 2008.

Loan Portfolio

Loan Portfolio Composition. The Company's loans consist primarily of mortgage loans secured by residential and non-residential properties as well as commercial loans which are either unsecured or secured by personal property collateral. Most of the Company's loans are either made to individuals or personally guaranteed by the principals of the business to which the loan is made. At December 31, 2009, 2008 and 2007, the Company had total loans, net of unearned income of $430.3 million, $466.8 million and $434.8 million, respectively, and an allowance for loan losses of $11.4 million, $9.2 million and $4.2 million, respectively. From time to time, the Bank may originate residential mortgage loans, sell them on the secondary market, normally recognizing fee income in connection with the sale.

Interest rates on loans are affected by the demand for loans, the supply of money available for lending, credit risks, the rates offered by competitors and other conditions. These factors are in turn affected by, among other things, economic conditions, monetary policies of the federal government, and legislative tax policies.

In order to manage interest rate risk, the Bank focuses its efforts on loans with interest rates that adjust based upon changes in the prime rate or changes in United States Treasury or similar indices. Generally, credit risks on adjustable-rate loans are somewhat greater than on fixed-rate loans primarily because, as interest rates rise, so do borrowers' payments, increasing the potential for default. The Bank seeks to impose appropriate loan underwriting standards in order to protect against these and other credit related risks associated with its lending operations.

In addition to analyzing the income and assets of its borrowers when underwriting a loan, the Bank obtains independent appraisals on all material real estate in which the Bank takes a mortgage. The Bank generally obtains title insurance in order to protect against title defects on mortgaged property.

Commercial and Mortgage Loans. The Bank originates commercial mortgage loans secured by office buildings, retail establishments, multi-family residential real estate and other types of commercial property. Substantially all of the properties are located in the New York City metropolitan area.

The Bank generally makes commercial mortgage loans with loan to value ratios not to exceed 75% and with terms to maturity that do not exceed 15 years. Loans secured by commercial properties generally involve a greater degree of risk than one-to four-family residential mortgage loans. Because payments on such loans are often dependent on successful operation or management of the properties, repayment may be subject, to a greater extent, to adverse conditions in the real estate market or the economy. The Bank seeks to minimize these risks through its underwriting policies. The Bank evaluates the qualifications and financial condition of the borrower, including credit history, profitability and expertise, as well as the value and condition of the underlying property. The factors considered by the Bank include net operating income; the debt coverage ratio (the ratio of cash net income to debt service); and the loan to value ratio. When evaluating the borrower, the Bank considers the financial resources and income level of the borrower, the borrower's experience in owning or managing similar property and the Bank's lending experience with the borrower. The Bank's policy requires borrowers to present evidence of the ability to repay the loan without having to resort to the sale of the mortgaged property. The Bank also seeks to focus its commercial mortgage loans on loans to companies with operating businesses, rather than passive real estate investors.

Commercial Loans. The Bank makes commercial loans to businesses for inventory financing, working capital, machinery and equipment purchases, expansion, and other business purposes. These loans generally have higher yields than mortgage loans, with maturities of one year, after which the borrower's financial condition and the terms of the loan are re-evaluated. At December 31, 2009 and 2008, approximately $50.7 million and $68.4 million, respectively, or 11.7% and 14.6%, respectively, of the Company's total loan portfolio consisted of such loans.

Commercial loans tend to present greater risks than mortgage loans because the collateral, if any, tends to be rapidly depreciable, difficult to sell at full value and is often easier to conceal. In order to limit these risks, the Bank evaluates these loans based upon the borrower's ability to repay the loan from ongoing operations. The Bank considers the business history of the borrower and perceived stability of the business as important factors when considering applications for such loans. Occasionally, the borrower provides commercial or residential real estate collateral for such loans, in which case the value of the collateral may be a significant factor in the loan approval process.

Residential Mortgage Loans (1 to 4 family loans). The Bank makes residential mortgage loans secured by first liens on one-to-four family owner-occupied or rental residential real estate. At December 31, 2009 and 2008, approximately $129.9 million and $140.2 million, respectively, or 30.1% and 30.0%, respectively, of the Company's total loan portfolio consisted of such loans. The Bank offers both adjustable rate mortgages ("ARMS") and fixed-rate mortgage loans. The relative proportion of fixed-rate loans versus ARMs originated by the Bank depends principally upon current customer preference, which is generally driven by economic and interest rate conditions and the pricing offered by the Bank's competitors. At December 31, 2009 and 2008, approximately 14% and 13%, respectively, of the Bank's residential one-to-four family owner-occupied first mortgage portfolio were ARMs and approximately 86% and 87%, respectively, were fixed-rate loans. The percentage represented by fixed-rate loans tends to increase during periods of low interest rates. The ARMs generally carry annual caps and life-of-loan ceilings, which limit interest rate adjustments.

The Bank's residential loan underwriting criteria are generally comparable to those required by Fannie Mae and other major secondary market loan purchasers. Generally, ARM credit risks are somewhat greater than fixed-rate loans primarily because, as interest rates rise, the borrowers' payments rise, increasing the potential for default. The Bank's teaser rate ARMs (ARMs with low initial interest rates that are not based upon the index plus the margin for determining future rate adjustments) were underwritten based on the payment due at the fully-indexed rate.

In addition to verifying income and assets of borrowers, the Bank obtains independent appraisals on all residential first mortgage loans and title insurance is required at closing. Private mortgage insurance is required on all loans with a loan-to-value ratio in excess of 80% and the Bank requires real estate tax escrows on such loans. Real estate tax escrows are voluntary on residential mortgage loans with loan-to-value ratios of 80% or less.

Fixed-rate residential mortgage loans are generally originated by the Bank for terms of 15 to 30 years. Although 30 year fixed-rate mortgage loans may adversely affect our net interest income in periods of rising interest rates, the Bank originates such loans to satisfy customer demand. Such loans are generally originated at initial interest rates which exceed the fully indexed rate on ARMs offered at the same time. Fixed-rate residential mortgage loans originated by the Bank generally include due-on-sale clauses, which permit the Bank to demand payment in full if the borrower sells the property without the Bank's consent.

Due-on-sale clauses are an important means of adjusting the rates on the Bank's fixed-rate mortgage loan portfolio, and the Bank will generally exercise its rights under these clauses if necessary to maintain market yields.

ARMs originated in recent years have interest rates that adjust annually based upon the movement of the one year treasury bill constant maturity index, plus a margin of 2.00% to 2.75%. These loans generally have a maximum interest rate adjustment of 2% per year, with a lifetime maximum interest rate adjustment, measured from the initial interest rate, of 5.5% or 6.0%.

The Bank offers a variety of other loan products including residential single family construction loans to persons who intend to occupy the property upon completion of construction, home equity loans secured by junior mortgages on one-to-four family owner-occupied residences, and short-term fixed-rate consumer loans either unsecured or secured by monetary assets such as bank deposits and marketable securities or personal property. At December 31, 2009 and 2008, the Company's loan portfolio was comprised of $250.8 million and $259.3 million, respectively, or 58.2% and 55.4%, respectively, of other loan products.

Origination of Loans. Loan originations can be attributed to depositors, retail customers, phone inquiries, advertising, the efforts of the Bank's loan officers, and referrals from other borrowers, real estate brokers and builders. The Bank originates loans primarily through its own efforts, occasionally obtaining loan opportunities as a result of referrals from loan brokers.

At December 31, 2009, the Bank was generally not permitted to make loans to one borrower in excess of approximately $13.5 million, with an additional amount of approximately $9.0 million being permitted if secured by readily marketable collateral. The Bank was also not permitted to make any single loan in an amount in excess of approximately $13.5 million. At December 31, 2009, the Bank was in compliance with these standards.

Delinquency Procedures. When a borrower fails to make a required payment on a loan, the Bank attempts to cause the deficiency to be cured by contacting the borrower. The Bank reviews past due loans on a case by case basis, taking the action it deems appropriate in order to collect the amount owed. Litigation may be necessary if other procedures are not successful. Judicial resolution of
a past due loan can be delayed if the borrower files a bankruptcy petition because collection action cannot be continued unless the Bank first obtains relief from the automatic stay provided by the Bankruptcy Code.

If a non-mortgage loan becomes delinquent and satisfactory arrangements for payment cannot be made, the Bank seeks to realize upon any personal property collateral to the extent feasible and collect any remaining amount owed from the borrower through legal proceedings, if necessary.

It is the Bank's policy to discontinue accruing interest on a loan when it is 90 days past due or if management believes that continued interest accruals are unjustified. The Bank may continue interest accruals if a loan is more than 90 days past due if the Bank determines that the nature of the delinquency and the collateral are such that collection of the principal and interest on the loan in full is reasonably assured. When the accrual of interest is discontinued, all accrued but unpaid interest is charged against current period income. Once the accrual of interest is discontinued, the Bank records interest as and when received until the loan is restored to accruing status. If the Bank determines that collection of the loan in full is in reasonable doubt, then amounts received are recorded as a reduction of principal until the loan is returned to accruing status.

The following table sets forth information concerning the Company's loan portfolio by type of loan at the dates indicated. (dollars in thousands):

	December 31,									
	2009		2008		2007		2006		2005	
	Amount	% of Total	Amount	% of Total	Amount	% of Total	Amount	% of Total	Amount	% of Total
Commercial and professional loans	$ 50,672	11.7%	$ 68,418	14.6%	$ 76,132	17.4%	$ 63,331	17.0%	$ 33,370	10.8%
Secured by real estate										
1 - 4 family	129,925	30.1	140,150	30.0	142,140	32.6	139,611	37.5	139,931	45.1
Multi family	7,432	1.7	4,031	0.9	3,506	0.8	4,013	1.1	2,874	0.9
Non-residential (commercial)	242,927	56.4	254,831	54.4	212,850	48.8	160,417	43.1	132,142	42.6
Consumer	396	0.1	460	0.1	1,691	0.4	4,763	1.3	2,018	0.6
Total loans	431,352	100.0%	467,890	100.0%	436,319	100.0%	372,135	100.0%	310,335	100.0%
Less: Allowance for loan losses	(11,416)		(9,204)		(4,183)		(3,771)		(3,266)	
Unearned fees	(1,003)		(1,137)		(1,534)		(1,212)		(1,105)	
Loans, net	$ 418,933		$ 457,549		$ 430,602		$ 367,152		$ 305,964	

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Impaired loan balance, nonaccrual loans and loans greater than 90 days still accruing

The following table sets forth certain information regarding nonaccrual loans, including the ratio of such loans to total assets as of the dates indicated, and certain other related information. The Bank had no foreclosed real estate during these periods and loans past due more than 90 days still accruing were $0 and $99,000 at December 31, 2009 and 2008, respectively.

	December 31,				
	2009	2008	2007	2006	2005
	(Dollars in Thousands)				
Nonaccrual loans:					
Commercial and professional loans	$ 1,700	$ —	$ —	$ —	$ —
Consumer	—	—	—	—	3
Secured by real estate	12,210	130	153	201	253
Total nonaccrual loans	13,910	130	153	201	256
Accruing loans delinquent 90 days or more	—	99	314	—	74
Total nonperforming loans	$ 13,910	$ 229	$ 467	$ 201	$ 330
Total nonperforming loans to total assets	1.54%	.02%	.04%	.02%	.03%

The following tables present information regarding the Company's total allowance for loan losses as well as the allocation of such amounts to the various categories of loans at the dates indicated. (dollars in thousands):

	December 31, 2009		
	Allowance for Loan Losses	Percent of Allowance	Percent of Total Loans
Commercial and professional loans	$ 1,774	15.5%	11.7%
Secured by real estate			
1 - 4 family	651	5.7	30.1
Multi family	30	0.3	1.7
Non-residential	8,194	71.7	56.4
Consumer and other	7	0.1	0.1
General allowance (1)	760	6.7	
Total allowance for loan losses	$ 11,416	100.0%	100.0%

(1)The allowance for loan losses is allocated to specific loans as necessary.

	December 31, 2008		
	Allowance for Loan Losses	Percent of Allowance	Percent of Total Loans
Commercial and professional loans	$ 898	9.7%	14.6%
Secured by real estate			
1 - 4 family	696	7.6	30.0
Multi family	19	0.2	0.9
Non-residential	7,512	81.6	54.4
Consumer and other	4	0.1	0.1
General allowance (1)	75	0.8	
Total allowance for loan losses	$ 9,204	100.0%	100.0%

(1)The allowance for loan losses is allocated to specific loans as necessary.

	December 31, 2007		
	Allowance for Loan Losses	Percent of Allowance	Percent of Total Loans
Commercial and professional loans	$ 929	22.2%	17.4%
Secured by real estate			
1 - 4 family	591	14.2	32.6
Multi family	43	1.0	0.8
Non-residential	2,597	62.1	48.8
Consumer and other	21	0.5	0.4
General allowance (1)	3	0.0	
Total allowance for loan losses	$ 4,183	100.0%	100.0%

(1)The allowance for loan losses is allocated to specific loans as necessary.

The following table sets forth information regarding the aggregate maturities of the Company's loans in the specified categories and the amount of such loans which have fixed and variable rates.

	December 31, 2009			
	Within 1 Year	1 to 5 Years	After 5 Years	Total
	(In thousands)			
Fixed Rate				
Commercial and professional	$ 7,904	$ 18,561	$ 893	$ 27,358
Non-residential	25,556	7,100	47,303	79,959
Total fixed rate	$ 33,460	$ 25,661	$ 48,196	$ 107,317
Adjustable Rate				
Commercial and professional	13,215	7,028	3,071	23,314
Non-residential	61,280	23,624	78,064	162,968
Total adjustable rate	$ 74,495	$ 30,652	$ 81,135	$ 186,282
Total	$ 107,955	$ 56,313	$ 129,331	$ 293,599

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Demand loans, loans with no stated maturity, are included in the table above in the Within One Year category.

The following table sets forth information with respect to activity in the Company's allowance for loan losses during the periods indicated (in thousands, except percentages):

	Years Ended December 31,				
	2009	2008	2007	2006	2005
Average loans outstanding	$ 448,394	$ 461,678	$ 389,520	$ 327,210	$ 287,178
Allowance at beginning of period	9,204	4,183	3,771	3,266	2,927
Charge-offs:					
Commercial and other loans	1,169	1	—	42	26
Real estate loans	6,025	—	—	—	—
Total loans charged-off	7,194	1	—	42	26
Recoveries:					
Commercial and other loans	106	118	57	137	185
Real estate loans	—	—	—	—	—
Total loans recovered	106	118	57	137	185
Net recoveries (charge-offs)	(7,088)	117	57	95	159
Provision for loan losses charged to operating expenses	9,300	4,904	355	410	180
Allowance at end of period	$ 11,416	$ 9,204	$ 4,183	$ 3,771	$ 3,266
Ratio of net recoveries (charge-offs) to average loans outstanding	(1.58)%	.03%	.01%	.03%	.06%
Allowance as a percent of total loans	2.65%	1.97%	0.96%	1.01%	1.05%
Total loans at end of period	$ 431,352	$ 467,890	$ 436,319	$ 372,135	$ 310,335

Deposits

The Bank concentrates on obtaining deposits from a variety of businesses, professionals and retail customers. The Bank offers a number of different deposit programs, including statement savings accounts, NOW accounts, money market deposits accounts, checking accounts and certificates of deposits with terms from seven days to five years. Deposit account terms vary according to the minimum balance required, the time period the funds must remain on deposit and the interest rate, among other factors. The Bank prices its deposit offerings competitively within the market it serves. These products are designed to attract new customers, retain existing customers and create opportunities to offer other bank products or services. While the market and pricing for deposit funds are very competitive, the Bank believes that personalized, quality service is also an important element in retaining core deposit customers.

The following table summarizes the composition of the average balances of major deposit categories:

	December 31,					
	2009		2008		2007	
	Average Amount	Average Yield	Average Amount	Average Yield	Average Amount	Average Yield
	(Dollars in thousands)					
Demand deposits	$ 56,544	—	$ 54,452	—	$ 50,647	—
NOW and money market	23,900	0.31%	39,849	1.58%	29,984	0.76%
Savings deposits	180,729	1.24	247,923	2.84	261,065	3.83
Time deposits	426,892	2.32	456,803	3.79	449,754	4.83
Total deposits	$ 688,065	1.78%	$ 799,027	3.13%	$ 791,450	4.04%

The aggregate amount of jumbo certificates of deposit, each with a minimum denomination of $100,000, was approximately $191.32 million and $213.58 million at December 31, 2009 and 2008, respectively.

The following table summarizes the maturity distribution of time deposits of $100,000 or more as of December 31, 2009 and 2008:

	December 31,	
	2009	2008
	(In thousands)	
3 months or less	$ 51,133	$ 121,288
Over 3 months but within 6 months	60,658	69,751
Over 6 months but within 12 months	35,452	19,920
Over 12 months	44,078	2,619
Total	$ 191,321	$ 213,578

It has been the Bank's experience that the majority of these certificates will renew.

Short-Term Borrowings

Securities sold under agreements to repurchase generally mature within 30 days from the date of the transactions. Short-term borrowings consist of securities sold under agreements to repurchase and various other borrowings which generally have maturities of less than one year. The details of these categories are presented below:

	Years Ended December 31,		
	2009	2008	2007
	(Dollars in thousands)		
Securities sold under repurchase agreements and federal funds purchased			
Balance at year-end	$ 50,000	$ 59,504	$ 76,842
Average during the year	$ 56,436	$ 61,162	$ 40,049
Maximum month-end balance	$ 57,000	$ 72,324	$ 76,842
Weighted average rate during the year	4.08%	3.83%	4.93%
Rate at December 31	4.02%	3.76%	4.65%

Capital Resources and Liquidity

Liquidity

The management of the Company's liquidity focuses on ensuring that sufficient funds are available to meet loan funding commitments, withdrawals from deposit accounts, the repayment of borrowed funds, and ensuring that the Bank and the Company comply with regulatory liquidity requirements. Liquidity needs of the Bank have historically been met by deposits, investments in federal funds sold, principal and interest payments on loans, and maturities of investment securities. Additional liquidity, up to approximately $284 million is available from the Federal Reserve Bank and the FHLBNY.

The current uncertainties in the credit markets have negatively impacted our ability to liquidate, if necessary, investments in auction rate securities. We are not certain as to when the liquidity issues relating to these investments will improve; however, we have the intent to hold these available for sale securities to maturity, and do not believe we will be required to sell these securities prior to maturity.

Approximately $18.0 million principal amount of auction rate securities that came due during the twelve months ended December 31, 2009 were redeemed.

At December 31, 2009, our portfolio of investment securities included approximately $26.5 million, at cost, of corporate notes, including single issuer and pooled trust preferred securities, for which an OTTI charge has not been recorded in our financial statements. Due primarily to market liquidity issues, the fair value of these securities, presently $18.9 million, may be negatively impacted in the future.

OTTI is a non-cash charge and not necessarily an indicator of a permanent decline in value. Security valuations require significant estimates, judgments and assumptions by management and are considered a critical accounting policy of the Company. See "New Accounting Pronouncements - Accounting For Fair Value Measurement" below for further discussion of this policy.

Based on our expected operating cash flows, and our other sources of cash, we do not expect the potential lack of liquidity in these auction rate securities and corporate notes to affect our capital, liquidity or our ability to execute our current business plan. We have cash and cash equivalents totaling $60.8 million, or 6.7% of total assets at December 31, 2009. In addition, we have the capacity to borrow up to approximately $195 million from the Federal Reserve Bank and approximately $89 million from the FHLBNY if the need should arise.

For the parent company, Berkshire Bancorp Inc., liquidity means having cash available to fund its operating expenses and to pay stockholder dividends on its preferred and common stock, when and if declared by the Company's Board of Directors. On March 31, 2009, the Company announced that it would temporarily suspend its previously announced policy of paying a regular cash dividend on the Company's common stock. We are current as to dividend payments on our preferred stock.

The ability of the Company to meet these obligations, including the payment of dividends on its preferred and common stock when and if declared by the Board of Directors, is not currently dependent upon the receipt of dividends from the Bank. At December 31, 2009, the Company had cash of approximately $6.6 million and investment securities with a fair market value of $5.8 million.

On September 7, 2008, the US Treasury and the FHFA announced a plan to place Fannie Mae and Freddie Mac into conservatorship under the authority of the FHFA, a plan which eliminated dividends on Fannie Mae and Freddie Mac common and preferred stock for the foreseeable future.

As of June 30, 2008, the Bank held auction rate securities with a cost basis of $86.3 million, including securities which were collateralized by Fannie Mae or Freddie Mac preferred shares. The Bank also held preferred shares of Fannie Mae and Freddie Mac with a cost basis of $8.7 million and $6.9 million, respectively, and a corporate note from Lehman Brothers which filed for bankruptcy protection on September 15, 2008. Due to the U.S. Treasury actions and the bankruptcy of Lehman Brothers, we determined that these securities were other than temporarily impaired and recognized a pre-tax charge totaling $94.3 million, consisting of $80.2 million related to the auction rate securities; $8.1 million related to the Fannie Mae and Freddie Mac preferred shares and $6.1 million charge for the Lehman Brothers corporate note. The Freddie Mac auction rate securities were further reduced in 2009 through an other-than-temporary impairment charge of approximately $2.0 million.

The OTTI charge related to the Lehman Brothers corporate note was considered an ordinary loss under the current federal tax code. Therefore, we recognized a deferred tax asset, and related tax benefit, related to this ordinary loss of $6.1 million. The other than temporary charge related to the Fannie Mae and Freddie Mac preferred shares, both direct investments and through the auction rate securities, were originally considered capital losses under the federal tax code. As such, we recognized a tax benefit of $760,000 relating to $1.735 million of previously recognized capital gains. A valuation allowance was recorded on the remaining deferred tax asset.

In October 2008, the U.S. Congress passed EESA which changed the characteristics of direct and indirect ownership of the Fannie Mae and Freddie Mac capital losses to ordinary losses. In addition to this change in the nature of the losses, the EESA also provided for financial institutions to apply for funds under the Troubled Asset Repurchase Program which provided capital from the US Treasury in the form of Preferred Shares. We applied to participate in this program, but declined to accept the funds offered in December 2009.

As a result of the previously discussed OTTI charge related to the Fannie Mae and Freddie Mac stock and the Lehman Brothers note, the Bank no longer met the definition of a "well capitalized" institution as of September 30, 2008. In order to restore our "well capitalized" position, in October 2008, the Company's Chairman of the Board and majority stockholder, and two non-affiliated investors, purchased an aggregate of 60,000 Series A Preferred Shares at $1,000 per share, or $60 million in the aggregate. Each Series A Preferred Share bears non-cumulative cash dividends at the rate of 8% per annum, payable quarterly, is mandatorily convertible into 123.153 shares of our Common Stock on October 31, 2011, unless previously redeemed, and is redeemable at the option of the Company between April 30, 2009 and November 1, 2010 at a redemption price of $1,100. The transaction was consummated on October 31, 2008. There were no redemptions of Series A Preferred Shares during the year ended December 31, 2009. After the sale of the Series A Preferred Stock, we met the definition of "well capitalized" institution.

At December 31, 2009 and 2008, our portfolio of investment securities included approximately $78.9 million and $101 million at cost, respectively, of auction rate securities for which an OTTI charge has not been recorded in our financial statements.

Contingent Liabilities and Commitments

The Bank maintains financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit and stand-by letters of credit. The following table presents the Company's commitments at December 31, 2009.

	Expiration By Period				
	Total	Less Than 1 Year	1-3 Years	3-5 Years	More Than 5 Years
	(In thousands)				
Lines of Credit	$ 7,859	$ 5,521	$ 28	$ 54	$ 2,256
Standby Letters of Credit	1,117	1,117	00	00	00
Loan Commitments	1,292	1,292	00	00	00
Total	$ 10,268	$ 7,930	$ 28	$ 54	$ 2,256

Contractual Obligations

The following table presents the Company's contractual obligations at December 31, 2009.

	Payments Due By Periods				
	Total	Less Than 1 Year	1-3 Years	3-5 Years	More Than 5 Years
	(In thousands)				
Borrowings	$ 31,004	$ 16,000	$ 15,004	$ —	$ —
Operating Leases	4,385	1,284	2,252	623	226
Time Deposits	427,777	343,279	82,259	2,239	—
Total Contractual Obligations	$ 463,166	$ 360,563	$ 99,515	$ 2,862	$ 226

Capital

The capital ratios of the Bank and the Company are presently in excess of the requirements necessary to meet the "well capitalized" capital category established by bank regulators. See Note O - "Regulatory Matters" to the Consolidated Financial Statements.

Interest Rate Risk

Fluctuations in market interest rates can have a material effect on the Bank's net interest income because the yields earned on loans and investments may not adjust to market rates of interest with the same frequency, or with the same speed, as the rates paid by the Bank on its deposits.

Most of the Bank's deposits are either interest-bearing demand deposits or short term certificates of deposit and other interest-bearing deposits with interest rates that fluctuate as market rates change. Management of the Bank seeks to reduce the risk of interest rate fluctuations by concentrating on loans and securities investments with either short terms to maturity or with adjustable rates or other features that cause yields to adjust based upon interest rate fluctuations. In addition, to cushion itself against the potential adverse effects of a substantial and sustained increase in market interest rates, the Bank has from time to time purchased off balance sheet interest rate cap contracts which generally provide that the Bank will be entitled to receive payments from the other party to the contract if interest rates exceed specified levels. These contracts, when written, are entered into with major financial institutions.

The Company seeks to maximize its net interest margin within an acceptable level of interest rate risk. Interest rate risk can be defined as the amount of the forecasted net interest income that may be gained or lost due to favorable or unfavorable movements in interest rates. Interest rate risk, or sensitivity, arises when the maturity or repricing characteristics of assets differ significantly from the maturity or repricing characteristics of liabilities.

In the banking industry, a traditional measure of interest rate sensitivity is known as "gap" analysis, which measures the cumulative differences between the amounts of assets and liabilities maturing or repricing at various time intervals. The following table sets forth the Company's interest rate repricing gaps for selected maturity periods:

Berkshire Bancorp Inc.
Interest Rate Sensitivity Gap at December 31, 2009
(in thousands, except for percentages)

	3 Months or Less	3 Through 12 Months	1 Through 3 Years	Over 3 Years	Total	Fair Value
Federal funds sold	—				—	
(Rate)						
Interest bearing deposits in banks	55,376	—	—	—	55,376	55,376
(Rate)	0.43%				0.43%	
Loans (1)(2)						
Adjustable rate loans	103,268	17,904	60,091	27,660	208,923	204,030
(Rate)	5.09%	6.03%	7.02%	6.58%	5.91%	
Fixed rate loans	12,990	20,690	27,852	160,897	222,429	224,936
(Rate)	5.15%	6.74%	7.33%	6.25%	6.35%	
Total loans	116,258	38,594.00	87,943	188,557	431,352	419,918
Investments (3)(4)	121,651	22,777	36,656	194,996	376,080	357,815
(Rate)	4.69%	2.42%	1.67%	5.49%	4.67%	
Total rate-sensitive assets	293,285	61,371.00	124,599	383,553	862,808	
Deposit accounts (5)						
Savings and NOW	213,366	—	—	—	213,366	213,366
(Rate)	0.94%				0.94%	
Money market	9,431	—	—	—	9,431	9,431
(Rate)	0.43%				0.43%	
Time Deposits	115,942	227,336	82,259	2,240	427,777	429,449
(Rate)	1.56%	1.65%	2.27%	1.80%	1.75%	
Total deposit accounts	338,739	227,336.00	82,259	2,240	650,574	
Repurchase Agreements	—	5,000	45,000	—	50,000	49,842
(Rate)		4.68%	3.89%		3.97%	
Other borrowings	2,000	14,000	15,004	22,681	53,685	54,437
(Rate)	5.95%	5.97%	3.85%	2.72%	4.00%	
Total rate-sensitive liabilities	340,739	246,336.00	142,263	24,921	754,259	
Interest rate caps	40,000			(40,000)		
Gap (repricing differences)	(87,454)	(184,965)	(17,664)	398,632	108,549	
Cumulative Gap	(87,454)	(272,419)	(290,083)	108,549		
Cumulative Gap to Total Rate Sensitive Assets	(10.14)%	(31.57)%	(33.62)%	12.58%		

(1) Adjustable-rate loans are included in the period in which the interest rates are next scheduled to adjust rather than in the period in which the loans mature. Fixed-rate loans are scheduled according to their maturity dates.
(2) Includes nonaccrual loans.

(3) Investments are scheduled according to their respective repricing (variable rate investments) and maturity (fixed rate securities) dates.
(4) Investments are stated at book value.
(5) NOW accounts and savings accounts are regarded as readily accessible withdrawal accounts. The balances in such accounts have been allocated among maturity/repricing periods based upon The Berkshire Bank's historical experience. All other time accounts are scheduled according to their respective maturity dates.

Impact of Inflation and Changing Prices

The Company's financial statements measure financial position and operating results in terms of historical dollars without considering the changes in the relative purchasing power of money over time due to inflation. The impact of inflation is reflected in the increasing cost of the Company's operations. The assets and liabilities of the Company are largely monetary. As a result, interest rates have a greater impact on the Company's performance than do the effects of general levels of inflation. In addition, interest rates do not necessarily move in the direction, or to the same extent as the price of goods and services. However, in general, high inflation rates are accompanied by higher interest rates, and vice versa.

New Accounting Pronouncements

Accounting For Derivative Instruments and Hedging Activities

The FASB issued FASB ASC 815, "Derivatives and Hedging", ("ASC 815"), which requires enhanced disclosures about an entity's derivative and hedging activities, including information about (a) how and why an entity uses derivative instruments, (b) how derivative instruments and related hedged items are accounted for under ASC 815 and its related interpretations, and (c) how derivative instruments and related hedged items affect an entity's financial position, financial performance, and cash flows. The requirements are effective for all financial statements issued for fiscal years and interim periods beginning after November 15, 2008, with earlier adoption permitted. Adoption of ASC 815 on January 1, 2009 did not have a material impact on the Company's results of operations or financial condition.

Determining The Fair Value Of A Financial Asset When The Market For That Asset Is Not Active

The FASB amended FASB ASC 820, "Fair Value Measurements and Disclosures", ("ASC 820"), which applies to financial assets within the scope of accounting pronouncements that require or permit fair value measurements in accordance with ASC 820. ASC 820 clarifies the application of ASC 820 in a market that is not active and provides an example to illustrate key considerations in determining the fair value of a financial asset when the market for that financial asset is not active. ASC 820 permits, in determining fair value for a financial asset in a dislocated market, the use of a reporting entity's own assumptions about future cash flows and appropriately risk-adjusted discount rates when relevant observable inputs are not available. ASC 820 was effective upon issuance. Adoption of ASC 820 did not have a material impact on the Company's results of operations or financial condition.

Employer's Disclosures about Postretirement Benefit Plan Assets

The FASB issued FASB ASC 715, "Compensation-Retirement Benefits", ("ASC 715"), which provides guidance on an employer's disclosures about plan assets of a defined benefit pension or other postretirement plan. ASC 715 clarifies that the objectives of the disclosures about plan assets in an employer's defined benefit pension or other postretirement plan are to provide users of financial statements with an understanding of: (1) how investment allocation decisions are made, including the factors that are pertinent to an understanding of investment policies and strategies; (2) the categories of plan assets; (3) the inputs and valuation techniques used to measure the fair value of plan assets; (4) the effect of fair value measurements using significant unobservable inputs (Level 3) on changes in plan assets for the period; and (5) significant concentrations of risk within plan assets. ASC 715 also expands the disclosures related to these objectives. The disclosures about plan assets required by ASC 715 are effective for fiscal years ending after December 15, 2009, or January 1, 2010 as to the Company. Upon initial application, the provisions of ASC 715 are not required for earlier periods that are presented for comparative purposes, although application of the provisions of ASC 715 to prior periods is permitted. Early adoption is not permitted. Adoption of ASC 715 is not expected to have a material impact on the Company's results of operations or financial condition.

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FASB ASC 325, Investments-Other

The FASB amended ASC 325, "Investments-Other", to align the impairment guidance with that in FASB ASC 320, Investments-Debt and Equity Securities, and related implementation guidance. ASC 325 was effective for reporting periods ending after December 15, 2008, and is applied prospectively. Adoption of ASC 325 on January 1, 2009 did not have a material impact on the Company's results of operations or financial condition.

Recognition and Presentation of Other-Than-Temporary Impairments

The FASB issued FASB ASC 320, "Investments-Debt and Equity Securities", ("ASC 320"), to make the guidance on other-than-temporary impairments of debt securities more operational and improve the financial statement disclosures related to other-than-temporary impairments for debt and equity securities. ASC 320 clarifies the interaction of the factors that should be considered when determining whether a debt security is other-than-temporarily impaired.

To evaluate whether a debt security is other-than-temporarily impaired, an entity must first determine whether the fair value of the debt security is less than its amortized cost basis at the statement of condition date. If the fair value is less than the amortized cost basis, then the entity must assess whether it intends to sell the security or whether it is more likely than not that it will be required to sell the debt security before recovery of its amortized cost basis. If an entity determines that it will sell a debt security or that it more likely than not will be required to sell a debt security before recovery of its amortized cost basis, then it must recognize the difference between the fair value and the amortized cost basis of the debt security in earnings. Otherwise, the other-than-temporary impairment must be separated into two components: the amount related to the credit loss and the amount related to all other factors. The amount related to the credit loss must be recognized in earnings, while the other component must be recognized in other comprehensive income, net of tax. The portion of other-than-temporary impairment recognized in earnings would decrease the amortized cost basis of the debt security, and subsequent recoveries in the fair value of the debt security would not result in a write-up of the amortized cost basis.

The Company adopted ASC 320 effective April 1, 2009. The adoption did not have a material impact on the Company's financial condition and results of operations. The additional disclosures related to ASC 320 are included in Note C - Investment Securities in the Consolidated Financial Statements.

Determining Fair Value When The Volume And Level of Activity For The Asset Or Liability Have Significantly Decreased And Identifying Transactions That Are Not Orderly

The FASB amended FASB ASC 820 to provide additional guidance on estimating fair value when the volume and level of activity for an asset or liability have significantly decreased. ASC 820 also includes guidance on identifying circumstances that indicate a transaction is not orderly. ASC 820 emphasizes that, regardless of whether the volume and level of activity for an asset or liability have decreased significantly and regardless of which valuation technique was used, the objective of a fair value measurement remains the same - to estimate the price that would be received to sell an asset or transfer a liability in an orderly transaction between market participants at the measurement date under current market conditions.

The Company adopted ASC 820 effective April 1, 2009. The adoption did not have a material impact on the Company's financial condition and results of operations. The additional disclosures related to ASC 820 are included in Note M - Fair Value of Financial Instruments in the Consolidated Financial Statements.

Subsequent Events

The FASB issued FASB ASC 855, "Subsequent Events", ("ASC 855"), to incorporate the accounting and disclosures requirements for subsequent events into U.S. GAAP. ASC 855 introduces new terminology, defines a date through which management must evaluate subsequent events, and lists the circumstances under which an entity must recognize and disclose events or transactions occurring after the balance-sheet date. The Company adopted ASC 855 as of June 30, 2009, which was the required effective date. The Company evaluated its December 31, 2009 financial statements for subsequent events.

The FASB Accounting Standards Codification

The FASB issued FASB ASC 105, "Generally Accepted Accounting Principles", ("ASC 105"), which has become the source of authoritative U.S. GAAP recognized by the FASB to be applied by nongovernmental entities. Rules and interpretive releases of the Securities and Exchange Commission ("SEC") under authority of the federal securities laws are also sources of authoritative U.S. GAAP for SEC registrants. On the effective date of ASC 105, the Codification superseded all then-existing non-SEC accounting and reporting standards. All other non-grandfathered non-SEC accounting literature not included in the Codification has become non-authoritative. ASC 105 is effective for financial statements issued for interim and annual periods ending after September 15, 2009. In the FASB's views, the issuance of ASC 105 and the Codification does not change U.S. GAAP, except for those nonpublic nongovernmental entities that must now apply FASB ASC 985-Software. The Company adopted ASC 105 as of September 30, 2009 with no material impact on the Company's consolidated financial statements.

Internal Control Over Financial Reporting

The objective of the Company's Internal Control Program is to allow the Bank and management to comply with Part 363 of the FDIC's regulations ("FDICIA") and to allow the Company to comply with Section 302 of the Sarbanes-Oxley Act of 2002 (the "Act"). In November 2005, the FDIC amended Part 363 of its regulations by raising the asset-size threshold from $500 million to $1 billion for internal control assessments by management and external auditors. The final rule was effective December 28, 2005.

Section 302 of the Act requires the CEOs and CFOs of the Company to (i) certify that the annual and quarterly reports filed with the Securities and Exchange Commission are accurate and (ii) acknowledge that they are responsible for establishing, maintaining and periodically evaluating the effectiveness of the disclosure controls and procedures. Section 404 of the Act requires management to (i) report on internal control over financial reporting, (ii) assess the effectiveness of such internal controls, and (iii) obtain an external auditor's report on management's assessment of its internal control. The Company is not an accelerated filer as defined in Rule 12b-2 of the Securities Exchange Act of 1934.

On October 2, 2009, the SEC issued a final extension of SOX 404(b) for non-accelerated filers to fiscal years ending on or after June 15, 2010. Therefore, the Company, which would have been first required to comply with Section 404 for the fiscal year ended December 31, 2007, will be required to obtain an external auditor's report on internal control over financial reporting for the fiscal year ending December 31, 2010.

The Committee of Sponsoring Organizations (COSO) methodology may be used to document and test the internal controls pertaining to the accuracy of Company issued financial statements and related disclosures. COSO requires a review of the control environment (including anti-fraud and audit committee effectiveness), risk assessment, control activities, information and communication, and ongoing monitoring.

ITEM 7A. Quantitative and Qualitative Disclosures About Market Risk.

Not Applicable

ITEM 8. Financial Statements and Supplementary Data.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Shareholders
Berkshire Bancorp Inc.

We have audited the accompanying consolidated balance sheets of Berkshire Bancorp Inc. and Subsidiaries (the "Company") as of December 31, 2009 and 2008, and the related consolidated statements of operations, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2009. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company was not required to have, nor were we engaged to perform an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Berkshire Bancorp Inc. and Subsidiaries as of December 31, 2009 and 2008, and the consolidated results of their operations and their consolidated cash flows for each of the three years in the period ended December 31, 2009, in conformity with accounting principles generally accepted in the United States of America.

/s/ GRANT THORNTON LLP

New York, New York
June 9, 2010

BERKSHIRE BANCORP INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(Dollars in Thousands)

	December 31, 2009	December 31, 2008
ASSETS		
Cash and due from banks	$ 5,427	$ 3,290
Interest bearing deposits	55,376	69,097
Federal funds sold	—	30,000
Total cash and cash equivalents	60,803	102,387
Investment Securities:		
Available-for-sale	357,478	297,536
Held-to-maturity, fair value of $337 in 2009 and $362 in 2008	340	360
Total investment securities	357,818	297,896
Loans, net of unearned income	430,349	466,753
Less: allowance for loan losses	(11,416)	(9,204)
Net loans	418,933	457,549
Accrued interest receivable	4,253	5,866
Premises and equipment, net	8,532	8,844
Goodwill, net	18,549	18,549
Trade date securities receivable	—	13,431
Other assets	40,379	39,190
Total assets	$ 909,267	$ 943,712
LIABILITIES AND STOCKHOLDERS' EQUITY		
Deposits:		
Non-interest bearing	$ 62,870	$ 51,312
Interest bearing	650,574	674,797
Total deposits	713,444	726,109
Securities sold under agreements to repurchase	50,000	59,504
Borrowings	31,004	45,272
Subordinated debt	22,681	22,681
Accrued interest payable	3,578	6,522
Other liabilities	3,324	17,672
Total liabilities	824,031	877,760
Stockholders' equity		
Preferred stock - $.01 Par value:		
Authorized — 2,000,000 shares		
Issued — 60,000 shares		
Outstanding —		
December 31, 2009, 60,000 shares		
December 31, 2008, 60,000 shares	1	1
Common stock - $.10 par value	770	770
Authorized — 25,000,000 shares		
Issued — 7,698,285 shares		
Outstanding —		
December 31, 2009, 7,054,183 shares		

December 31, 2008, 7,054,183 shares				
Additional paid-in capital		150,985		150,985
Accumulated Deficit		(46,833)		(39,795)
Accumulated other comprehensive loss, net		(13,276)		(39,598)
Treasury Stock at cost December 31, 2009 and 2008, 644,102 shares		(6,411)		(6,411)
Total stockholders' equity		85,236		65,952
Total liabilities and stockholders' equity	$	909,267	$	943,712

The accompanying notes are an integral part of these statements

BERKSHIRE BANCORP INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
(In Thousands, Except Per Share Data)

	For The Years Ended December 31, 2009	2008	2007
INTEREST INCOME			
Federal funds sold and interest bearing deposits	$ 639	$ 1,380	$ 1,553
Investment securities	15,506	25,456	27,178
Loans, including related fees	29,777	32,754	29,804
Total interest income	45,922	59,590	58,535
INTEREST EXPENSE			
Deposits	12,237	24,968	32,083
Securities sold under agreements to repurchase	2,305	2,344	1,976
Borrowings and subordinated debt	2,561	3,211	3,734
Total interest expense	17,103	30,523	37,793
Net interest income	28,819	29,067	20,742
PROVISION FOR LOAN LOSSES	9,300	4,904	355
Net interest income after provision for loan losses	19,519	24,163	20,387
NON-INTEREST INCOME			
Service charges on deposit accounts	490	585	658
Investment securities gains (losses)	(860)	(685)	86
Other income	567	858	915
Total non-interest income	197	758	1,659
NON-INTEREST EXPENSE			
Total other than temporary impairment ("OTTI") charges on securities	23,748	94,346	—
Less non-credit portion of OTTI recorded in Accumulated other comprehensive loss	6,313	—	—
Net OTTI recognized in earnings	17,435	94,346	—
Salaries and employee benefits	9,517	9,366	8,971
Net occupancy expense	2,150	2,079	2,050
Equipment expense	378	386	80
FDIC assessment	1,928	1,082	86
Data processing expense	452	442	417
Other	3,311	2,915	2,714
Total non-interest expense	35,171	110,616	14,318
Income (loss) before provision for income taxes	(15,455)	(85,695)	7,728
Provision (benefit) for income taxes	(13,217)	(5,790)	2,374
Net income (loss)	$ (2,238)	$ (79,905)	$ 5,354
Dividends on preferred stock	4,800	—	—
Income (loss) allocated to common stockholders	$ (7,038)	$ (79,905)	$ 5,354
Net income (loss) per common share:			
Basic	$ (1.00)	$ (11.45)	$ .77
Diluted	$ (1.00)	$ (11.45)	$ .76
Number of shares used to compute net income (loss) per common share:			
Basic	7,054	7,054	6,987
Diluted	7,054	7,054	7,005

Dividends per common share	$ —	$ .20	$ .18

The accompanying notes are an integral part of these statements

BERKSHIRE BANCORP INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY
For The Years Ended December 31, 2009, 2008 and 2007
(In Thousands)

	Common Shares	Preferred Shares	Common Stock Par value	Preferred Stock Par value	Additional paid-in capital	Accumulated other comprehensive (loss) net	Retained Earnings (Accumulated deficit)	Treasury stock	Comprehensive income (loss)	Total stockholders' equity
Balance at January 1, 2007	7,698		$ 770	$ —	$ 90,659	$ (4,772)	$ 38,250	$ (8,165)		$ 116,742
Net income							5,354		$ 5,354	5,354
Exercise of stock options					(32)			1,754		1,722
Tax benefit from exercise of stock options					359					359
Other comprehensive income net of reclassification adjustment and taxes						1,333			1,333	1,333
Comprehensive income									$ 6,687	
Cash dividends							(1,252)			(1,252)
Balance at December 31, 2007	7,698		770		90,986	(3,439)	42,352	(6,411)		124,258
Net loss							(79,905)		(79,905)	(79,905)
Issuance of Series A Preferred Stock		60		1	59,999					60,000
Other comprehensive loss net of reclassification adjustment and taxes						(36,159)			(36,159)	(36,159)
Comprehensive loss									$ (116,064)	
Cash dividends - Preferred Stock							(837)			(837)
Cash dividends - Common Stock							(1,405)			(1,405)
Balance at December 31, 2008	7,698	60	$ 770	$ 1	$ 150,985	$ (39,598)	$ (39,795)	$ (6,411)		$ 65,952
Net loss							(2,238)		(2,238)	(2,238)
						26,322			26,322	26,322

Other comprehensive income net of taxes										
Comprehensive income									$ 24,084	
Cash dividends - Preferred Stock							(4,800)			(4,800)
Balance at December 31, 2009	7,698	60	$ 770	$ 1	$ 150,985	$ (13,276)	$ (46,833)	$ (6,411)		$ 85,236

The accompanying notes are an integral part of these statements

BERKSHIRE BANCORP INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)

	For The Years Ended December 31, 2009	2008	2007
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net (loss) income	$ (2,238)	$ (79,905)	$ 5,354
Adjustments to reconcile net (loss) income to net cash (used in) provided by operating activities:			
Realized losses (gains) on investment securities	860	685	(86)
Other than temporary impairment charges on securities	17,435	94,346	—
Net amortization (accretion) of premiums of investment securities	721	(225)	(1,339)
Depreciation and amortization	533	604	739
Provision for loan losses	9,300	4,904	355
CHANGES IN ASSETS AND LIABILITIES:			
Decrease (increase) in accrued interest receivable	1,613	2,757	(2,205)
Decrease (increase) in other assets	11,015	(45,767)	1,184
(Decrease) increase in accrued interest payable and other liabilities	(17,292)	12,280	(439)
Net cash provided by (used in) operating activities	21,947	(10,321)	3,563
CASH FLOWS FROM INVESTING ACTIVITIES:			