

SALISBURY BANCORP INC  
Form 10-K  
March 30, 2016

**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM 10-K**

(Mark One)

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

**For the fiscal year ended December 31, 2015**

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

Commission file number 0-24751

**SALISBURY BANCORP, INC.**

(Exact name of registrant as specified in its charter)

Connecticut 06-1514263  
(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

5 Bissell Street, Lakeville, CT 06039  
(Address of principal executive offices) (Zip code)

Registrant's telephone number, including area code: **(860) 435-9801**

Securities registered pursuant to Section 12(b) of the Act::  
Common Stock, par value \$.10 per share NASDAQ Capital Market  
(Title of each class) (Name of each exchange on which registered)

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

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

Edgar Filing: SALISBURY BANCORP INC - Form 10-K

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). 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 registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendments to this Form 10-K.

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 definitions of "large accelerated filer," "accelerated filer," and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

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

The aggregate market value of common stock held by non-affiliates of the registrant on June 30, 2015 was \$73.9 million based on the closing sales price of \$31.69 of such stock. The number of shares of the registrant's Common Stock outstanding as of March 1, 2016, was 2,753,426.

**DOCUMENTS INCORPORATED BY REFERENCE**

Portions of the registrant's definitive Proxy Statement for the 2016 Annual Meeting of Shareholders to be held on May 18, 2016, which will be filed within 120 days of fiscal year ended December 31, 2015, are incorporated by reference into Part III (Items 10, 11, 12, 13 and 14) of this Form 10-K.

**FORM 10-K****SALISBURY BANCORP, INC.**

For the Year Ended December 31, 2015

**TABLE OF CONTENTS**

Description	Page
<b>PART I</b>	
Item 1. BUSINESS	3
Item 1A. RISK FACTORS	15
Item 1B. UNRESOLVED STAFF COMMENTS	19
Item 2. PROPERTIES	19
Item 3. LEGAL PROCEEDINGS	19
Item 4. MINE SAFETY DISCLOSURES	20
<b>PART II</b>	
Item 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED SHAREHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES	21
Item 6. SELECTED FINANCIAL DATA	22
Item 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS	23
Item 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK	43
Item 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA	45
Item 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE	96
Item 9A. CONTROLS AND PROCEDURES	96
Item 9B. OTHER INFORMATION	96
<b>PART III</b>	
Item 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE	96
Item 11. EXECUTIVE COMPENSATION	97
Item 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED SHAREHOLDER MATTERS	97
Item 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE	97
Item 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES	97
<b>PART IV</b>	
Item 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES	97

## PART I

## Forward-Looking Statements

This Annual Report on Form 10-K may contain and incorporates by reference statements relating to future results of Salisbury Bancorp, Inc. (the "Company") and its Subsidiary, Salisbury Bank and Trust Company (the "Bank") (collectively, "Salisbury"), that are considered "forward-looking" within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements can be identified by words such as "believes," "anticipates," "expects," "intends," "targeted," "continue," "remain," "will," "should," "may," "plans," "estimates," and similar references to future periods; however, such words are not the exclusive means of identifying such statements. These statements relate to, among other things, expectations concerning loan demand, growth and performance, simulated changes in interest rates and the adequacy of the allowance for loan losses. Actual results may differ materially from those expressed or implied as a result of certain risks and uncertainties, including, but not limited to, changes in political and economic conditions, interest rate fluctuations, competitive product and pricing pressures within Salisbury's markets, equity and fixed income market fluctuations, personal and corporate customers' bankruptcies, inflation, acquisitions and integrations of acquired businesses, technological changes and cybersecurity matters, changes in law and regulations, changes in fiscal, monetary, regulatory and tax policies, monetary fluctuations, success in gaining regulatory approvals when required as well as other risks and uncertainties reported from time to time in Salisbury's filings with the Securities and Exchange Commission. See also, the "Risk Factors" set forth below.

Forward-looking statements made by Salisbury in this Annual Report on Form 10-K speaks only as of the date they are made. Events or other facts that could cause Salisbury's actual results to differ may arise from time to time, and Salisbury cannot predict all such events and factors. Salisbury undertakes no obligation to publicly update any forward-looking statement, unless as may be required by law.

## Item 1. BUSINESS

Salisbury Bancorp, Inc.

Salisbury Bancorp, Inc., a Connecticut corporation, formed in 1998, is the bank holding company for Salisbury Bank and Trust Company (the "Bank"), a Connecticut-chartered and Federal Deposit Insurance Corporation (the "FDIC") insured commercial bank headquartered in Lakeville, Connecticut. Salisbury's common stock is traded on the NASDAQ Capital Market under the symbol "SAL." Salisbury's principal business consists of its operation and control of the business of the Bank.

The Bank, formed in 1848, currently provides commercial banking, consumer financing, retail banking and trust and wealth advisory services through a network of thirteen banking offices and nine ATMs located in: Litchfield County, Connecticut; Dutchess and Orange Counties, New York; and Berkshire County, Massachusetts and through its internet website ([salisburybank.com](http://salisburybank.com)).

## Abbreviations Used Herein

Bank	Salisbury Bank and Trust Company	FRA	Federal Reserve Act
BHC	Bank Holding Company	FRB	Federal Reserve Board
BHCA	Bank Holding Company Act	GAAP	Generally Accepted Accounting Principles in the United States of America
BOLI	Bank Owned Life Insurance	GLBA	Gramm-Leach-Bliley Act
CFPB	Consumer Financial Protection Bureau	LIBOR	London Interbank Offered Rate
CPP	Capital Purchase Program	OREO	Other Real Estate Owned
CRA	Community Reinvestment Act of 1977	OTTI	Other Than Temporarily Impaired
CTDOB		PIC	Passive Investment Company

State of Connecticut Department of  
Banking

Dodd- Frank Act	Dodd-Frank Wall Street Reform and Consumer Protection Act		Salisbury	Salisbury Bancorp, Inc. and Subsidiary
ESOP	Employee Stock Ownership Plan	SBLF		Small Business Lending Fund
FACT Act	Fair and Accurate Credit Transactions Act	SEC		Securities and Exchange Commission
FASB	Financial Accounting Standards Board	SOX		Sarbanes-Oxley Act of 2002
FDIC	Federal Deposit Insurance Corporation	TARP		Troubled Asset Relief Program
FHLBB	Federal Home Loan Bank of Boston	Treasury		United States Department of the Treasury

#### Lending Activities

##### General

The Bank originates commercial loans, commercial real estate loans, residential and commercial construction loans, residential real estate loans collateralized by one-to-four family residences, home equity lines of credit and fixed rate loans and other consumer loans predominately in Connecticut's Litchfield County, New York's Dutchess, Orange and Ulster Counties and Massachusetts' Berkshire County in towns proximate to the Bank's thirteen full service offices.

The majority of the Bank's loans as of December 31, 2015, including some loans classified as commercial loans, were secured by real estate. Interest rates charged on loans are affected principally by the Bank's current asset/liability strategy, the demand for such loans, the cost and supply of money available for lending purposes and the rates offered by competitors. These factors are, in turn, affected by general economic and credit conditions, monetary policies of the federal government, including the FRB, federal and state tax policies and budgetary matters. Loan portfolios acquired in business combinations include commercial loans acquired with Riverside Bank.

#### Residential Real Estate Loans

A principal lending activity of the Bank is to originate loans secured by first mortgages on one-to-four family residences. The Bank typically originates residential real estate loans through employees who are commissioned licensed mortgage originators (in accordance with the mortgage lending compensation guidelines issued by the CFPB). The Bank originates both fixed rate and adjustable rate mortgages.

The Bank currently sells the majority of the fixed rate 30 year residential mortgage loans it originates to the FHLBB under the Mortgage Partnership Finance program. The Bank typically retains loan servicing. The Bank retains some fixed rate residential mortgage loans and those loans originated under its first time home owner program.

The retention of adjustable rate residential mortgage loans in the portfolio and the sale of longer term, fixed rate residential mortgage loans helps reduce the Bank's exposure to interest rate risk. However, adjustable rate mortgages generally pose credit risks different from the credit risks inherent in fixed rate loans primarily because as interest rates rise, the underlying debt service payments of the borrowers rise, thereby increasing the potential for default. Management believes that these risks, which have not had a material adverse effect on the Bank to date, generally are less onerous than the interest rate risks associated with holding long-term fixed rate loans in the loan portfolio.

#### Commercial Real Estate Loans

The Bank makes commercial real estate loans for the purpose of allowing borrowers to acquire, develop, construct, improve or refinance commercial real estate where the property is the primary collateral securing the loan, and the income generated from the property is the primary repayment source. Office buildings, light industrial, retail facilities or multi-family income properties, normally collateralize commercial real estate loans. Among the reasons for management's continued emphasis on commercial real estate lending is the desire to invest in assets with yields which are generally higher than yields on one-to-four family residential mortgage loans, and are more sensitive to changes in interest rates. These loans typically have terms/amortizations of up to ten and twenty five years, respectively, and interest rates, which adjust over periods of three to ten years, based on one of various rate indices.

Commercial real estate lending generally poses a greater credit risk than residential mortgage lending to owner-occupants. The repayment of commercial real estate loans depends on the business and financial condition of the borrower. Economic events and changes in government regulations, which the Bank and its borrowers do not control, could have an adverse impact on the cash flows generated by properties securing commercial real estate loans and on the market value of such properties.

#### Construction Loans

The Bank originates both residential and commercial construction loans. Typically, loans are made to owner-borrowers who will occupy the properties as either their primary or secondary residence and to licensed and experienced developers for the construction of single-family homes or commercial properties.

The proceeds of commercial construction loans are disbursed in stages. Bank officers, appraisers and/or independent engineers inspect each project's progress before additional funds are disbursed to verify that borrowers have completed project phases.

Residential construction loans to owner-borrowers generally convert to a fully amortizing long-term mortgage loan upon completion of construction. The typical construction phase is generally twelve months.

Construction lending, particularly commercial construction lending, poses greater credit risk than mortgage lending to owner-occupants. The repayment of commercial construction loans depends on the business, the financial condition of the borrower, and on the economic viability of the project financed. Economic events and changes in government regulations, which the Bank and its borrowers do not control, could have an adverse impact on the value of properties securing construction loans and on the borrower's ability to complete projects financed and sell them for amounts anticipated at the time the projects commenced.

### Commercial Loans

Commercial loans are generally made on a secured basis and are primarily collateralized by equipment, inventory, accounts receivable and/or leases. Commercial loans primarily provide working capital, equipment financing, financing for leasehold improvements and financing for expansion. The Bank offers both term and revolving commercial loans. Term loans have either fixed or adjustable rates of interest and, generally, terms of between two and seven years. Term loans generally amortize during their life, although some loans require a balloon payment at maturity if the amortization exceeds seven years. Revolving commercial lines of credit typically are renewable annually and have a floating rate of interest normally indexed to the prime rate as published in the Wall Street Journal.

Commercial lending generally poses a higher degree of credit risk than real estate lending. Repayment of both secured and unsecured commercial loans depends substantially on the success of the borrower's underlying business, financial condition and cash flows. Unsecured loans generally involve a higher degree of risk of loss than do secured loans because, without collateral, repayment is primarily dependent upon the success of the borrower's business.

Secured commercial loans are generally collateralized by equipment, inventory, accounts receivable and leases. Compared to real estate, such collateral is more difficult to monitor, its value is more difficult to validate, it may depreciate more rapidly and it may not be as readily saleable if repossessed.

### Consumer Loans

The Bank originates various types of consumer loans, including home equity loans and lines of credit, auto and personal installment loans. Home equity loans and lines of credit are generally secured by second mortgages placed on one-to-four family owner-occupied properties. Home equity loans have fixed interest rates, while home equity lines of credit adjust based on the prime rate as published in the Wall Street Journal. Consumer loans are originated through the branch network with the exception of Home Equity Lines of Credit, which are originated by licensed Mortgage Lending Originator staff.

### Credit Risk Management and Asset Quality

One of the Bank's key objectives is to maintain a high level of asset quality. The Bank utilizes the following general practices to manage credit risk: ensuring compliance with prudent written policies; limiting the amount of credit that individual lenders may extend; establishing a process for credit approval accountability; careful initial underwriting and analysis of borrower, transaction, market and collateral risks; ongoing servicing of individual loans and lending relationships; continuous monitoring and risk rating of the portfolio, market dynamics and the economy; and periodically reevaluating the Bank's strategy and overall exposure as economic, market and other relevant conditions change.

Credit Administration is responsible for determining loan loss reserve adequacy and preparing monthly and quarterly reports regarding the credit quality of the loan portfolio, which are submitted to the Loan Committee to ensure compliance with the credit policy, and managing non-performing and classified assets as well as oversight of all collection activity. On a quarterly basis, the Loan Committee reviews commercial and commercial real estate loans that are risk rated as "Special Mention" or worse, focusing on the current status and strategies to improve the credit.

The Bank's loan review activities are performed by an independent third party loan review firm that evaluates the creditworthiness of borrowers and the appropriateness of the Bank's risk rating classifications. The firm's findings are reported to Credit Administration, Senior Management, and the Board level Loan and Audit Committees.

### Trust and Wealth Advisory Services



The Bank provides a range of fiduciary and trust services including general investment management, wealth advisory services to individuals, families and institutions, and estate administration and settlement services.

#### Securities

Salisbury's securities portfolio is structured to diversify the earnings, assets and risk structure of Salisbury, provide liquidity consistent with both projected and potential needs, collateralize certain types of deposits, assist with maintaining a satisfactory net interest margin and comply with regulatory capital and liquidity requirements. Types of securities in the portfolio generally include U.S. Government and Agency securities, mortgage-backed securities, collateralized mortgage obligations and tax exempt municipal bonds.

#### Sources of Funds

The Bank uses deposits, proceeds from loan and security maturities, repayments and sales, and borrowings to fund lending, investing and general operations. Deposits represent the Bank's primary source of funds.

## Deposits

The Bank offers a variety of deposit accounts with a range of interest rates and other terms, which are designed to meet customer financial needs. Retail and commercial deposits are primarily received through the Bank's banking offices. Additional depositor related services provided to customers include Landlord/Tenant Lease Security Accounts and Services, Merchant Services, Payroll Services, Cash Management (Remote Deposit Capture, ACH Origination, Wire Transfers and Positive Pay), ATM, Bank-by-Phone, Internet Banking, Internet Bill Pay, Person to Person Payments, Bank to Bank Transfers, Mobile Banking with remote deposit, and Online Financial Management with Account Aggregation Services.

The FDIC provides separate insurance coverage of \$250,000 per depositor for each account ownership category. Deposit flows are significantly influenced by economic conditions, the general level of interest rates and the relative attractiveness of competing deposit and investment alternatives. When determining deposit pricing, the Bank considers strategic objectives, competitive market rates, deposit flows, funding commitments and investment alternatives, FHLBB advance rates and rates on other sources of funds.

National, regional and local economic and credit conditions, changes in competitor money market, savings and time deposit rates, prevailing market interest rates and competing investment alternatives all have a significant impact on the level of the Bank's deposits. Deposit generation is a key focus for the Bank as a source of liquidity and to fund continuing asset growth. Competition for deposits has been, and is expected to, remain strong.

## Borrowings

The Bank is a member of the FHLBB, which provides credit facilities for regulated, federally insured depository institutions and certain other home financing institutions. Members of the FHLBB are required to own capital stock in the FHLBB and are authorized to apply for advances on the security of their FHLBB stock and certain home mortgages and other assets (principally securities, which are obligations of, or guaranteed by, the United States Government or its agencies) provided certain creditworthiness standards have been met. Under its current credit policies, the FHLBB limits advances based on a member's assets, total borrowings and net worth. Long-term and short-term FHLBB advances may be utilized as a source of funding to meet liquidity and planning needs when the cost of these funds is favorable as compared to deposits or alternate funding sources. Long-Term Debt increased \$10 million at December 31, 2015 as a result of the issuance of subordinated debentures during 2015; See "Deposits and Borrowings" below.

Additional funding sources are available through securities sold under agreements to repurchase and the Federal Reserve Bank of Boston.

## **Acquisitions**

On June 6, 2014, the Bank completed its purchase and assumption of the Sharon, Connecticut branch of Union Savings Bank, which included deposits of approximately \$18 million at a premium of 2.32%. Operations of the Bank's existing Sharon, Connecticut branch were consolidated into this new location. On December 5, 2014, the Bank completed its acquisition of Riverside Bank of Poughkeepsie, New York, adding four new offices and a strong commercial loan focus to Salisbury's New York market presence. Such transaction was valued at approximately \$27 million. In the merger, Riverside Bank shareholders received 1.35 shares of Salisbury Bancorp, Inc. common stock for each share of Riverside Bank common stock.

## Subsidiaries

Salisbury has one wholly-owned subsidiary, Salisbury Bank and Trust Company. The Bank has two wholly-owned subsidiaries, SBT Mortgage Service Corporation and S.B.T. Realty, Inc. SBT Mortgage Service Corporation is a passive investment company ("PIC") that holds loans collateralized by real estate originated or purchased by the Bank. Income of the PIC and its dividends to Salisbury are exempt from the Connecticut Corporate Business Tax. S.B.T. Realty, Inc. was formed to hold New York state real estate and is presently inactive.

#### Employees

At December 31, 2015, the Bank had 158 full-time employees and 30 part-time employees. The employees are not represented by a collective bargaining group. The Bank maintains a comprehensive employee benefit program providing, among other benefits, group medical and dental insurance, life insurance, disability insurance, an ESOP and an employee 401(k) plan. Management considers relations with its employees to be good.

#### Market Area

Salisbury and the Bank are headquartered in Lakeville, Connecticut, which is located in the northwestern quadrant of Connecticut's Litchfield County. The Bank has a total of thirteen banking offices, four of which are located in Connecticut's Litchfield County; three of which are located in Massachusetts' Berkshire County; five of which are located in New York's Dutchess County, and one of which is located in New York's Orange County. The Bank's primary deposit gathering and lending area consists of the communities and surrounding towns that are served by its branch network in these counties. The Bank also has deposit, lending and trust relationships outside of these areas.

## Competition

The Bank faces strong competition in attracting and retaining deposits and in making loans. The primary factors in competing for deposits are interest rates, personalized services, the quality and range of financial services, convenience of office locations, automated services and office hours. Its most direct competition for deposits and loans has come from other commercial banks, savings institutions and credit unions located in its market area. Competition for deposits also comes from mutual funds and other investment alternatives, which offer a range of deposit and deposit-like products. Although the Bank expects this continuing competition to have an effect upon the cost of funds, it does not anticipate any substantial adverse effect on maintaining the current deposit base. The Bank is competitive within its market area in the various deposit products it offers to depositors. Due to this fact, management believes the Bank has the ability to maintain its deposit base.

The Bank's competition for real estate loans comes primarily from mortgage banking companies, savings banks, commercial banks, insurance companies, and other institutional lenders. The primary factors in competing for loans are interest rates, loan origination fees, the quality and range of lending services and personalized service. Factors that affect competition include, among others, the general availability of funds and credit, general and local economic conditions, current interest rate levels and volatility in the mortgage markets.

The banking industry is also experiencing rapid changes in technology. In addition to improving customer services, effective use of technology increases efficiency and enables financial institutions to reduce costs. Technological advances are likely to increase competition by enabling more companies to provide cost effective products and services.

## Regulation and Supervision

### General

Salisbury is required to file reports and otherwise comply with the rules and regulations of the FRB, the FDIC, the SEC and NASDAQ as well as the state banking supervisory authorities in Connecticut, New York and Massachusetts.

The Bank is subject to extensive regulation by the CTDOB, as its chartering agency, and by the FDIC, as its deposit insurer. The Bank is required to file reports with, and is periodically examined by, the FDIC and the CTDOB concerning its activities and financial condition. It must obtain regulatory approvals prior to entering into certain transactions, such as mergers.

The following discussion of the laws, regulations and policies material to the operations of Salisbury and the Bank is a summary and is qualified in its entirety by reference to such laws, regulations and policies. Such statutes, regulations and policies are continually under review by Congress and the Connecticut, New York and Massachusetts State Legislatures and federal and state regulatory agencies. Any change in such laws, regulations, or policies could have a material adverse impact on Salisbury or the Bank.

### Bank Holding Company Regulation

#### *SEC and NASDAQ*

Salisbury is subject to the rules and regulations of the SEC and is required to comply with the disclosure and regulatory requirements of the Securities Act of 1933, as amended, and the Securities Exchange Act of 1934, as amended, as administered by the SEC. Salisbury's common stock is listed on the NASDAQ Capital Market under the trading symbol "SAL" and, accordingly, Salisbury is also subject to the rules of NASDAQ for listed companies.

*Federal Reserve Board Regulation*

Salisbury is a registered bank holding company under the BHCA and is subject to comprehensive regulation and regular examinations by the FRB. The FRB also has extensive enforcement authority over bank holding companies, including, among other things, the ability to assess civil money penalties, to issue cease and desist or removal orders and to require that a holding company divest subsidiaries (including its bank subsidiaries). In general, enforcement actions may be initiated for violations of law and regulations and unsafe or unsound practices.

Under FRB policy, a bank holding company must serve as a source of financial and managerial strength for its subsidiary bank. Under this policy, Salisbury is expected to commit resources to support the Bank. The FRB may require a holding company to contribute additional capital to an undercapitalized subsidiary bank.

Bank holding companies must obtain FRB approval before: (i) acquiring, directly or indirectly, ownership or control of another bank or bank holding company; (ii) acquiring all or substantially all of the assets of another bank or bank holding company; or (iii) merging or consolidating with another bank holding company.

The BHCA also prohibits a bank holding company, with certain exceptions, from acquiring direct or indirect ownership or control of any company, which is not a bank or bank holding company, or from engaging directly or indirectly in activities other than those of banking, managing or controlling banks, or providing services for its subsidiaries. The principal exceptions to these prohibitions involve certain non-bank activities, which, by statute or by FRB regulation or order, have been identified as activities closely related to the business of banking or managing or controlling banks. The list of activities permitted by the FRB includes, among other things: (i) operating a savings institution, mortgage company, finance company, credit card company or factoring company; (ii) performing certain data processing operations; (iii) providing certain investment and financial advice; (iv) underwriting and acting as an insurance agent for certain types of credit-related insurance; (v) leasing property on a full-payout, non-operating basis; (vi) selling money orders; (vii) real estate and personal property appraising; (viii) providing tax planning and preparation services; (ix) financing and investing in certain community development activities; and (x) subject to certain limitations, providing securities brokerage services for customers.

#### *Connecticut Bank Holding Company Regulation*

Salisbury is a Connecticut corporation and is also subject to the Connecticut Business Corporation Act and Connecticut banking law applicable to Connecticut bank holding companies. Under Connecticut banking law, no person may acquire beneficial ownership of more than 10% of any class of voting securities of a Connecticut-chartered bank, or any bank holding company of such a bank, without prior notification to, and lack of disapproval by, the CTDOB. The CTDOB will disapprove the acquisition if the bank or holding company to be acquired has been in existence for less than five years, unless the CTDOB waives this five-year restriction, or if the acquisition would result in the acquirer controlling 30% or more of the total amount of deposits in insured depository institutions in Connecticut. Similar restrictions apply to any person who holds in excess of 10% of any such class and desires to increase its holdings to 25% or more of such class.

#### Dividends

Salisbury's dividends to shareholders are substantially dependent upon Salisbury's receipt of dividends from the Bank. The FRB has issued a policy statement on the payment of cash dividends by bank holding companies, which expresses the FRB's view that a bank holding company should be a "source of strength" to its bank subsidiary and should pay cash dividends only to the extent that the holding company's net income for the past year is sufficient to cover both the cash dividends and a rate of earnings retention that is consistent with the holding company's capital needs, asset quality and overall financial condition. The FRB also indicated its view that, generally, it would be inappropriate for a company experiencing serious financial problems to borrow funds to pay dividends. Furthermore, the FRB may prohibit a bank holding company from paying any dividends if the holding company's bank subsidiary is classified as "undercapitalized" or if the dividend would violate applicable law or would be an unsafe or unsound banking practice.

#### Financial Modernization

GLBA permits greater affiliation among banks, securities firms, insurance companies, and other companies under a type of financial services company known as a "financial holding company." A financial holding company essentially is a bank holding company with expanded powers. Financial holding companies are authorized by statute to engage in a number of financial activities previously impermissible for bank holding companies, including securities underwriting, dealing and market making; sponsoring mutual funds and investment companies; insurance underwriting and agency; and merchant banking activities. The act also permits the FRB and the Treasury to authorize additional activities for financial holding companies if they are "financial in nature" or "incidental" to financial activities. A bank holding company may become a financial holding company if each of its subsidiary banks is "well capitalized" and "well managed" as defined in the FRB's Regulation Y, and has at least a "satisfactory" Community Reinvestment Act rating. A financial holding company must provide notice to the FRB within 30 days after commencing activities previously determined to be permissible by statute or by the FRB and the Treasury. Salisbury is a registered financial

holding company.

All financial institutions are required to establish policies and procedures with respect to the ability of the Bank to share nonpublic customer data with nonaffiliated parties and to protect customer data from unauthorized access. The Bank has developed policies and procedures, and believes it is in compliance with all privacy, information sharing, and notification provisions of GLBA and the FACT Act.

#### Connecticut Banking Laws and Supervision

The Bank is a state-chartered commercial bank under Connecticut law and as such is subject to regulation and examination by the CTDOB. The CTDOB regulates commercial banks, among other financial institutions, for compliance with the laws and regulations of the States of Connecticut, New York and Massachusetts, as well as the appropriate rules and regulations of federal agencies. The approval of the CTDOB is required for, among other things, the establishment of branch offices and business combination transactions. The CTDOB conducts periodic examinations of Connecticut-chartered banks. The FDIC also regulates many of the areas regulated by the CTDOB, and federal law may limit some of the authority provided to Connecticut-chartered banks by Connecticut law.

#### Lending Activities

Connecticut banking laws grant commercial banks broad lending authority. With certain limited exceptions, total secured and unsecured loans made to any one obligor generally may not exceed 15% of the Bank's equity capital and reserves for loan and lease losses. However, if the loan is fully secured, such limitations generally may be increased by an additional 10%.

## Dividends

The Bank may pay cash dividends out of its net profits. For purposes of this restriction, “net profits” represents the remainder of all earnings from current operations. Further, the total amount of all dividends declared by the Bank in any year may not exceed the sum of its net profits for the year in question combined with its retained net profits from the preceding two years, unless the CTDOB approves the larger dividend. Federal law also prevents the Bank from paying dividends or making other capital distributions that would cause it to become “undercapitalized.” The FDIC may also limit a bank’s ability to pay dividends based upon safety and soundness considerations.

## Powers

Connecticut law permits Connecticut banks to sell insurance and fixed and variable-rate annuities if licensed to do so by the Connecticut Insurance Department. With the prior approval of the CTDOB, Connecticut banks are also authorized to engage in a broad range of activities related to the business of banking, or that are financial in nature or that are permitted under the BHCA, other federal statutes, or the regulations promulgated pursuant to these statutes. Connecticut banks generally are also authorized to engage in any activity permitted for a federal bank or upon filing prior written notice of its intention to engage in such activity with the CTDOB, unless the CTDOB disapproves the activity.

## Assessments

Connecticut banks are required to pay assessments to the CTDOB based upon a bank’s asset size to fund the CTDOB’s operations. The assessments are generally made annually.

## Enforcement Authority

Under Connecticut law, the CTDOB has extensive enforcement authority over Connecticut banks and, under certain circumstances, affiliated parties, insiders, and agents. The CTDOB’s enforcement authority includes cease and desist orders, fines, receivership, conservatorship, removal of officers and directors, emergency closures, dissolution and liquidation.

## New York and Massachusetts Banking Laws and Supervision

The Bank conducts activities and operates branch offices in New York and Massachusetts as well as Connecticut. Generally, with respect to its business in New York and Massachusetts, the Bank may conduct any activity that is authorized under Connecticut law that is permissible for either New York or Massachusetts state banks or for an out-of-state national bank, at its New York and Massachusetts branch offices, respectively. The New York State Superintendent of Banks may exercise regulatory authority with respect to the Bank’s New York branch offices. The Bank is subject to certain rules related to community reinvestment, consumer protection, fair lending, establishment of intra-state branches and the conduct of banking activities with respect to its branches located in New York State. The Massachusetts Commissioner of Banks may exercise similar authority, and the Bank is subject to similar rules under Massachusetts Banking Law with respect to the Bank’s Massachusetts branch offices. Federal and state laws authorize the interstate merger of banks. Among other things, banks may establish new branches on an interstate basis provided that such action is specifically authorized by the law of the host state.

## Federal Regulations

## Capital Requirements



Under FDIC regulations, federally insured state-chartered banks, such as the Bank, that are not members of the Federal Reserve System (“state non-member banks”) are required to comply with minimum leverage capital requirements. A common equity Tier 1 capital to risk-based assets ratio of 4.5%, a Tier 1 capital to risk-based assets ratio of 6.0%, a total capital to risk-based assets of 8.0%, and a 4.0% Tier 1 capital to total assets leverage ratio. The existing capital requirements were effective January 1, 2015 and are the result of a final rule implementing regulatory amendments based on recommendations of the Basel Committee on Banking Supervision and certain requirements of the Dodd-Frank Act. Common equity Tier 1 capital is generally defined as common stockholders’ equity and retained earnings. Tier 1 capital is generally defined as common equity Tier 1 and additional Tier 1 capital. Additional Tier 1 capital includes certain noncumulative perpetual preferred stock and related surplus and minority interests in equity accounts of consolidated subsidiaries. Total capital includes Tier 1 capital (common equity Tier 1 capital plus additional Tier 1 capital) and Tier 2 capital. Tier 2 capital is comprised of capital instruments and related surplus, meeting specified requirements, and may include cumulative preferred stock and long-term perpetual preferred stock, mandatory convertible securities, intermediate preferred stock and subordinated debt. Also included in Tier 2 capital is the allowance for loan and lease losses limited to a maximum of 1.25% of risk-weighted assets and, for institutions that have exercised an opt-out election regarding the treatment of accumulated other comprehensive income (“AOCI”), up to 45% of net unrealized gains on available-for-sale equity securities with readily determinable fair market values. The Bank chose the opt-out election. Institutions that have not exercised the AOCI opt-out have AOCI incorporated into common equity Tier 1 capital (including unrealized gains and losses on available-for-sale securities). Calculation of all types of regulatory capital is subject to deductions and adjustments specified in the regulations.

The FDIC regulations require state non-member banks to maintain certain levels of regulatory capital in relation to regulatory risk-weighted assets. The ratio of regulatory capital to regulatory risk-weighted assets is referred to as a bank's "risk-based capital ratio." Risk-based capital ratios are determined by allocating assets and specified off-balance sheet items (including recourse obligations, direct credit substitutes and residual interests) to risk-weighted categories ranging from 0% to 1,250%, with higher levels of capital being required for the categories perceived as representing greater risk.

In addition to establishing the minimum regulatory capital requirements, the regulations limit capital distributions and certain discretionary bonus payments to management if the institution does not hold a "capital conservation buffer" consisting of 2.5% of common equity Tier 1 capital to risk-weighted asset above the amount necessary to meet its minimum risk-based capital requirements. The capital conservation buffer requirement is being phased in beginning January 1, 2016 at 0.625% of risk-weighted assets and increasing each year until fully implemented at 2.5% on January 1, 2019.

In assessing an institution's capital adequacy, the FDIC takes into consideration not only these numeric factors, but qualitative factors as well, and has the authority to establish higher capital requirements for individual institutions where deemed necessary. As a bank holding company, the Company is also subject to regulatory capital requirements, as described in a subsequent section.

As a bank holding company, Salisbury is subject to FRB capital adequacy guidelines for bank holding companies similar to those of the FDIC for state-chartered banks.

In July 2013, the FRB approved the final rules implementing the Basel Committee on Banking Supervision's capital guidelines for bank holding companies and their bank subsidiaries. On July 9, 2013, the FDIC also approved, as an interim final rule, the regulatory capital requirements for U.S. banks, following the actions of the FRB. On April 8, 2014, the FDIC adopted as final its interim final rule, which is identical in substance to the final rules issued by the FRB in July 2013. Under the final rules, minimum requirements will increase for both the quantity and quality of capital held by the Bank and Company. The rules include a new common equity Tier 1 capital risk-weighted assets minimum ratio of 4.5%, raise the minimum ratio of Tier 1 capital to risk-weighted assets from 4.0% to 6.0%, require a minimum ratio of Total capital to risk-weighted assets of 8.0%, and require a minimum Tier 1 leverage ratio of 4.0%. A new capital conservation buffer, comprised of common equity Tier 1 capital, is also established above the regulatory minimum capital requirements. This capital conservation buffer is being phased in effective January 1, 2016 at 0.625% of risk-weighted assets and increase each subsequent year by an additional 0.625% until reaching its final level of 2.5% on January 1, 2019. Strict eligibility criteria for regulatory capital instruments were also implemented under the final rules.

The phase-in period for the final rules began for Salisbury on January 1, 2015. As of December 31, 2015, the Company and the Bank met each of their capital requirements and the most recent notification from the FDIC categorized the Bank as "well-capitalized." There are no conditions or events since that notification that management believes have changed the Bank's category.

#### Prompt Corrective Regulatory Action

Federal law requires, among other things, that federal bank regulatory authorities take "prompt corrective action" with respect to banks that do not meet minimum capital requirements. For these purposes, the law establishes five capital categories:

• Well capitalized – at least 5% leverage capital, 6.5% Common Equity Tier 1 capital, 8% Tier 1 risk based capital and 10% total risk based capital.

Adequately capitalized – at least 4% leverage capital, 4.5% Common Equity Tier 1 capital, 6% Tier 1 risk based capital and 8% total risk based capital.

Undercapitalized – less than 4% leverage capital, 4.5% Common Equity Tier 1 capital, 6% Tier 1 risk based capital and 8% total risk based capital. “Undercapitalized” banks must adhere to growth, capital distribution (including dividend) and other limitations and are required to submit a capital restoration plan. A bank’s compliance with such a plan is required to be guaranteed by any company that controls the undercapitalized institution in an amount equal to the lesser of 5% of the institution’s total assets when deemed undercapitalized or the amount necessary to achieve the status of adequately capitalized.

Significantly undercapitalized – less than 3% leverage capital, 3% Common Equity Tier 1 capital, 4% Tier 1 risk based capital and 6% total risk based capital. “Significantly undercapitalized” banks must comply with one or more of a number of additional restrictions, including but not limited to an order by the FDIC to sell sufficient voting stock to become adequately capitalized, requirements to reduce total assets, cease receipt of deposits from correspondent banks or dismiss directors or officers, and restrictions on interest rates paid on deposits, compensation of executive officers and capital distributions by the parent holding company.

Critically undercapitalized – less than 2% tangible capital. “Critically undercapitalized” institutions are subject to additional measures including, subject to a narrow exception, the appointment of a receiver or conservator within 270 days after it obtains such status.

### *Transactions with Affiliates*

Under federal law, transactions between depository institutions and their affiliates are governed by Sections 23A and 23B of the FRA. In a holding company structure, at a minimum, the parent holding company of a bank, and any companies that are controlled by such parent holding company are deemed affiliates of its subsidiary bank. Generally, Sections 23A and 23B are intended to protect insured depository institutions from suffering losses arising from transactions with non-insured affiliates, by limiting the extent to which a bank or its subsidiaries may engage in covered transactions with any one affiliate and with all affiliates of the bank in the aggregate, and by requiring that such transactions be on terms that are consistent with safe and sound banking practices.

The FRA and Regulation O impose restrictions on loans to directors, executive officers, and principal shareholders (“insiders”). Loans to insiders and their related interests may not exceed, together with all other outstanding loans to such persons and affiliated entities, the institution’s total capital and surplus. Loans to insiders above specified amounts must receive the prior approval of the board of directors and must be made on terms substantially the same as offered in comparable transactions to other persons. The FRA imposes additional limitations on loans to executive officers.

### Enforcement

The FDIC has extensive enforcement authority over insured banks, including the Bank. This enforcement authority includes, among other things, the ability to assess civil money penalties, issue cease and desist orders and remove directors and officers. In general, these enforcement actions may be initiated in response to violations of laws and regulations and unsafe or unsound practices.

### Standards for Safety and Soundness

The FDIC, together with the other federal bank regulatory agencies, prescribe standards of safety and soundness by regulations or guidelines, relating generally to operations and management, asset growth, asset quality, earnings, stock valuation and compensation. The federal bank regulatory agencies have adopted a set of guidelines prescribing safety and soundness standards, which establish general standards relating to internal controls and information systems, internal audit systems, loan documentation, credit underwriting, interest rate exposure, asset growth, and compensation, fees and benefits. In general, the guidelines require, among other things, appropriate systems and practices to identify and manage the risks and exposures specified in the guidelines. The guidelines prohibit excessive compensation as an unsafe and unsound practice and describe compensation as excessive when the amounts paid are unreasonable or disproportionate to the services performed by an executive officer, employee, director or principal shareholder. In addition, the federal bank regulatory agencies adopted regulations that authorize, but do not require, the agencies to order an institution that has been given notice that it is not satisfying the safety and soundness guidelines to submit a compliance plan. The federal bank regulatory agencies have also adopted guidelines for asset quality and earning standards. As a state-chartered bank, the Bank is also subject to state statutes, regulations and guidelines relating to safety and soundness, in addition to the federal requirements.

### Insurance of Deposit Accounts

The Bank’s deposit accounts are insured by the Deposit Insurance Fund (“DIF”) of the FDIC up to applicable legal limits (generally, \$250,000 per depositor for each account ownership category and \$250,000 for certain retirement plan accounts) and are subject to deposit insurance assessments. The FDIC insurance coverage limit applies per depositor, per insured depository institution for each account ownership category.

The FDIC utilizes a risk-based assessment system that imposes insurance premiums based upon a risk matrix that takes into account a bank’s capital level and supervisory rating. The FDIC assigns an institution to one of the following capital categories based on the institution’s financial condition consisting of (1) well capitalized, (2) adequately

capitalized or (3) undercapitalized, and one of three supervisory subcategories within each capital group. The supervisory subgroup to which an institution is assigned is based on a supervisory evaluation provided to the FDIC by the institution's primary federal regulator and information which the FDIC determines to be relevant to the institution's financial condition and the risk posed to the deposit insurance funds. An institution's assessment rate depends on the capital category and supervisory category to which it is assigned.

FDIC insured institutions are required to pay assessments to the FDIC to fund the DIF. The Bank's current annual assessment rate is approximately 8.6 basis points of total assets. Additionally, FDIC insured institutions are required to pay assessments to the FDIC to fund interest payments on bonds issued by The Financing Corporation, an agency of the federal government established to recapitalize the predecessor to the Savings Association Insurance Fund. The assessment rate is adjusted quarterly to reflect changes in the assessment bases of the fund based on quarterly Call Report submissions. From time to time, the FDIC may impose a supplemental special assessment in addition to other special assessments and regular premium rates to replenish the deposit insurance funds during periods of economic difficulty. The amount of an emergency special assessment imposed on a bank will be determined by the FDIC if such amount is necessary to provide sufficient assessment income to repay amounts borrowed from the Treasury; to provide sufficient assessment income to repay obligations issued to and other amounts borrowed from insured depository institutions; or for any other purpose the FDIC may deem necessary.

The FDIC may terminate insurance of deposits, after notice and a hearing, if it finds that the institution is in an unsafe or unsound condition to continue operations, has engaged in unsafe or unsound practices, or has violated any applicable law, regulation, rule, order or condition imposed by the FDIC. The management of the Bank does not know of any practice, condition or violation that might lead to termination of deposit insurance.

#### The Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”)

The Dodd-Frank Act, enacted in July 2010, significantly changed the bank regulatory landscape and has impacted lending, deposit, investment, trading and operating activities of financial institutions and their holding companies. The Dodd-Frank Act revised the statutory authorities governing the FDIC’s management of the DIF. The Dodd-Frank Act granted the FDIC new DIF management tools: maintaining a positive fund balance even during a banking crisis and maintaining moderate, steady assessment rates throughout economic and credit cycles.

Among other things, the Dodd-Frank Act: (1) raised the minimum Designated Reserve Ratio (DRR), which the FDIC must set each year, to 1.35% (from the former minimum of 1.15%) and removed the upper limit on the DRR (which was formerly capped at 1.5%) and therefore on the size of the DIF; (2) required that the DIF reserve ratio reach 1.35% by September 30, 2020 (rather than 1.15% by the end of 2016, as formerly required); (3) required that, in setting assessments, the FDIC offset the effect of requiring that the reserve ratio reach 1.35% by September 30, 2020 (rather than 1.15% by the end of 2016) on insured depository institutions with total consolidated assets of less than \$10 billion; (4) eliminated the requirement that the FDIC provide dividends from the Fund when the reserve ratio is between 1.35% and 1.50%; and (5) continued the FDIC’s authority to declare dividends when the reserve ratio at the end of a calendar year is at least 1.50%, but granted the FDIC sole discretion in determining whether to suspend or limit the declaration or payment of dividends.

The Dodd-Frank Act also required that the FDIC amend its regulations to redefine the assessment base used for calculating deposit insurance assessments. Under the Dodd-Frank Act, the assessment base must, with some possible exceptions, equal average consolidated total assets minus average tangible equity.

The FDIC amended 12 CFR 327 to implement revisions to the Federal Deposit Insurance Act made by the Dodd-Frank Act by modifying the definition of an institution’s deposit insurance assessment base; to change the assessment rate adjustments; to revise the deposit insurance assessment rate schedules in light of the new assessment base and altered adjustments; to implement the Dodd-Frank Act’s dividend provisions; to revise the large insured depository institution assessment system to better differentiate for risk and better take into account losses from large institution failures that the FDIC may incur; and to make technical and other changes to the FDIC’s assessment rules. The FDIC Board of Directors adopted the final rule, which redefined the deposit insurance assessment base as required by the Dodd-Frank Act; made changes to assessment rates; implemented the Dodd-Frank Act’s DIF dividend provisions; and revised the risk-based assessment system for all large insured depository institutions, generally, those institutions with at least \$10 billion in total assets. Nearly all institutions with assets less than \$10 billion, including the Bank, have benefited from a reduction in their assessments as a result of this final rule.

The Dodd-Frank Act requires publicly traded companies to give shareholders a non-binding vote of executive compensation at least every three (3) years. The legislation also authorizes the SEC to prohibit broker discretion on any voting on election of directors, executive compensation matters, and any other significant matter.

The Dodd-Frank Act also adopts various mortgage lending and predatory lending provisions and requires loan originators to retain 5% of any loan sold and securitized, unless it is a “qualified residential mortgage,” which includes standard 30 and 15-year fixed rate loans.

#### Consumer Protection and the Financial Protection Bureau

The Dodd-Frank Act created the Consumer Financial Protection Bureau (“CFPB”). As required by the Dodd-Frank Act, jurisdiction for all existing consumer protection laws and regulations has been transferred to the CFPB. In addition, the CFPB is granted authority to promulgate new consumer protection regulations for banks and nonbank financial firms offering consumer financial services or products to ensure that consumers are protected from “unfair, deceptive, or abusive” acts or practices.

Salisbury is subject to a number of federal and state laws designed to protect borrowers and promote lending to various sectors of the economy and population. These laws include the Equal Credit Opportunity Act, the Fair Credit Reporting Act, the Truth in Lending Act, the Home Mortgage Disclosure Act, the Real Estate Settlement Procedures Act, various state law counterparts, and the Consumer Financial Protection Act of 2010, which constitutes part of the Dodd-Frank Act and establishes the CFPB, as described above.

In 2013, the CFPB issued a final rule implementing the ability-to-repay and qualified mortgage (“QM”) provisions of the Truth in Lending Act, as amended by the Dodd-Frank Act (the “QM Rule”). The ability-to-repay provision requires creditors to make reasonable, good faith determinations that borrowers are able to repay their mortgages before extending the credit based on a number of factors and consideration of financial information about the borrower from reasonably reliable third-party documents. Under the Dodd-Frank Act and the QM Rule, loans meeting the definition of “qualified mortgage” are entitled to a presumption that the lender satisfied the ability-to-repay requirements. The presumption is a conclusive presumption/safe harbor for prime loans meeting the QM requirements and a rebuttable presumption for higher-priced/subprime loans meeting the QM requirements. The definition of a “qualified mortgage” incorporates the statutory requirements, such as not allowing negative amortization or terms longer than 30 years. The QM Rule also adds an explicit maximum 43% debt-to-income ratio for borrowers if the loan is to meet the QM definition.

#### Federal Reserve System

All depository institutions must hold a percentage of certain types of deposits as reserves. Reserve requirements currently are assessed on the depository institution's net transaction accounts (mostly checking accounts). Depository institutions must also regularly submit deposit reports of their deposits and other reservable liabilities.

For net transaction accounts in 2015, the first \$14.5 million (which may be adjusted by the FRB) was exempt from reserve requirements. A 3% reserve ratio was assessed on net transaction accounts over \$14.5 million up to and including \$103.6 million (which may be adjusted by the FRB). A 10% reserve ratio was assessed on net transaction accounts in excess of \$103.6 million (which may be adjusted by the FRB). The Bank is in compliance with these requirements.

#### Federal Home Loan Bank System

The Bank is a member of the Boston region of the Federal Home Loan Bank System, which consists of 11 regional Federal Home Loan Banks. The FHLBB provides a central credit facility primarily for member institutions. Member institutions are required to acquire and hold shares of capital stock in the FHLBB calculated periodically based primarily on its level of borrowings from the FHLBB. The Bank was in compliance with this requirement. At December 31, 2015, the Bank had FHLBB stock of \$3.2 million and FHLBB advances of \$27.0 million.

No market exists for shares of the FHLBB and, therefore, they are carried at par value. FHLBB stock may be redeemed at par value five years following termination of FHLBB membership, subject to limitations which may be imposed by the FHLBB or its regulator, the Federal Housing Finance Board, to maintain capital adequacy of the FHLBB. While the Bank currently has no intentions to terminate its FHLBB membership, the ability to redeem its investment in FHLBB stock would be subject to the conditions imposed by the FHLBB.

#### Small Business Lending Fund

Treasury’s SBLF program is a \$30 billion fund established under the Small Business Jobs Act of 2010 to encourage lending to small businesses by providing Tier 1 capital to qualified community banks with assets of less than \$10 billion.

Salisbury elected to participate in Treasury’s SBLF program and on August 25, 2011, Salisbury sold to the Secretary of the Treasury \$16 million of its Series B Preferred Stock under the SBLF program, and simultaneously repurchased all of its Series A Preferred Stock sold to the Treasury in 2009 under the Capital Purchase Program, a part of TARP. All of the proceeds from the sale of its Series B Preferred Stock were treated as Tier 1 Capital for regulatory purposes.



The Series B Preferred Stock paid noncumulative dividends. The dividend rate on the Series B Preferred Stock for the initial ten quarterly dividend periods, commencing with the period ended September 30, 2011 and ending with the period ended December 31, 2013, was determined each quarter based on the increase in the Bank's Qualified Small Business Lending over a baseline amount. The dividend rate for the quarterly period ended December 31, 2015 was 1.0%. For the eleventh quarterly dividend payment through four and one-half years after its issuance, the dividend rate on the Series B Preferred Stock would have been 1.0%. Salisbury redeemed all of its Series B Preferred Stock in December 2015 prior to the scheduled increase in the dividend rate on such securities. Commencing with the second quarter of 2016, four and one-half years from its issuance, the dividend rate would have been fixed at 9.0% per annum.

#### Other Regulations

##### *Sarbanes-Oxley Act of 2002*

The stated goals of SOX are to increase corporate responsibility, to provide for enhanced penalties for accounting and auditing improprieties at publicly traded companies and to protect investors by improving the accuracy and reliability of corporate disclosures pursuant to the securities laws.

SOX includes very specific disclosure requirements and corporate governance rules, requires the SEC and securities exchanges to adopt extensive additional disclosure, corporate governance and other related rules, and mandates further studies of certain issues by the SEC and the Comptroller General. SOX represents significant federal involvement in matters traditionally left to state regulatory systems, such as the regulation of the accounting profession, and to state corporate law, such as the relationship between a board of directors and management and between a board of directors and its committees.

SOX addresses, among other matters, audit committees; certification of financial statements and internal controls by the Chief Executive Officer and Chief Financial Officer; the forfeiture of bonuses or other incentive-based compensation and profits from the sale of an issuer's securities by directors and senior officers in the twelve-month period following initial publication of any financial statements that later require restatement; a prohibition on insider trading during pension plan black-out periods; disclosure of off-balance sheet transactions; a prohibition on certain loans to directors and officers; expedited filing requirements for Forms 4; disclosure of a code of ethics and filing a Form 8-K for significant changes or waivers of such code; "real time" filing of periodic reports; the formation of a public company accounting oversight board; auditor independence; and various increased criminal penalties for violations of securities laws. The SEC has enacted rules to implement various provisions of SOX.

#### *USA PATRIOT Act*

Under the USA PATRIOT Act, all financial institutions are required to take certain measures to identify their customers, prevent money laundering, monitor customer transactions and report suspicious activity to U.S. law enforcement agencies. Financial institutions also are required to respond to requests for information from federal banking regulatory authorities and law enforcement agencies. Information sharing among financial institutions for the above purposes is encouraged by an exemption granted to complying financial institutions from the privacy provisions of GLBA and other privacy laws. Financial institutions that hold correspondent accounts for foreign banks or provide private banking services to foreign individuals are required to take measures to avoid dealing with certain foreign individuals or entities, including foreign banks with profiles that raise money laundering concerns, and are prohibited from dealing with foreign "shell banks" and persons from jurisdictions of particular concern. The primary federal banking regulators and the Secretary of the Treasury have adopted regulations to implement several of these provisions. All financial institutions are also required to establish internal anti-money laundering programs. The effectiveness of a financial institution in combating money laundering activities is a factor to be considered in any application submitted by the financial institution under the Bank Merger Act or the BHCA. Salisbury has in place a Bank Secrecy Act and USA PATRIOT Act compliance program, and has implemented internal practices, procedures, and controls to comply with anti-money laundering requirements.

#### *Community Reinvestment Act and Fair Lending Laws*

Salisbury has a responsibility under the CRA to help meet the credit needs of our communities, including low and moderate-income neighborhoods. The CRA does not establish specific lending requirements or programs for financial institutions nor does it limit an institution's discretion to develop the types of products and services that it believes are best suited to its particular community, consistent with the CRA. In connection with its examination, the FDIC assesses the Bank's record of compliance with the CRA. In addition, the Equal Credit Opportunity Act and the Fair Housing Act prohibit discrimination in lending practices on the basis of characteristics specified in those statutes. The Bank's failure to comply with the provisions of the CRA could, at a minimum, result in regulatory restrictions on our activities. The Bank's failure to comply with the Equal Credit Opportunity Act and the Fair Housing Act could result in enforcement actions against the Bank by the FDIC as well as other federal regulatory agencies and the Department of Justice. The Bank's most recent FDIC CRA rating was "satisfactory."

#### The Electronic Funds Transfer Act, Regulation E and Related Laws

The Electronic Funds Transfer Act (the “EFTA”) provides a basic framework for establishing the rights, liabilities, and responsibilities of consumers who use electronic funds transfer (“EFT”) systems. The EFTA is implemented by the Federal Reserve's Regulation E, which governs transfers initiated through ATMs, point-of-sale terminals, payroll cards, automated clearing house (“ACH”) transactions, telephone bill-payment plans, or remote banking services. Regulation E requires consumers to opt in (affirmatively consent) to participation in a bank's overdraft service program for ATM and one-time debit card transactions before overdraft fees may be assessed on the consumer's account. Notice of the opt-in right must be provided to all new customers who are consumers, and the customer's affirmative consent must be obtained, before charges may be assessed on the consumer's account for paying such overdrafts.

Regulation E also provides bank customers with an ongoing right to revoke consent to participation in an overdraft service program for ATM and one-time debit card transactions and prohibits banks from conditioning the payment of overdrafts for checks, ACH transactions, or other types of transactions that overdraw the consumer's account on the consumer's opting into an overdraft service for ATM and one-time debit card transactions. For customers who do not affirmatively consent to overdraft service for ATM and one-time debit card transactions, a bank must provide those customers with the same account terms, conditions, and features that it provides to consumers who do affirmatively consent, except for the overdraft service for ATM and one-time debit card transactions. Salisbury does not provide an overdraft service with respect to one time point-of-sale or ATM transactions.

## Impact of Inflation and Changing Prices

The Consolidated Financial Statements and their Notes presented within this document have been prepared in accordance with GAAP, which require the measurement of financial position and operating results in terms of historical dollar amounts without considering changes in the relative purchasing power of money over time due to inflation. The impact of inflation is reflected in the increased cost of Salisbury's operations. Unlike the assets and liabilities of industrial companies, nearly all of the assets and liabilities of Salisbury are monetary in nature. As a result, interest rates have a greater impact on Salisbury's performance than do the effects of general levels of inflation. Interest rates do not necessarily move in the same direction or to the same extent as the prices of goods and services.

## Availability of Securities and Exchange Commission Filings

Salisbury makes available free of charge on its website ([www.salisburybank.com](http://www.salisburybank.com)) a link to its annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) of the Securities Exchange Act of 1934 as soon as practicable after such reports are electronically filed with or furnished to the SEC. Such reports filed with the SEC are also available on its website ([www.sec.gov](http://www.sec.gov)). The public may also read and copy any materials filed with the SEC at the SEC's Public Reference Room, 100 F Street, NE, Washington, DC 20549. Information about accessing company filings can be obtained by calling 1-800-SEC-0330. Information on Salisbury's website is not incorporated by reference into this report. Investors are encouraged to access these reports and the other information about Salisbury's business and operations on its website. Copies of these filings may also be obtained from Salisbury free of charge upon request.

## Guide 3 Statistical Disclosure by Bank Holding Companies

The following information required by Securities Act Guide 3 "Statistical Disclosure by Bank Holding Companies" is located on the pages noted below.

	Page
I. Distribution of Assets, Liabilities and Shareholders' Equity; Interest Rates and Interest Differential	25-26
II. Investment Portfolio	32, 61-63
III. Loan Portfolio	33-40, 63-75
IV. Summary of Loan Loss Experience	27-29, 71-75
V. Deposits	40, 77
VI. Return on Equity and Assets	22
VII. Short-Term Borrowings	40, 77

## Item 1A. RISK FACTORS

Salisbury is the registered bank holding company for the Bank, its wholly-owned subsidiary. Salisbury's business and activity is currently limited to the holding of the Bank's outstanding capital stock, and the Bank is Salisbury's primary investment.

An investment in Salisbury common stock entails certain risks, some of which are inherent in the financial services industry and others of which are more specific to the Bank's business. Salisbury considers the most significant factors of which we are aware affecting risk in Salisbury common stock as those that are set forth below. These are not the only risks of an investment in Salisbury common stock, and none of the factors set forth below relates to the personal circumstances of individual investors. Investors should read this entire Form 10-K, as well as other documents and exhibits that are incorporated by reference in the 10-K and that have been filed with the SEC, in order to better understand these risks and to evaluate investment in Salisbury common stock.

Changes in interest rates and spreads could have a negative impact on earnings and financial condition.

Salisbury's earnings and financial condition are dependent to a large degree upon net interest income, which is the difference between interest earned from loans and investments and interest paid on deposits and borrowings. The narrowing of interest rate spreads, meaning the difference between interest rates earned on loans and investments, and the interest rates paid on deposits and borrowings, could adversely affect Salisbury's earnings and financial condition. Salisbury cannot predict with certainty or control changes in interest rates. Global, national, regional, and local economic conditions and the policies of regulatory authorities, including monetary policies of the FRB, affect interest income and interest expense. Salisbury has ongoing policies and procedures designed to manage the risks associated with changes in market interest rates.

However, changes in interest rates still may have an adverse effect on Salisbury's profitability. For example, high interest rates could also affect the volume of loans that Salisbury originates, because higher rates could cause customers to apply for fewer mortgages, or cause depositors to shift funds from accounts that have a comparatively lower rate, to accounts with a higher rate, or experience customer attrition due to competitor pricing or disintermediation. If the cost of interest-bearing deposits increases at a rate greater than the yields on interest-earning assets increase, net interest income will be negatively affected. Changes in the asset and liability mix may also affect net interest income. Similarly, lower interest rates cause higher yielding assets to prepay and floating or adjustable rate assets to reset to lower rates. If Salisbury is not able to reduce its funding costs sufficiently, due to either competitive factors or the maturity schedule of existing liabilities, then Salisbury's net interest margin will decline.

Weakness in the markets for residential or commercial real estate, including the secondary residential mortgage loan markets, could reduce Salisbury's net income and profitability.

Declines in home prices, increases in delinquency and default rates, and constrained secondary credit markets affect the mortgage industry generally. Salisbury's financial results may be adversely affected by changes in real estate values. Decreases in real estate values could adversely affect the value of property used as collateral for loans and investments. If poor economic conditions result in decreased demand for real estate loans, Salisbury's net income and profits may decrease.

Weakness in the secondary market for residential lending could have an adverse impact upon Salisbury's profitability. The effects of ongoing mortgage market challenges, combined with the ongoing correction in residential real estate market prices and reduced levels of home sales, could result in further price reductions in single family home values, adversely affecting the value of collateral securing mortgage loans held, mortgage loan originations and gains on sale of mortgage loans. Declines in real estate values and home sales volumes, and financial stress on borrowers as a result of job losses, or other factors, could have further adverse effects on borrowers that result in higher delinquencies and greater charge-offs in future periods beyond that which is provided for in Salisbury's allowance for loan losses, which would adversely affect Salisbury's financial condition or results of operations.

Fluctuations in economic conditions and collateral values could impact the adequacy of Salisbury's allowance for loan losses.

Salisbury's business is subject to periodic fluctuations based on national and local economic conditions. These fluctuations are not predictable, cannot be controlled and may have a material adverse impact on Salisbury's operations and financial condition. For example, declines in housing activity including declines in building permits, housing sales and home prices may make it more difficult for Salisbury's borrowers to sell their homes or refinance their debt. Slow sales could strain the resources of real estate developers and builders. The ongoing economic uncertainty has affected employment levels and could impact the ability of Salisbury's borrowers to service their debt. Bank regulatory agencies also periodically review Salisbury's allowance for loan losses and may require an increase in the provision for credit losses or the recognition of further loan charge-offs, based on judgments different than those of management. In addition, if charge-offs in future periods exceed the allowance for loan losses Salisbury will need additional provisions to increase the allowance for loan losses. Any increases in the allowance for loan losses will result in a decrease in net income and, possibly, capital, and may have a material adverse effect on Salisbury's financial condition and results of operations. Salisbury may suffer higher loan losses as a result of these factors and the resulting impact on its borrowers.

Credit market conditions may impact Salisbury's investments.

Significant credit market anomalies may impact the valuation and liquidity of Salisbury's investment securities. Illiquidity could reduce the market value of Salisbury's investments, even those with no apparent credit exposure. The valuation of Salisbury's investments requires judgment and as market conditions change investment values may also

change.

Salisbury's securities portfolio performance in difficult market conditions could have adverse effects on Salisbury's results of operations.

Under GAAP, Salisbury is required to review Salisbury's investment portfolio periodically for the presence of other-than-temporary impairment of its securities, taking into consideration current market conditions, the extent and nature of changes in fair value, issuer rating changes and trends, volatility of earnings, current analysts' evaluations, Salisbury's ability and intent to hold investments until a recovery of amortized cost, as well as other factors. Adverse developments with respect to one or more of the foregoing factors may require Salisbury to deem particular securities to be other-than-temporarily impaired, with the credit related portion of the reduction in the value recognized as a charge to Salisbury's earnings. Market volatility may make it extremely difficult to value certain securities of Salisbury. Subsequent valuations, in light of factors prevailing at that time, may result in significant changes in the values of these securities in future periods. Any of these factors could require Salisbury to recognize further impairments in the value of Salisbury's securities portfolio, which may have an adverse effect on Salisbury's results of operations in future periods.

16

If the goodwill that Salisbury has recorded in connection with its acquisitions becomes impaired, it could have a negative impact on Salisbury's profitability.

Applicable accounting standards require that the purchase method of accounting be used for all business combinations. Under purchase accounting, if the purchase price of an acquired company exceeds the fair value of the acquired company's net assets, the excess is carried on the acquirer's balance sheet as goodwill. At December 31, 2015, Salisbury had \$12.6 million of goodwill on its balance sheet. Salisbury must evaluate goodwill for impairment at least annually. Write-downs of the amount of any impairment, if necessary, are to be charged to the results of operations in the period in which the impairment occurs. There can be no assurance that future evaluations of goodwill will not result in findings of impairment and related write-downs, which may have a material adverse effect on Salisbury's financial condition and results of operations.

Salisbury's ability to pay dividends substantially depends upon its receipt of dividends from the Bank.

Cash dividends from the Bank and Salisbury's liquid assets are the principal sources of funds for paying cash dividends on Salisbury's common stock and preferred stock. Unless Salisbury receives dividends from the Bank or chooses to use its liquid assets, it may not be able to pay dividends. Salisbury must pay dividends on its preferred stock before it may pay dividends on its common stock. The Bank's ability to pay dividends to Salisbury is subject to its condition and profitability as well as its regulatory requirements.

Strong competition within Salisbury's market areas may limit growth and profitability.

Competition in the banking and financial services industry is intense. Salisbury competes with commercial banks, savings institutions, mortgage brokerage firms, credit unions, finance companies, mutual funds, insurance companies, and brokerage and investment banking firms operating locally and elsewhere. As Salisbury grows, it may expand into contiguous market areas where it may not be as well-known as other institutions that have been operating in those areas for some time. In addition, larger banking institutions may become increasingly active in Salisbury's market areas, may have substantially greater resources and lending limits and may offer certain services that Salisbury does not, or cannot efficiently, provide. Salisbury's profitability depends upon its continued ability to successfully compete in its market areas. The greater resources and deposit and loan products offered by some competitors may limit its ability to grow profitably.

**Salisbury and the Bank are subject to extensive federal and state regulation and supervision.**

Salisbury and the Bank are subject to extensive federal and state regulation and supervision. Banking regulations are primarily intended to protect depositors' funds, federal deposit insurance funds and the banking system as a whole, not shareholders. These regulations affect Salisbury's lending practices, capital structure, investment practices, and dividend policy and growth, among other things. State and federal legislatures and regulatory agencies continually review banking laws, regulations and policies for possible changes. Changes to statutes, regulations or regulatory policies, including changes in interpretation or implementation of statutes, regulations or policies, could affect Salisbury in substantial and unpredictable ways. Such changes could subject Salisbury to additional costs, limit the types of financial services and products it may offer and/or increase the ability of non-banks to offer competing financial services and products, among other things. Failure to comply with laws, regulations or policies could result in sanctions by regulatory agencies, civil money penalties and/or reputation damage, which could have a material adverse effect on Salisbury's business, financial condition and results of operations. While Salisbury has policies and procedures designed to prevent any such violations, there can be no assurance that such violations will not occur. See the section captioned "Regulation and Supervision" in Item 1 of this report for further information.

Salisbury's stock price may be volatile.



Salisbury's stock is inactively traded and its stock price may fluctuate widely in response to a variety of factors including:

- Actual or anticipated variations in quarterly operating results
- Recommendations by securities analysts
- New technology used, or services offered, by competitors
- Significant acquisitions or business combinations, strategic partnerships, joint ventures or capital commitments by or involving Salisbury or Salisbury's competitors
  - Failure to integrate acquisitions or realize anticipated benefits from acquisitions
- Operating and stock price performance of other companies that investors deem comparable to Salisbury
  - News reports relating to trends, concerns and other issues in the financial services industry
    - Changes in government regulations
  - Geopolitical conditions such as acts or threats of terrorism or military conflicts
  - Changes in the economic environment of the market areas the Bank serves

General market fluctuations, industry factors and general economic and political conditions and events, such as economic slowdowns or recessions, interest rate changes, credit loss trends or currency fluctuations could also cause Salisbury's stock price to decrease regardless of Salisbury's operating results.

Salisbury's ability to attract and retain skilled personnel may impact its success.

Salisbury's success depends, in large part, on its ability to attract and retain key people. Competition for people with specialized knowledge and skills can be intense, and Salisbury may not be able to hire people or to retain them. The unexpected loss of services of one or more of Salisbury's key personnel could have a material adverse impact on the business because of their skills, knowledge of the market, years of industry experience and the difficulty of promptly finding qualified replacement personnel.

Salisbury continually encounters technological change.

The financial services industry is continually undergoing rapid technological change with frequent introductions of new technology-driven products and services. The effective use of technology can increase efficiency and enable financial institutions to better serve customers and to reduce costs. However, some new technologies needed to compete effectively result in incremental operating costs. Salisbury's future success depends, in part, upon its ability to address the needs of its customers by using technology to provide products and services that will satisfy customer demands, as well as to create additional efficiencies in operations. Many of Salisbury's competitors have substantially greater resources to invest in technological improvements. Salisbury may not be able to effectively implement new technology-driven products and services or be successful in marketing these products and services to its customers. Failure to successfully keep pace with technological change affecting the financial services industry could have a material adverse impact on Salisbury's business and, in turn, its financial condition and results of operations.

A failure involving controls and procedures may have an adverse effect on Salisbury.

Management regularly reviews and updates Salisbury's internal controls, disclosure controls and procedures, and corporate governance policies and procedures. Any system of controls, however well designed and operated, is based in part on certain assumptions and can provide only reasonable, not absolute, assurances that the objectives of the system are met. Any failure or circumvention of the controls and procedures or failure to comply with regulations related to controls and procedures could have a material adverse effect on Salisbury's business, results of operations and financial condition.

If customer information was to be misappropriated and used fraudulently, due to a breach of our systems, or those of third party vendors or service providers, including as a result of cyberattacks, Salisbury could be exposed to potential liability and reputation risk as well as increased costs.

Risk of theft of customer information resulting from security breaches by third parties exposes banks to reputation risk and potential monetary loss. Like other financial institutions, Salisbury has exposure to fraudulent misuse of its customers' personal information resulting from its general business operations through loss or theft of the information and through misappropriation of information by third parties in connection with customer use of financial instruments, such as debit cards.

In addition, Salisbury relies upon a variety of computing platforms and networks over the internet for the purposes of data processing, communications and information exchange. Despite the safeguards instituted by Salisbury, any system is susceptible to a breach of security. In addition, Salisbury relies on the services of a variety of third party vendors to meet Salisbury's data processing and communication needs. The occurrence of any failures, interruptions or security breaches of Salisbury's information systems or that of its vendors could damage Salisbury's reputation, result in a loss of customer business or expose Salisbury to civil litigation and possible financial loss. Such costs and/or losses could materially impact Salisbury's earnings.

Changes in accounting standards can materially impact Salisbury's financial statements.

Salisbury's accounting policies and methods are fundamental to how Salisbury records and reports its financial condition and results of operations. From time to time, the Financial Accounting Standards Board or regulatory authorities change the financial accounting and reporting standards that govern the preparation of Salisbury's financial statements. These changes can be hard to predict and can materially impact how it records and reports its financial condition and results of operations. In some cases, it could be required to apply a new or revised standard retroactively, resulting in Salisbury restating prior period financial statements.

Changes and interpretations of tax laws and regulations may adversely impact Salisbury's financial statements.

Local, state or federal tax authorities may interpret tax laws and regulations differently than Salisbury and challenge tax positions that Salisbury has taken on its tax returns. This may result in the disallowance of deductions or differences in the timing of deductions and result in the payment of additional taxes, interest or penalties that could materially affect Salisbury's performance.

Unprecedented disruption and significantly increased risk in the financial markets may impact Salisbury.

The banking industry experienced unprecedented turmoil in the past as some of the world's major financial institutions collapsed, were seized or were forced into mergers as the credit markets tightened and the economy headed into a recession. Continuing measures taken by the Government in an effort to stabilize the economy may have unintended consequences, and there can be no assurance that Salisbury will not be impacted by current market uncertainty in a way it cannot currently predict or mitigate.

The risks presented by recent or future acquisitions could adversely affect our financial condition and results of operations.

Our business strategy has included, and may continue to include, growth through acquisition from time to time. Any recent and future acquisitions will be accompanied by the risks commonly encountered in acquisitions. These risks may include, among other things: our ability to realize anticipated cost savings; the difficulty of integrating operations and personnel; the loss of key employees; the potential disruption of our or the acquired company's ongoing business in such a way that could result in decreased revenues; the inability of our management to maximize our financial and strategic position; the inability to maintain uniform standards, controls, procedures and policies; and the impairment of relationships with the acquired company's employees and customers as a result of changes in ownership and management.

#### Item 1B. UNRESOLVED SEC STAFF COMMENTS

None.

#### Item 2. PROPERTIES

Salisbury does not directly own or lease any properties. The properties described below are owned or leased by the Bank.

The Bank conducts its business at its main office, located at 5 Bissell Street, Lakeville, Connecticut, and through thirteen full service branch offices located in Canaan, Salisbury and Sharon, Connecticut; Great Barrington, South Egremont and Sheffield, Massachusetts; and Dover Plains, Fishkill, Millerton, Newburgh, Poughkeepsie, and Red Oaks Mill, New York. The Bank's trust and wealth advisory services division is located in a separate building adjacent to the main office of the Bank in Lakeville, Connecticut. The Bank owns its main office and six of its branch offices and currently leases six branch offices.

The Company acquired one branch in Sharon, Connecticut from Union Savings Bank on June 6, 2014, and the acquisition of Riverside Bank on December 5, 2014 added four additional full-service branch offices.

For additional information, see Note 7, "Bank Premises and Equipment," and Note 18, "Commitments and Contingent Liabilities" to the Consolidated Financial Statements.

The following table includes all property owned or leased by the Bank, but does not include Other Real Estate Owned.

Offices	Location	Owned/Leased	Lease expiration
Main Office	5 Bissell Street, Lakeville, CT	Owned	—
Trust and Wealth Advisory Services Division	19 Bissell Street, Lakeville, CT	Owned	—
Salisbury Office	18 Main Street, Salisbury, CT	Owned	—
Sharon Office	5 Gay Street, Sharon, CT	Owned	—
Canaan Operations	94 Main Street, Canaan, CT	Owned	—
Canaan Office	100 Main Street, Canaan, CT	Owned	—
South Egremont Office	51 Main Street, South Egremont, MA	Leased	9/10/16
Sheffield Office	640 North Main, Street, Sheffield, MA	Owned	—
Gt. Barrington Office	210 Main Street, Gt. Barrington, MA	Leased	4/30/29
Millerton Office	87 Main Street, Millerton, NY	Owned	—
Poughkeepsie Office	11 Garden Street, Poughkeepsie, NY	Owned	—

Edgar Filing: SALISBURY BANCORP INC - Form 10-K

Fishkill Office	1004 Main Street, Fishkill, NY	Leased	12/31/20
Red Oaks Mill Office	2064 New Hackensack Road, Poughkeepsie, NY	Leased	7/31/23
Newburgh Office	52 Route 17K, Newburgh, NY	Leased	3/31/18
Dover Plains Office	5 Dover Village Plaza, Dover Plains, NY	Leased	8/01/17

LEGAL PROCEEDINGS

Item 3.

The Bank is involved in various claims and legal proceedings, which are not material, arising in the ordinary course of business.

As previously disclosed, the Bank, individually and in its capacity as a former Co-Trustee of the Erling C. Christophersen Revocable Trust (the "Trust"), was named as a defendant in litigation filed in the Connecticut Complex Litigation Docket in Stamford, captioned John Christophersen v. Erling Christophersen, et al., X08-CV-08-5009597S (the "First Action"). The Bank also was a counterclaim-defendant in related mortgage foreclosure litigation in the Connecticut Complex Litigation Docket in Stamford, captioned Salisbury Bank and Trust Company v. Erling C. Christophersen, et al., X08-CV-10-6005847-S (the "Foreclosure Action," together with the First Action, the "Actions"). The other parties to the Actions were John R. Christophersen; Erling C. Christophersen, individually and as Co-Trustee of the Trust; Bonnie Christophersen and Elena Dreiske, individually and as Co-Trustees of the Mildred B. Blount Testamentary Trust; People's United Bank; Law Offices of Gary Oberst, P.C.; Rhoda Rudnick; and Hinckley Allen & Snyder LLP.

The Actions involved a dispute over title to certain real property located in Westport, Connecticut that was conveyed by Erling Christophersen, as grantor, to the Trust on or about August 8, 2007. Subsequent to this conveyance, the Bank loaned \$3,387,000 to the Trust, which was secured by a commercial mortgage in favor of the Bank on the Westport property. This mortgage is the subject of the Foreclosure Action brought by the Bank.

As previously disclosed, John R. Christophersen claimed an interest in the Westport real property transferred to the Trust and sought to quiet title to the property and to recover money damages from the defendants for the alleged wrongful divestiture of his claimed interest in the property.

On June 25, 2012, the Bank and John R. Christophersen entered into a Settlement Agreement, which resolved all differences between John R. Christophersen and the Bank and resulted in the withdrawal (with prejudice) of the claims made by John R. Christophersen. All claims against the Bank have been withdrawn and the Bank is no longer a defendant or counterclaim defendant in any litigation involving the Actions. As an additional consequence of the Settlement Agreement, Bonnie Christophersen, Elena Dreiske and People's United Bank are no longer parties to any of the litigation referenced above.

On July 27, 2012, Erling Christophersen filed a Motion to Restore the First Action, and on October 15, 2012 filed a Motion to Stay the Foreclosure Action pending resolution of the Motion to Restore. The Bank opposed both motions. On February 1, 2013, the Court issued orders denying both motions. On February 14, 2013, Erling Christophersen appealed the orders denying his Motion to Restore the First Action, and Motion to Stay the Foreclosure Action.

The Appellate Court dismissed the appeal of the Foreclosure Action in May 2013, and later denied Erling Christophersen's motion for reconsideration of its decision.

The Bank proceeded in its Foreclosure Action against Erling Christophersen. Erling Christophersen asserted two special defenses and set-off claims alleging (1) that the Bank failed to defend the title claims against the properties, and (2) that the Bank took certain trustee fees without approval. The Bank moved to strike the special defenses and set off claims. In a decision issued on November 6, 2013, the Court granted the motion to strike as to the second special defense and set off, but denied the motion as to the first special defense and set off. Trial began on February 4, 2014, and concluded on February 14, 2014.

In a decision issued on June 2, 2014, the Court dismissed Erling Christophersen's special defense, and made findings as to the amount of the debt owed by Erling Christophersen and the value of the property, reserving judgment on whether to order a strict foreclosure or foreclosure by sale pending a hearing on the amount of attorneys' fees accrued, and the debt accrued since the commencement of the trial. That hearing was held on July 29, 2014. On July 25, 2014, Erling Christophersen moved to disqualify the Bank's counsel, seeking, in part, the remedy of a new trial. The Court denied that motion in a decision dated July 30, 2014. On August 5, 2014, the Court issued a Judgment of Strict Foreclosure (the "Judgment") in favor of the Bank and set September 16, 2014 as the Law Day, which is the final date fixed by the Court on which the debtor can pay off the debt or redeem the real property, with subsequent dates for subsequent encumbrances in inverse order of priority.

On September 15, 2014, Christophersen moved to open the Judgment, which motion was denied by order of the Court dated September 30, 2014. On October 3, 2014, Christophersen filed an Appeal of the Judgment and of the denial of his motion to reopen. Salisbury Bank moved to dismiss the Appeal on October 24, 2014, on grounds that Christophersen cannot represent the Trust as he is not an attorney, and that Christophersen in his individual capacity does not have any interest in the Appeal. On December 17, 2014, such motion was granted in part and dismissed in part, but the decision was moot because counsel submitted an appearance on behalf of the Trust on December 29, 2014. On January 20, 2015, Christophersen filed a motion for reconsideration, which motion was denied by order of the Appellate Court on February 10, 2015.

The parties submitted briefs and oral arguments were heard on January 7, 2016. On March 1, 2016, the Appellate Court affirmed the trial court's judgment and remanded the case for the setting of new Law Days. Subsequently, the defendant filed an application for review with the Connecticut Supreme Court, which denied Mr. Christophersen's Petition For Certification on March 23, 2016. The case will be remanded to the trial court to set new law days.

There are no other material pending legal proceedings, other than ordinary routine litigation incidental to the registrant's business, to which Salisbury is a party or to which any of its property is subject.

Item 4. MINE SAFETY DISCLOSURES

Not applicable.

PART II

Item MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED SHAREHOLDER MATTERS AND  
5. ISSUER PURCHASED OF EQUITY SECURITIES

Market Information

For the information required by this item see Note 24 – “Selected Quarterly Consolidated Financial Data (Unaudited)” of Notes to Consolidated Financial Statements.

Holdings

There were approximately 2,141 holders of record of the common stock of Salisbury as of March 1, 2016. This number includes brokerage firms and other financial institutions that hold stock in their name, but which is actually beneficially owned by third parties.

Equity Compensation Plan Information

For the information required by this item see Note 15 – “Long Term Incentive Plan” of Notes to Consolidated Financial Statements.

Recent Sales of Unregistered Securities

None.

Dividends

For a discussion of Salisbury's dividend policy and restrictions on dividends see "Management's Discussion and Analysis of Financial Condition and Results of Operations" under the caption "Dividends."

21



## Item 6. SELECTED FINANCIAL DATA

The following table contains certain information concerning the financial position and results of operations of Salisbury at the dates and for the periods indicated. This information should be read in conjunction with the Consolidated Financial Statements and related notes.

## SELECTED CONSOLIDATED FINANCIAL DATA

(in thousands, except ratios and per share amounts)

At or for the years ended December 31, Statement of Income	2015	2014	2013	2012	2011
Interest and dividend income	\$34,571	\$22,855	\$21,750	\$22,658	\$24,044
Interest expense	3,026	2,704	3,062	4,282	5,559
Net interest and dividend income	31,545	20,151	18,688	18,376	18,485
Provision for loan losses	917	1,134	1,066	1,070	1,440
Gains on securities, net	192	—	—	279	11
Trust and wealth advisory	3,265	3,295	3,074	2,945	2,548
Service charges and fees	3,070	2,473	2,298	2,189	2,090
Gains on sales of mortgage loans, net	274	64	579	1,596	687
Mortgage servicing, net	1	94	35	(21)	65
Other	510	326	319	326	255
Non-interest income	7,312	6,252	6,305	7,314	5,656
Non-interest expense	25,920	22,138	18,935	19,554	17,639
Income before income taxes	12,020	3,131	4,992	5,066	5,062
Income tax provision	3,563	610	909	989	950
Net income	8,457	2,521	4,083	4,077	4,112
Net income available to common shareholders	8,299	2,355	3,922	3,861	3,588
<b>Financial Condition</b>					
Total assets	\$891,192	\$855,427	\$587,109	\$600,813	\$609,284
Loans receivable, net	699,018	673,330	438,178	388,758	370,766
Allowance for loan losses	5,716	5,358	4,683	4,360	4,076
Securities	79,870	94,827	99,831	132,034	161,876
Deposits	754,533	715,426	477,369	491,215	471,306
Federal Home Loan Bank of Boston advances	26,979	28,813	30,411	31,980	54,615
Repurchase agreements	3,914	4,163	2,554	1,784	12,148
Subordinated debt, net of issuance cost	9,764	—	—	—	—
Total shareholders' equity	90,574	101,821	72,790	71,997	66,862
Non-performing assets	16,265	10,892	7,549	10,104	10,820
<b>Per Common Share Data</b>					
Earnings, basic	\$3.04	\$1.32	\$2.30	\$2.28	\$2.12
Earnings, diluted	3.02	1.32	2.30	2.28	2.12
Cash dividends paid	1.12	1.12	1.12	1.12	1.12
Tangible book value	27.69	25.83	27.12	26.85	23.69
<b>Statistical Data</b>					
Net interest margin (taxable equivalent)	3.99	% 3.64	% 3.57	% 3.45	% 3.51
Efficiency ratio (taxable equivalent)	63.03	78.41	70.70	69.38	68.16
Effective tax rate	29.64	19.49	18.21	19.49	18.80
Return on average assets	0.94	0.37	0.66	0.64	0.61
Return on average common shareholders' equity	9.36	3.88	7.01	7.22	7.26
Dividend payout ratio	36.82	81.43	48.83	49.02	52.70

Edgar Filing: SALISBURY BANCORP INC - Form 10-K

Allowance for loan losses to loans receivable, gross	0.81	0.79	1.06	1.11	1.09
Non-performing assets to total assets	1.82	1.45	1.29	1.68	1.78
Tier 1 leverage capital	8.56	12.31	10.65	9.87	9.45
Total risk-based capital	13.51	14.27	16.46	16.63	15.97
Weighted average common shares outstanding, basic	2,706	1,764	1,691	1,690	1,689
Weighted average common shares outstanding, diluted	2,723	1,765	1,691	1,690	1,689

Item 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS  
BUSINESS

Salisbury, a Connecticut corporation, formed in 1998, is the bank holding company for the Bank, a Connecticut-chartered and FDIC insured commercial bank headquartered in Lakeville, Connecticut. Salisbury's principal business consists of the business of the Bank. The Bank, formed in 1848, is engaged in customary banking activities, including general deposit taking and lending activities to both retail and commercial markets, and trust and wealth advisory services. The Bank conducts its banking business from thirteen full-service offices in the towns of: Canaan, Lakeville, Salisbury and Sharon, Connecticut; Great Barrington, South Egremont and Sheffield, Massachusetts; and, Fishkill, Newburgh, Poughkeepsie, Red Oaks Mill, Dover Plains and Millerton, New York, and its trust and wealth advisory services from offices in Lakeville, Connecticut. In May 2014, the Bank established a new branch in Great Barrington, Massachusetts. In June 2014, the Bank acquired a branch office and related deposits from another institution in Sharon, Connecticut and consolidated its existing Sharon office with the new branch.

Additionally, on December 5, 2014, Salisbury completed its acquisition of Riverside Bank of Poughkeepsie, New York, adding four new offices and a strong commercial loan focus to Salisbury's New York market presence.

Critical Accounting Policies and Estimates

Salisbury's consolidated financial statements follow GAAP as applied to the banking industry in which it operates. Application of these principles requires management to make estimates, assumptions and judgments that affect the amounts reported in the financial statements. These estimates, assumptions and judgments are based on information available as of the date of the financial statements; accordingly, as this information changes, the financial statements could reflect different estimates, assumptions and judgments and as such have a greater possibility of producing results that could be materially different than originally reported. Estimates, assumptions and judgments are necessary when assets and liabilities are required to be recorded at fair value, when a decline in the value of an asset not carried at fair value warrants an impairment write-down or valuation reserve to be established, or when an asset or liability needs to be recorded contingent upon a future event.

Salisbury's significant accounting policies are presented in Note 1 of Notes to Consolidated Financial Statements, which, along with this Management's Discussion and Analysis, provide information on how significant assets are valued in the financial statements and how those values are determined. Management believes that the following accounting estimates are the most critical to aid in fully understanding and evaluating Salisbury's reported financial results, and they require management's most difficult, subjective or complex judgments, resulting from the need to make estimates about the effect of matters that are inherently uncertain.

Loans acquired in business combinations are initially recorded at fair value with no carryover of the related allowance for credit losses. Determining the fair value of the loans involves estimating the amount and timing of cash flows initially expected to be collected and discounting those cash flows at an appropriate market rate of interest. The Bank continues to evaluate reasonableness of the timing and the amount of cash to be collected. Subsequent decreases in expected cash flows may result in changes in the amortization or accretion of fair market value adjustments, and in some cases may result in the loan being considered impaired. For collateral dependent loans with deteriorated credit quality, the Bank estimates the fair value of the underlying collateral of the loans. These values are discounted using market derived rates of return, with consideration given to the period of time and costs associated with the foreclosure and disposition of the collateral.

The allowance for loan losses represents management's estimate of credit losses inherent in the loan portfolio. Determining the amount of the allowance for loan losses is considered a critical accounting estimate because it requires significant judgment and the use of estimates related to the amount and timing of expected future cash flows

on impaired loans, estimated losses on pools of homogeneous loans based on historical loss experience, and consideration of current economic trends and conditions, all of which may be susceptible to significant change. The loan portfolio also represents the largest asset type on the balance sheet. Note 1 describes the methodology used to determine the allowance for loan losses. A discussion of the factors driving changes in the amount of the allowance for loan losses are included in the “Provision and Allowance for Loan Losses” section of Management’s Discussion and Analysis.

Management evaluates goodwill and identifiable intangible assets for impairment annually using valuation techniques that involve estimates for discount rates, projected future cash flows and time period calculations, all of which are susceptible to change based on changes in economic conditions and other factors. Future events or changes in the estimates, which are used to determine the carrying value of goodwill and identifiable intangible assets or which otherwise adversely affect their value or estimated lives could have a material adverse impact on the results of operations.

Management evaluates securities for other-than-temporary impairment giving consideration to the extent to which the fair value has been less than cost, estimates of future cash flows, delinquencies and default severity, and the intent and ability of Salisbury to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value. The consideration of the above factors is subjective and involves estimates and assumptions about matters that are inherently uncertain. Should actual factors and conditions differ materially from those used by management, the actual realization of gains or losses on investment securities could differ materially from the amounts recorded in the financial statements.

## OVERVIEW AND HIGHLIGHTS

Selected 2015 highlights are as follows:

Net income available to common shareholders was \$8.3 million, or \$3.04 per common share, for December 31, 2015, compared with \$2.4 million, or \$1.32 per common share, for December 31, 2014

Redemption of \$16 million of Senior Non-Cumulative Perpetual Preferred Stock and a \$10 million private placement of subordinated debt

- Total assets increased \$36 million, or 4.2%, as compared with December 2014

- Total deposits increased \$39 million, or 5.5% as compared with December 2014

- Book value per share of \$33.13 increased \$1.59, or 5% as compared with December 2014

- Tangible book value per share of \$ 27.69 increased \$1.85, or 7% as compared with December 2014

- Earnings per share increased from 2014 by \$1.72, or 130%, to \$3.04

The following discussion and analysis of Salisbury's consolidated results of operations should be read in conjunction with the Consolidated Financial Statements and footnotes.

## RESULTS OF OPERATIONS

Comparison of the Years Ended December 31, 2015 and 2014

## Net Interest and Dividend Income

Net interest and dividend income (presented on a tax-equivalent basis) increased \$11,304,000 in 2015 over 2014. The net interest margin increased 35 basis points to 3.99% from 3.64%, due to a 26 basis point increase in the average yield on interest-earning assets and a 9 basis point decline in the average cost of interest-bearing liabilities. The net interest margin is affected by changes in the mix of interest-earning assets and funding liabilities, asset and liability growth, and the effects of changes in market interest rates on the pricing and re-pricing of assets and liabilities. The following table sets forth the components of Salisbury's net interest income and yields on average interest-earning assets and interest-bearing funds. Income and yields on tax-exempt securities are presented on a fully taxable equivalent basis.

Years ended December 31, (dollars in thousands)	Average Balance			Income / Expense			Average Yield / Rate		
	2015	2014	2013	2015	2014	2013	2015	2014	2013
Loans (a)(d)(f)	\$687,755	\$473,706	\$419,193	\$32,208	\$20,041	\$18,250	4.68 %	4.23 %	4.35 %
Securities (c)(d)	78,420	86,956	106,603	3,359	3,980	4,650	4.28	4.58	4.36
FHLBB stock	3,430	4,343	5,417	89	71	21	2.59	1.63	0.39
Short term funds (b)	50,870	24,407	26,281	120	58	67	0.24	0.24	0.25
Total earning assets	820,475	589,412	557,494	35,776	24,150	22,988	4.36	4.10	4.12
Other assets	60,319	41,737	37,966						
Total assets	\$880,794	\$631,149	\$595,460						
Interest-bearing demand deposits	\$121,431	\$84,212	\$75,185	311	266	278	0.26	0.32	0.37
Money market accounts	177,956	130,618	128,951	472	299	330	0.27	0.23	0.26
Savings and other	125,181	116,524	106,224	220	204	206	0.18	0.18	0.19
Certificates of deposit	134,577	87,516	88,352	841	696	999	0.62	0.80	1.13
Total interest-bearing deposits	559,145	418,870	398,712	1,844	1,465	1,813	0.33	0.35	0.45
Repurchase agreements	4,111	4,598	3,035	7	8	6	0.17	0.18	0.19
Capital lease	423	424	—	70	47	—	16.57	11.08	0.00
Note payable	138	—	—	6	—	—	4.62	0.00	0.00
Subordinated Debt (net of issuance costs)	594	—	—	35	—	—	5.84	0.00	0.00
FHLBB advances	27,827	30,214	31,176	1,064	1,184	1,243	3.82	3.92	3.99
Total interest-bearing liabilities	592,238	454,106	432,923	3,026	2,704	3,062	0.51	0.60	0.71
Demand deposits	178,943	96,199	84,416						
Other liabilities	5,043	4,058	6,162						
Shareholders' equity	104,570	76,786	71,959						
Total liabilities & shareholders' equity	\$880,794	\$631,149	\$595,460						
Net interest income (f)				\$32,750	\$21,446	\$19,926			
Spread on interest-bearing funds							3.85	3.50	3.41
Net interest margin (e)							3.99	3.64	3.57

- (a) Includes non-accrual loans.*
- (b) Includes interest-bearing deposits in other banks and federal funds sold.*
- (c) Average balances of securities are based on amortized cost.*
- (d) Includes tax exempt income of \$1,205,000, \$1,295,000 and \$1,238,000, respectively for 2015, 2014 and 2013 on tax-exempt securities and loans whose income and yields are calculated on a tax-equivalent basis.*
- (e) Net interest income divided by average interest-earning assets.*
- (f) Interest income for 2015 reflects net accretion related to the fair value adjustments of loans acquired in the Riverside Bank acquisition in the amount of \$2.7 million.*

The following table sets forth the changes in net interest income (presented on a tax-equivalent basis) due to volume and rate.

Years ended December 31, (in thousands)	2015 versus 2014			2014 versus 2013		
	Volume	Rate	Net	Volume	Rate	Net
Change in interest due to						
Loans	\$9,540	\$2,627	\$12,167	\$2,341	\$(550)	\$1,791
Securities	(378 )	(243 )	(621 )	(878 )	208	(670 )
FHLBB stock	(19 )	37	18	(11 )	61	50
Short term funds	60	2	62	(4 )	(5 )	(9 )
Interest-earning assets	9,203	2,423	11,626	1,448	(286)	1,162
Deposits	572	(193 )	379	46	(394)	(348 )
Repurchase agreements	(1 )	—	(1 )	3	(1 )	2
Capital lease	—	23	23	24	23	47
Note payable	3	3	6	—	—	—
Subordinated Debt	18	17	35	—	—	—
FHLBB advances	(92 )	(28 )	(120 )	(37 )	(22 )	(59 )
Interest-bearing liabilities	500	(178 )	322	36	(394)	(358 )
Net change in net interest income	\$8,703	\$2,601	\$11,304	\$1,412	\$108	\$1,520

Net interest and dividend income represents the difference between interest and dividends earned on loans and securities and interest expense incurred on deposits and borrowings. The level of net interest income is a function of volume, rates and mix of both earning assets and interest-bearing liabilities. Net interest income can be affected by changes in interest rate levels, changes in the volume of assets and liabilities that are subject to re-pricing within different future time periods, and in the level of non-performing assets.

#### Interest and Dividend Income

Tax equivalent interest and dividend income increased \$11.6 million, or 48.1%, to \$35.8 million in 2015.

Loan income increased \$12.2 million, or 60.7%, primarily due to a \$214.0 million, or 45.2%, increase in average loans and a 45 basis point increase in average yield. Interest income for 2015 reflects purchase accounting adjustments consisting of net accretion related to the fair value adjustments of loans acquired in the Riverside Bank acquisition in the amount of \$2.7 million.

Tax equivalent interest and dividend income from securities decreased \$621,000, or 15.6%, in 2015, as a result of an \$8.5 million decrease in average security balances, and a 30 basis point decrease in average yield. Contributing factors to the lower yield includes the maturity, sale, call or pay down of lower yielding securities resulting in a remaining mix of lower yielding securities in the portfolio. Interest from short term funds increased \$62,000 in 2015 as a result of a \$26.5 million increase in average short term balances.

#### Interest Expense

Interest expense increased \$322,000, or 11.9%, to \$3.0 million in 2015.

Interest expense on interest bearing deposit accounts increased \$379,000, or 25.8%, in 2015, as a result of a \$140.3 million, or 33.5%, increase in average interest bearing deposits, partially offset by a 2 basis point decline in the average rate to 0.33%. The decline in average rate was due to the decline in interest rates and changes in product mix.

Interest expense on FHLBB advances decreased \$120,000, or 10.1%, due to a \$2.4 million, or 7.9%, decrease in average advances as a result of scheduled maturities as well as the modification of two advances, in accordance with ASC 470-50, during the third quarter 2015. The modification extended \$21 million in advances to a weighted average



of 39 months. The average borrowing rate decreased to 3.82% from 3.92%.

In December 2015, Salisbury issued \$10 million of subordinated debentures. Interest expense on the subordinated debt, along with issuance costs, in 2015 totaled \$35,000. The proceeds of such issuance, along with cash-on-hand, were used by Salisbury to fully redeem \$16 million of its outstanding Series B Preferred Stock, which was issued pursuant to the participation in the U.S. Treasury's SBLF program.

#### Provision and Allowance for Loan Losses

The provision for loan losses was \$917,000 for 2015, compared with \$1,134,000 for 2014. Net loan charge-offs were \$559,000 and \$459,000, for the respective years. The higher provision for loan losses was supported by maintaining an adequate allowance to gross loans as gross loans continue to increase.

The following table sets forth changes in the allowance for loan losses and other statistical data:

#### Business Activities Loans

Years ended December 31, (dollars in thousands)	2015	2014	2013	2012	2011
Balance, beginning of period	\$5,337	\$4,683	\$4,360	\$4,076	\$3,920
Provision for loan losses	734	1,113	1,066	1,070	1,440
Charge -offs					
Real estate mortgages	(1,045 )	(512 )	(700 )	(573 )	(985 )
Commercial and industrial	(69 )	(19 )	(4 )	(222 )	(180 )
Consumer	(82 )	(28 )	(70 )	(91 )	(201 )
Charge-offs	(1,196 )	(559 )	(774 )	(886 )	(1,366 )
Recoveries					
Real estate mortgages	124	60	6	36	26
Commercial and industrial	464	16	1	38	29
Consumer	18	24	24	26	27
Recoveries	606	100	31	100	82
Net (charge-offs) recoveries	(590 )	(459 )	(743 )	(786 )	(1,284 )
Balance, end of period	\$5,481	\$5,337	\$4,683	\$4,360	\$4,076
Acquired Loan					
Years ended December 31, (dollars in thousands)	2015	2014			
Balance, beginning of period	\$21	\$—			
Provision for loan losses	183	21			
Charge-offs					
Real estate mortgages	(16 )	—			
Charge-offs	(16 )	—			
Recoveries					
Real estate mortgages	5	—			
Commercial and industrial	34	—			
Consumer	8	—			
Recoveries	47	—			
Net recoveries	31	—			
Balance, end of period	\$235	\$21			
Loans receivable, gross	\$703,545	\$677,485	\$441,679	\$392,086	\$373,838
Non-performing loans	16,265	9,890	7,172	9,860	8,076
Accruing loans past due 30-89 days	4,499	4,128	5,374	5,629	2,460
Ratio of allowance for loan losses:					
to loans receivable, gross	0.81 %	0.79 %	1.06 %	1.11 %	1.09 %
to non-performing loans	35.15	54.18	65.30	44.22	50.47
Ratio of non-performing loans					
to loans receivable, gross	2.31	1.46	1.62	2.51	2.16
Ratio of accruing loans past due 30-89 days					
to loans receivable, gross	0.64	0.61	1.22	1.44	0.66

The reserve coverage at December 31, 2015, as measured by the ratio of allowance for loan losses to gross loans, was 0.81%, as compared with 0.79% at December 31, 2014. Non-performing loans (non-accrual loans and accruing loans past-due 90 days or more) increased \$6.4 million to \$16.3 million, or 2.31% of gross loans receivable, at December 31, 2015, up from 1.46% at December 31, 2014. Such increase in non-performing loans is concentrated among a few specific relationships and is not considered to be generally indicative of any adverse trend. Accruing loans past due 30-89 days increased \$0.4 million to \$4.5 million, or 0.64% of gross loans receivable at December 31, 2015. See

“Financial Condition – Loan Credit Quality” below for further discussion and analysis.

27

The credit quality segments of loans receivable and the allowance for loan losses are as follows:

Business Activities Loans

(in thousands)	December 31, 2015		December 31, 2014		December 31, 2013	
	Loans	Allowance	Loans	Allowance	Loans	Allowance
Performing loans	\$527,905	\$4,110	\$457,744	\$3,283	\$416,734	\$2,835
Potential problem loans	1,223	44	9,423	509	8,687	282
Unallocated	—	482	—	409	—	425
Collectively evaluated	529,128	4,636	467,167	4,201	425,421	3,542
Performing loans	—	—	—	—	157	69
Potential problem loans	—	—	11	—	429	19
Impaired loans	19,938	845	16,569	1,136	15,672	1,053
Individually evaluated	\$19,938	\$845	\$16,580	\$1,136	16,258	1,141
Totals	\$549,066	\$5,481	\$483,747	\$5,337	\$441,679	\$4,683

Acquired Loans

(in thousands)	December 31, 2015		December 31, 2014	
	Loans	Allowance	Loans	Allowance
Performing loans	\$148,580	\$46	\$187,966	\$21
Potential problem loans	2,119	2	2,708	—
Unallocated	—	—	—	—
Collectively evaluated	150,699	48	190,674	21
Performing loans	—	—	—	—
Potential problem loans	—	—	—	—
Impaired loans	3,780	187	3,064	—
Individually evaluated	\$3,780	\$187	\$3,064	\$—
Totals	\$154,479	\$235	\$193,738	\$21

The following table sets forth the allocation of the allowance for loan losses among the broad categories of the loan portfolio and the percentage of loans in each category to total loans. Although the allowance has been allocated among loan categories for purposes of the table, it is important to recognize that the allowance is applicable to the entire portfolio. Furthermore, future charge-offs may not necessarily occur in these amounts or proportions.

December 31, (dollars in thousands)(a)	2015		2014		2013		2012		2011	
	Allowance	Loans	Allowance	Loans	Allowance	Loans	Allowance	Loans	Allowance	
Residential	\$2,202	41.20 %	\$1,947	53.12 %	\$1,545	54.34 %	\$1,477	52.87 %	\$1,097	
Commercial	1,598	32.64	1,704	24.37	1,385	23.04	1,059	23.45	1,139	
Construction, land & land development	188	1.67	164	1.91	226	2.11	300	2.71	409	
Home equity lines of credit	354	4.98	359	7.20	393	7.92	457	9.03	382	
Real estate secured	4,342	80.49	4,174	86.60	3,549	87.41	3,293	88.06	3,027	
Commercial and industrial	707	17.26	597	11.25	561	10.72	499	9.94	704	
Consumer	124	0.89	117	0.87	105	0.87	92	1.09	79	
Municipal	61	1.36	61	1.28	43	1.00	36	0.91	24	

General unallocated	482	—	409	—	425	—	440	—	242
Total allowance	\$5,716	100.00%	\$5,358	100.00%	\$4,683	100.00%	\$4,360	100.00%	\$4,076

(a) Percent of loans in each category to total loans.

The allowance for loan losses represents management's estimate of the probable credit losses inherent in the loan portfolio as of the reporting date. The allowance is increased by provisions charged to earnings and by recoveries of amounts previously charged off, and is reduced by loan charge-offs. Loan charge-offs are recognized when management determines a loan, or portion of a loan, to be uncollectible. The allowance for loan losses is computed by segregating the portfolio into three components: (1) loans collectively evaluated for impairment: general loss allocation factors for non-impaired loans are segmented into pools of loans based on similar risk characteristics such as loan product, collateral type and loan-to-value, loan risk rating, historical loss experience, delinquency factors and other similar economic indicators, (2) loans individually evaluated for impairment: individual loss allocations for loans deemed to be impaired based on discounted cash flows or collateral value, and (3) unallocated: general loss allocations for other environmental factors.

Impaired loans and certain potential problem loans, when warranted, are individually evaluated for impairment. Impairment is measured for each individual loan, or for a borrower's aggregate loan exposure, using either the fair value of the collateral, if the loan is collateral dependent, or the present value of expected future cash flows discounted at the loan's effective interest rate. A specific allowance is generally established when the collateral value or discounted cash flows of the loan is lower than the carrying value of that loan.

The component of the allowance for loan losses for loans collectively evaluated for impairment is estimated by stratifying loans into segments and credit risk ratings and then applying management's general loss allocation factors. The general loss allocation factors are based on expected loss experience adjusted for historical loss experience and other qualitative factors, including levels or trends in delinquencies; trends in volume and terms of loans; effects of changes in risk selection and underwriting standards and other changes in lending policies, procedures and practices; experience/ability/depth of lending management and staff; and national and local economic trends and conditions. The qualitative factors are determined based on the various risk characteristics of each loan segment. There were no significant changes in Salisbury's policies or methodology pertaining to the general component of the allowance for loan losses during 2015.

The unallocated component of the allowance is maintained to cover uncertainties that could affect management's estimate of probable losses. It reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating allocated and general reserves in the portfolio.

Determining the adequacy of the allowance at any given period is difficult, particularly during deteriorating or uncertain economic periods, and management must make estimates using assumptions and information that are often subjective and changing rapidly. The review of the loan portfolio is a continuing event in light of a changing economy and the dynamics of the banking and regulatory environment. Should the economic climate deteriorate, borrowers could experience difficulty and the level of non-performing loans, charge-offs and delinquencies could rise, requiring increased provisions. In management's judgment, Salisbury remains adequately reserved both against total loans and non-performing loans at December 31, 2015.

Management's loan risk rating assignments, loss percentages and specific reserves are subjected annually to an independent credit review by an external firm. In addition, the Bank is examined annually on a rotational process by one of its two primary regulatory agencies, the FDIC and CTDOB. As an integral part of their examination process, the FDIC and CTDOB review the adequacy and methodology of the Bank's credit risk ratings and allowance for loan losses.

#### Non-Interest Income

The following table details the principal categories of non-interest income.

Years ended December 31, (dollars in thousands)	2015	2014	2013	2015 vs. 2014		2014 vs. 2013	
Gains on securities, net	\$192	\$—	\$—	\$192	0.0 %	\$—	0.0 %
Trust and wealth advisory	3,265	3,295	3,074	(30 )	(0.9 )	221	7.2
Service charges and fees	3,070	2,473	2,298	597	24.1	175	7.6
Gains on sales of mortgage loans, net	274	64	579	210	328.1	(515)	(88.9 )
Mortgage servicing, net	1	94	35	(93 )	(98.9 )	59	168.6
Bank-owned life insurance	371	245	234	126	51.4	11	4.7
Other	139	81	85	58	71.6	(4 )	(4.7 )
Total non-interest income	\$7,312	\$6,252	\$6,305	\$1,060	17.0 %	\$(53 )	(0.85 )%

Non-interest income increased \$1,060,000, or 16.95%, in 2015 versus 2014. Trust and Wealth Advisory revenues decreased \$30,000 primarily due to decreased market values and a lower volume of assets under management,

partially offset by increased estate fee income. Service charges and fees increased \$597,000 mainly due to the increased volume of accounts due to the Riverside Bank merger in December 2014. Gains on sales of mortgage loans increased \$210,000 due to higher volume of loans sold to the FHLBB Mortgage Partnership Finance Program. Mortgage loans sales totaled \$8.4 million in 2015 versus \$4.4 million in 2014. Income from servicing of mortgage loans decreased \$93,000 due primarily to a slow-down in amortization and impairment charges. Loans serviced under the FHLBB Mortgage Partnership Finance Program totaled \$130.8 million and \$138.1 million at December 31, 2015 and 2014, respectively. BOLI income increased \$58,000 reflecting the BOLI investments of Riverside Bank which Salisbury obtained as a result of the Riverside Bank acquisition.

## Non-Interest Expense

The following table details the principal categories of non-interest expense.

Years ended December 31, (dollars in thousands)	2015	2014	2013	2015 vs. 2014		2014 vs. 2013	
Salaries	\$10,301	\$8,029	\$7,467	\$2,272	28.3	% \$562	7.5 %
Employee benefits	3,729	3,136	2,804	593	18.9	332	11.8
Premises and equipment	3,541	2,831	2,398	710	25.1	433	18.1
Data processing	1,677	1,502	1,514	175	11.7	(12 )	(0.8 )
Professional fees	2,150	1,331	1,212	819	61.5	119	9.8
Collections, OREO, and appraisals	505	458	519	47	10.3	(61 )	(11.9 )
FDIC insurance	658	461	470	197	42.7	(9 )	(1.9 )
Marketing and community support	593	396	393	197	49.7	3	0.8
Amortization of intangible assets	652	291	222	361	124.1	69	31.1
Merger and acquisition related expenses	—	1,974	312	(1,974)	(100.00)	1,662	532.7
Other	2,114	1,729	1,624	385	22.3	105	(6.5 )
Non-interest expense	\$25,920	\$22,138	\$18,935	\$3,782	17.1	% \$3,203	16.9 %

Non-interest expense increased \$3,782,000, or 17.1%, in 2015 versus 2014. Salary expense increased \$2,272,000 due to changes in staffing levels and mix, merit increases, and increased personnel related to the Riverside Bank acquisition. Employee benefit expense increased \$593,000 primarily as a result of increased personnel related to the Riverside Bank merger, partially offset by one-time 2014 expenses related to the termination of the Bank's previously frozen defined benefit pension plan. Premises and equipment expense increased \$710,000 primarily as a result of the increased buildings, computers and equipment related to the Riverside Bank merger. Data processing expense increased \$175,000 mainly as a result of increased volume due to the Riverside bank merger. Professional fees increased \$819,000 primarily due to increased consulting (core conversion, technology support, and imaging projects), legal, and merger related auditing services. Collections, OREO and appraisal expenses increased \$47,000 mainly due to delinquent real estate taxes paid on acquired loans, partially offset by lower collection costs. Amortization of intangible assets increased \$361,000 reflecting the increased intangible asset related to the Sharon branch acquisition and the Riverside Bank merger. FDIC insurance increased \$197,000 due to the increase in assets mainly related to the Riverside Bank merger. Marketing and community support increased \$197,000 mainly related to the acquired branches. 2014 merger and acquisition related expenses were primarily related to legal fees, consulting, and data conversion expenses. All other operating expenses increased \$385,000.

## Income Taxes

The effective income tax rates for 2015 and 2014 were 29.64% and 19.49%, respectively. Fluctuations in the effective tax rate result from changes in the mix of taxable and tax exempt income. Salisbury's effective tax rate was less than the 34% federal statutory rate due to tax-exempt income, primarily from municipal bonds, tax advantaged loans and bank-owned life insurance. For further information on income taxes, see Note 12 of Notes to Consolidated Financial Statements.

Salisbury did not incur Connecticut income tax in 2015 or 2014, other than minimum state income tax, as a result of a Connecticut law that permits banks to shelter certain mortgage income from the Connecticut corporation business tax through the use of a special purpose entity called a Passive Investment Company or PIC. In 2004, Salisbury availed itself of this benefit by forming a PIC, SBT Mortgage Service Corporation. Salisbury's income tax provision reflects the full impact of the Connecticut legislation. Salisbury does not expect to pay other than minimum state income tax in the foreseeable future unless there is a change in Connecticut tax law.

## Comparison of the Years Ended December 31, 2014 and 2013



## Net Interest and Dividend Income

Net interest and dividend income (presented on a tax-equivalent basis) increased \$1,520,000 in 2014 over 2013. The net interest margin increased 7 basis points to 3.64% from 3.57%, due to an 11 basis point decline in the average cost of interest-bearing liabilities and a 2 basis point decline in the average yield on interest-earning assets. The net interest margin is affected by changes in the mix of interest-earning assets and funding liabilities, asset and liability growth, and the effects of changes in market interest rates on the pricing and re-pricing of assets and liabilities.

## Interest and Dividend Income

Tax equivalent interest and dividend income increased \$1.2 million, or 5.1%, to \$24.2 million in 2014.

Loan income increased \$1.8 million, or 9.8%, primarily due to a \$54.5 million, or 13.0%, increase in average loans. This increase in volume was partially offset by a 12 basis point decline in average yield, due to lower market interest rates and their effect on new loan rates, loan re-pricing and loan re-financing activity in 2014.

Tax equivalent interest and dividend income from securities decreased \$670,000, or 14.4%, in 2014, as a result of a \$19.6 million decrease in average security balances, offset partially by a 22 basis point increase in average yield. Contributing factors to the higher yield includes the maturity, call or pay down of lower yielding securities resulting in a remaining mix of higher yielding securities in the portfolio. Interest from short term funds decreased \$9,000 in 2014 as a result of a \$1.9 million decrease in average short term balances and by a 1 basis point decrease in average yield.

#### Interest Expense

Interest expense decreased \$358,000, or 11.7%, to \$2.7 million in 2014.

Interest expense on interest bearing deposit accounts decreased \$348,000, or 19.2%, in 2014, as a result of a 10 basis point decline in the average rate, to 0.35%, offset in part by a \$20.2 million, or 5.1%, increase in average interest bearing deposits. The decline in average rate was due to the decline in interest rates and changes in product mix.

Interest expense on FHLBB advances decreased \$59,000, or 4.7%, due to a \$962,000, or 3.1%, decrease in average advances as a result of scheduled maturities. The average borrowing rate decreased to 3.92% from 3.99%.

#### Provision and Allowance for Loan Losses

The provision for loan losses was \$1,134,000 for 2014, compared with \$1,066,000 for 2013. Net loan charge-offs were \$459,000 and \$743,000, for the respective years. The higher provision for loan losses was supported by maintaining an adequate allowance to gross loans as gross loans continue to increase.

The reserve coverage at December 31, 2014, as measured by the ratio of allowance for loan losses to gross loans, was 0.79%, as compared with 1.06% at December 31, 2013. Non-performing loans (non-accrual loans and accruing loans past-due 90 days or more) increased \$2.7 million to \$9.9 million, or 1.46% of gross loans receivable, at December 31, 2014, down from 1.62% at December 31, 2013, while accruing loans past due 30-89 days decreased \$1.2 million to \$4.1 million, or 0.61% of gross loans receivable at December 31, 2014. See "Financial Condition – Loan Credit Quality" below for further discussion and analysis.

#### Non-Interest Income

Non-interest income decreased \$53,000, or 0.8%, in 2014 versus 2013. Trust and Wealth Advisory revenues increased \$221,000 primarily due to increased market values and slightly higher estate fee income. Service charges and fees increased \$175,000 due to increased interchange, deposit and loan servicing fees. Gains on sales of mortgage loans decreased \$515,000 due to significantly lower mortgage volume of loans sold to the FHLBB Mortgage Partnership Finance Program. Mortgage loans sales totaled \$4.4 million in 2014 versus \$18.7 million in 2013. Income from servicing of mortgage loans increased \$59,000 due primarily to a slow-down in amortization. Loans serviced under the FHLBB Mortgage Partnership Finance Program totaled \$138.1 million and \$146.3 million at December 31, 2014 and 2013, respectively. BOLI income increased \$11,000 due to an increase in coverage previously provided by Riverside Bank.

#### Non-Interest Expense

Non-interest expense increased \$3.2 million, or 16.9%, in 2014 versus 2013. Salary expense increased \$562,000 due to changes in staffing levels and mix, merit increases, and expenses related to the Riverside Bank acquisition. Employee benefit expense increased \$332,000 primarily as a result of incurring \$208,000 (pre-tax) of expenses related to the termination of the Bank's previously frozen defined benefit pension plan. Premises and equipment expense increased \$433,000 primarily as a result of the opening of the Great Barrington, Massachusetts branch as well as the relocation, consolidation and renovation of the Sharon, Connecticut branch as a result of the acquisition of the Union

Savings Bank branch in Sharon, Connecticut. Data processing expense decreased \$12,000. Professional fees increased \$119,000 primarily due to increased consulting, legal and other professional services. Collections and OREO expenses decreased \$61,000 due to lower appraisal costs and lower OREO write-downs, offset partially by higher collection costs. Amortization of intangible assets increased \$69,000 reflecting the increased intangible asset related to the Sharon branch acquisition and the Riverside Bank merger. Printing supplies increased \$35,000 for the additional supplies needed at our new and acquired branches. Merger and acquisition related expenses were primarily related to legal fees, consulting, and data conversion expenses. All other operating expenses increased \$64,000.

#### Income Taxes

The effective income tax rates for 2014 and 2013 were 19.49% and 18.21%, respectively. Fluctuations in the effective tax rate result from changes in the mix of taxable and tax exempt income. Salisbury's effective tax rate was less than the 34% federal statutory rate due to tax-exempt income, primarily from municipal bonds, tax advantaged loans and bank-owned life insurance. For further information on income taxes, see Note 12 of Notes to Consolidated Financial Statements.

Salisbury did not incur Connecticut income tax in 2014 or 2013, other than minimum state income tax, as a result of a Connecticut law that permits banks to shelter certain mortgage income from the Connecticut corporation business tax through the use of a special purpose entity called a Passive Investment Company or PIC. In 2004, Salisbury availed itself of this benefit by forming a PIC, SBT Mortgage Service Corporation. Salisbury's income tax provision reflects the full impact of the Connecticut legislation. Salisbury does not expect to pay other than minimum state income tax in the foreseeable future unless there is a change in Connecticut tax law.

## Overview

### Assets

During 2015, Salisbury's assets increased by \$35.8 million to \$891.2 million, while loans increased \$25.7 million at December 31, 2015. At December 31, 2015, Salisbury's tangible book value per common share was \$27.69 and Tier 1 leverage and total risk-based capital ratios were 8.56% and 13.51%, respectively. As of December 31, 2015, the Bank was categorized as "well capitalized."

### Securities and Short Term Funds

During 2015, securities decreased \$14.9 million to \$79.9 million, while short-term funds (interest-bearing deposits with other banks) increased \$24.4 million to \$47.2 million. The carrying values of securities are as follows:

Years ended December 31, (dollars in thousands)	2015	2014	2013
Available-for-Sale			
U.S. Treasury notes	\$2,541	\$2,806	\$2,657
U.S. Government agency notes	498	5,874	2,590
Municipal bonds	30,385	40,352	40,437
Mortgage-backed securities	32,202	27,709	33,892
Collateralized mortgage obligations	6,962	9,275	11,888
SBA bonds	3,096	4,465	2,230
Other	1,010	831	797
Non-Marketable			
FHLBB stock	3,176	3,515	5,340
Total Securities	\$79,870	\$94,827	\$99,831

Salisbury evaluates securities for OTTI where the fair value of a security is less than its amortized cost basis at the balance sheet date. As part of this process, Salisbury considers its intent to sell each debt security and whether it is more likely than not that it will be required to sell the security before its anticipated recovery. If either of these conditions are met, Salisbury recognizes an OTTI charge to earnings equal to the entire difference between the security's amortized cost basis and its fair value at the balance sheet date. For securities that meet neither of these conditions, an analysis is performed to determine if any of these securities are at risk for OTTI.

Salisbury evaluates securities for strategic fit and may reduce its position in securities, although it is not more likely than not that Salisbury will be required to sell securities before recovery of their cost basis, which may be maturity. Therefore, management does not consider any of its securities, other than four non-agency CMO securities reflecting OTTI, to be OTTI at December 31, 2015.

In 2009 Salisbury determined that five non-agency CMO securities reflected OTTI and recognized losses for deterioration in credit quality of \$1,128,000. Salisbury deemed the four remaining securities not to have additional OTTI and all other CMO securities not to be OTTI as of December 31, 2014. It is possible that future loss assumptions could change necessitating Salisbury to recognize future OTTI. Salisbury evaluates securities for strategic fit and may reduce its position in securities, although it is not more likely than not that Salisbury will be

required to sell securities before recovery of their cost basis, which may be maturity. The carrying value of such securities judged to be OTTI are as follows:

Available-for-Sale (dollars in thousands)	Par value	Carrying value	Fair value
Non-agency CMO			
December 31, 2015	\$1,867	\$ 1,419	\$1,772
December 31, 2014	2,452	1,968	2,369
December 31, 2013	3,093	2,534	2,724

Accumulated other comprehensive income at December 31, 2015 included net unrealized holding gains, net of tax, of \$1.1 million, which is a decrease of \$1.0 million from December 31, 2014.

## Loans

During 2015, net loans receivable increased \$25.7 million, or 3.8%, to \$699.0 million at December 31, 2015. Portfolio growth during 2015 reflects Salisbury's strong market presence.

Salisbury's retail lending department originates residential mortgage, home equity loans and lines of credit, and consumer loans for the portfolio. During 2015, Salisbury originated \$48.0 million of residential mortgage loans and \$8.1 million of home equity loans for the portfolio, compared with \$52.1 million and \$6.1 million, respectively, in 2014. During 2015, total residential mortgage and home equity loans receivable grew by \$12.5 million to \$324.9 million at December 31, 2015, and represent 46.2% of loans receivable. During 2015, Salisbury's residential mortgage lending department also originated and sold \$8.4 million of residential mortgage loans, compared with \$4.4 million during 2014. All such sold loans were sold through the FHLBB Mortgage Partnership Finance Program with servicing retained by Salisbury. Consumer loans, amounting to \$6.3 million at December 31, 2015, represent 0.9% of loans receivable.

Salisbury's commercial lending department specializes in lending to small and mid-size companies, businesses and municipalities. More specifically, we meet our clients' credit needs by providing short-term and long-term financing, construction loans, commercial mortgages, equipment, working capital, property improvement loans and municipal financing. The department also works with both the Small Business Administration ("SBA") and United States Department of Agriculture ("USDA") Government Guaranteed Lending Programs; however, such loans represent a very small percent of the commercial loan portfolio. Salisbury originated \$121.1 million of commercial loans during 2015. During 2015, total commercial real estate, commercial and industrial and municipal loans increased \$11.8 million to \$372.4 million at December 31, 2015, and represent 53.3% of loans receivable.

The principal categories of loans receivable and loans held-for-sale are as follows:

## Business Activities Loans

December 31, (in thousands)	2015	2014	2013	2012	2011
Residential 1-4 family	\$261,495	\$252,258	\$231,113	\$198,552	\$187,676
Residential 5+ multifamily	6,411	5,556	4,848	3,889	3,187
Construction of residential 1-4 family	7,998	2,004	1,876	2,379	5,305
Home equity lines of credit	35,017	34,627	34,139	34,162	34,621
Residential real estate	310,921	294,445	271,976	238,982	230,789
Commercial	129,446	98,498	91,853	87,382	81,958
Construction of commercial	6,525	18,602	10,948	5,823	7,069
Commercial real estate	135,971	117,100	102,801	93,205	89,027
Farm land	3,193	3,239	3,402	4,320	4,925
Vacant land	8,563	9,342	9,067	9,926	12,828
Real estate secured	458,648	424,126	387,246	346,433	337,569
Commercial and industrial	74,657	49,204	46,292	38,094	29,358
Municipal	9,566	6,083	4,252	3,378	2,415
Consumer	6,195	4,334	3,889	4,181	4,496
Loans receivable, gross	549,066	483,747	441,679	392,086	373,838
Deferred loan origination fees and costs, net	1,189	1,203	1,182	1,032	1,004
Allowance for loan losses	(5,481 )	(5,337 )	(4,683 )	(4,360 )	(4,076 )
Loans receivable, net	\$544,774	\$479,613	\$438,178	\$388,758	\$370,766
Loans held-for-sale					
Residential 1-4 family	\$763	\$568	\$173	\$1,879	\$948



## Acquired Loans

December 31, (in thousands)	2015	2014
Residential 1-4 family	\$7,799	\$9,223
Residential 5+ multifamily	6,136	8,735
Construction of residential 1-4 family	—	—
Home equity lines of credit	—	—
Residential real estate	13,935	17,958
Commercial	88,829	97,899
Construction of commercial	4,874	9,045
Commercial real estate	93,703	106,944
Farm land	—	—
Vacant land	—	—
Real estate secured	107,638	124,902
Commercial and industrial	46,764	68,714
Municipal	—	—
Consumer	77	122
Loans receivable, gross	154,479	193,738
Deferred loan origination fees and costs, net	—	—
Allowance for loan losses	(235 )	(21 )
Loans receivable, net	\$154,244	\$193,717
Loans held-for-sale		
Residential 1-4 family	\$—	\$—

The composition of loans receivable by forecasted maturity distribution is as follows:

December 31, 2015 (in thousands)	Within 1 year	Within 1-5 years	After 5 years	Total
Residential	\$6,408	\$12,340	\$271,091	\$289,839
Home equity lines of credit	1,049	737	33,231	35,017
Commercial	15,913	63,809	138,553	218,275
Construction of commercial	6,376	695	4,328	11,399
Land	2,931	1,758	7,067	11,756
Real estate secured	32,677	79,339	454,270	566,286
Commercial and industrial	35,567	36,634	49,220	121,421
Municipal	2,942	1,119	5,505	9,566
Consumer	522	4,111	1,639	6,272
Loans receivable, gross	\$71,708	\$121,203	\$510,634	\$703,545

The composition of loans receivable due after one year with either fixed, variable or adjustable interest rates is as follows:

December 31, 2015 (in thousands)	Fixed interest rates	Variable or adjustable
		interest rates
Residential	\$130,305	\$153,126
Home equity lines of credit	—	33,968
Commercial	115,172	87,190
Construction of commercial	2,193	2,830
Land	47	8,778
Real estate secured	247,717	285,892
Commercial and industrial	49,194	36,660



Municipal	4,251	2,373
Consumer	4,880	870
Loans receivable, gross	\$ 306,042	\$ 325,795

## Loan Credit Quality

During 2015, total impaired and potential problem loans decreased by \$4.6 million to \$27.1 million, or 3.9% of gross loans receivable at December 31, 2015, from \$31.7 million, compared to 4.7% of gross loans receivable at December 31, 2014.

The credit quality segments of loans receivable and their credit risk ratings are as follows:

## Business Activities Loans

December 31, (in thousands)	2015	2014
Pass	\$514,154	\$430,316
Special mention	13,751	27,428
Performing loans	527,905	457,744
Substandard	1,223	9,434
Doubtful	—	—
Potential problem loans	1,223	9,434
Pass		
Troubled debt restructured loans, accruing	2,874	442
All other non-accrual loans	85	—
Special mention		
Troubled debt restructured loans, accruing	2,532	2,610
Substandard		
Troubled debt restructured loans, accruing	1,305	6,044
Troubled debt restructured loans, non-accrual	3,044	628
All other non-accrual loans	10,006	6,752
Doubtful		
Troubled debt restructured loans, accruing	92	93
Impaired loans	19,938	16,569
Loans receivable, gross	\$549,066	\$483,747
Acquired Loans		

December 31, (in thousands)	2015	2014
Pass	\$143,412	\$182,455
Special mention	5,085	5,511
Performing loans	148,497	187,966
Substandard	2,119	2,708
Doubtful	83	—
Potential problem loans	2,202	2,708
Pass		
Troubled debt restructured loans, accruing	—	—
Special mention		
Troubled debt restructured loans, accruing	—	—
Substandard		
Troubled debt restructured loans, accruing	742	571
Troubled debt restructured loans, non-accrual	—	—
All other non-accrual loans	3,038	1,967
Doubtful		
Troubled debt restructured loans, accruing	—	—
Troubled debt restructured loans, non-accrual	—	—

All other non-accrual loans	—	526
Impaired loans	3,780	3,064
Loans receivable, gross	\$154,479	\$193,738

Changes in impaired and potential problem loans are as follows:

Years ended December 31, (in thousands)	2015				2014			
	Impaired loans		Potential problem loans	Total	Impaired loans		Potential problem loans	Total
	Non-accrual	Accruing			Non-accrual	Accruing		
Net loans placed on non-accrual status	\$9,695	\$(3,181 )	\$(3,591 )	\$2,923	\$6,356	\$(378 )	\$(1,176 )	\$4,802
Loans restored to accrual status	(1,178 )	426	748	(4 )	(856 )	739	—	(117 )
Loan risk rating downgrades to substandard	—	—	88	88	—	—	5,941	5,941
Loan risk rating upgrades from substandard	—	—	(4,379 )	(4,379)	—	—	—	—
Loan repayments	(1,288 )	(555 )	(789 )	(2,632)	(1,745 )	(593 )	(1,235 )	(3,573)
Loan charge-offs (less charge offs for delinquent taxes)	(825 )	—	—	(825 )	(291 )	(6 )	(24 )	(321 )
Increase (decrease) in troubled debt restructuring	—	1,094	(766 )	328	—	1,499	(480 )	1,019
Real estate acquired in settlement of loans	(103 )	—	—	(103 )	(764 )	—	—	(764 )
Increase (decrease) in loans	\$6,301	\$(2,216 )	\$(8,689 )	\$(4,604)	\$2,700	\$1,261	\$3,026	\$6,987

Credit risk remained a focus of management's attention during 2015. There was a decrease in total impaired and potential problem loans, down \$4.6 million in 2015. Net loans placed on non-accrual status, due to payment and financial performance, decreased to \$2.9 million in 2015 from \$4.8 million in 2014. Loans restored to accrual status decreased slightly compared to \$0.1 million in 2014. Downgrades in loan risk ratings to substandard increased to \$0.1 million in 2015 from \$5.9 million in 2014. \$4.4 million in loans were upgraded from substandard in 2015 compared to no upgrades in 2014. Loan repayments decreased to \$2.6 million in 2015 from \$3.6 million in 2014. Loan charge-offs, primarily due to collateral deficiencies increased to \$0.8 million in 2015 from \$0.3 million in 2014. Troubled debt restructures decreased to \$0.3 million in 2015 from \$1.0 million in 2014. Real estate acquired in settlement of loans decreased to \$0.1 million in 2015 from \$0.8 million in 2014.

Salisbury has cooperative relationships with the vast majority of its non-performing loan customers. Substantially all non-performing loans are collateralized with real estate and the repayment of such loans is largely dependent on the return of such loans to performing status or the liquidation of the underlying real estate collateral. Salisbury pursues the resolution of all non-performing loans through collections, restructures, voluntary liquidation of collateral by the borrower and, where necessary, legal action. When attempts to work with a customer to return a loan to performing status, including restructuring the loan, are unsuccessful, Salisbury will initiate appropriate legal action seeking to acquire property by deed in lieu of foreclosure or through foreclosure, or to liquidate business assets.

### Credit Quality Segments

Salisbury categorizes loans receivable into the following credit quality segments.

Impaired loans consist of all non-accrual loans and troubled debt restructured loans, and represent loans for which it is probable that Salisbury will not be able to collect all principal and interest amounts due according to the contractual terms of the loan agreements.

Non-accrual loans, a sub-set of impaired loans, are loans for which the accrual of interest has been discontinued because, in the opinion of management, full collection of principal or interest is unlikely.

Non-performing loans consist of non-accrual loans, and accruing loans past due 90 days and over that are well collateralized, in the process of collection and where full collection of principal and interest is reasonably assured.

Non-performing assets consist of non-performing loans plus real estate acquired in settlement of loans.

Troubled debt restructured loans are loans for which concessions such as reduction of interest rates, other than normal market rate adjustments, or deferral of principal or interest payments, extension of maturity dates, or reduction of principal balance or accrued interest, have been granted due to a borrower's financial condition. Loan restructuring is employed when management believes the granting of a concession will increase the probability of the full or partial collection of principal and interest.

Potential problem loans consist of performing loans that have been assigned a substandard credit risk rating and are not classified as impaired.

Credit Risk Ratings

Salisbury assigns credit risk ratings to loans receivable in order to manage credit risk and to determine the allowance for loan losses. Credit risk ratings categorize loans by common financial and structural characteristics that measure the credit strength of a borrower. Salisbury's rating model has eight risk rating grades, with each grade corresponding to a progressively greater risk of default. Grades 1 through 4 are pass ratings and 5 through 8 are ratings (special mention, substandard, doubtful, and loss) defined by the Bank's regulatory agencies, the FDIC and CTDOB. Risk ratings are assigned to differentiate risk within the portfolio and are reviewed on an ongoing basis and revised, if needed, to reflect changes in the borrowers' current financial position and outlook, risk profiles and the related collateral and structural positions.

Loans risk rated as "special mention" possess credit deficiencies or potential weaknesses deserving management's close attention that if left uncorrected may result in deterioration of the repayment prospects for the loans at some future date.

Loans risk rated as "substandard" are loans where the Bank's position is clearly not protected adequately by borrower current net worth or payment capacity. These loans have well defined weaknesses based on objective evidence and include loans where future losses to the Bank may result if deficiencies are not corrected, and loans where the primary source of repayment such as income is diminished and the Bank must rely on sale of collateral or other secondary sources of collection.

Loans risk rated as "doubtful" have the same weaknesses as substandard loans with the added characteristic that the weakness makes collection or liquidation in full, given current facts, conditions, and values, to be highly improbable. The possibility of loss is high, but due to certain important and reasonably specific pending factors, which may work to strengthen the loan, its reclassification as an estimated loss is deferred until its exact status can be determined.

Loans risk rated as "loss" are considered uncollectible and of such little value that continuance as Bank assets is unwarranted. This classification does not mean that the loan has absolutely no recovery or salvage value, but rather, it is not practical or desirable to defer writing off this loan even though partial recovery may be made in the future. Management actively reviews and tests its credit risk ratings against actual experience and engages an independent third-party to annually validate its assignment of credit risk ratings. In addition, the Bank's loan portfolio and risk ratings are examined annually on a rotating basis by its two primary regulatory agencies, the FDIC and CTDOB.

Impaired Loans

Impaired loans increased \$4.1 million during 2015 to \$23.7 million, or 3.37% of gross loans receivable at December 31, 2014, from \$19.6 million, or 2.89% of gross loans receivable at December 31, 2014.

December 31, (in thousands)	2015	2014	2013
Troubled debt restructurings, accruing	\$7,544	\$9,760	\$8,500
Troubled debt restructurings, non-accrual	3,044	628	1,753
All other non-accrual loans	13,130	9,245	5,419
Impaired loans	\$23,718	\$19,633	\$15,672

Non-Performing Assets

Non-performing assets increased \$5.4 million to \$16.3 million at December 31, 2015, or 1.82% of assets, from \$10.9 million or 1.27% of assets at December 31, 2014. The components of non-performing assets are as follows:

December 31, (in thousands)	2015	2014	2013	2012	2011
Commercial	\$4,611	\$3,150	\$1,857	\$2,235	\$2,337
Vacant land	2,855	2,862	2,870	3,995	3,658
Farm land	1,031	384	384	—	—
Residential 1-4 family	6,446	3,007	1,525	3,024	1,240

Edgar Filing: SALISBURY BANCORP INC - Form 10-K

Residential 5+ multifamily	89	89	—	—	—
Home equity lines of credit	601	348	402	442	173
Real estate secured	15,633	9,840	7,038	9,696	7,408
Commercial and industrial	461	33	134	164	668
Consumer	80	—	—	—	—
Non-accrual loans	16,174	9,873	7,172	9,860	8,076
Accruing loans past due 90 days and over	90	17	—	—	—
Non-performing loans	16,264	9,890	7,172	9,860	8,076
Real estate acquired in settlement of loans, net	—	1,002	377	244	2,744
Non-performing assets	\$16,264	\$10,892	\$7,549	\$10,104	\$10,820

37

Reductions in interest income associated with non-accrual loans are as follows:

Years ended December 31, (in thousands)	2015	2014	2013
Income in accordance with original terms	\$1,416	\$680	\$551
Income recognized	327	48	64
Reduction in interest income	\$1,089	\$632	\$487

The past due status of non-performing loans is as follows:

December 31, (in thousands)	2015	2014	2013
Current	\$4,496	\$1,268	\$1,274
Past due 1-29 days	362	586	241
Past due 30-59 days	306	54	134
Past due 60-89 days	27	214	254
Past due 90-179 days	1,320	1,464	588
Past due 180 days and over	9,753	6,304	4,681
Total non-performing loans	\$16,264	\$9,890	\$7,172

At December 31, 2015, 27.64% of non-accrual loans were current with respect to loan payments, compared with 12.81% at December 31, 2014. Loans past due 180 days and over include one loan of \$2.8 million secured by vacant residential land where Salisbury initiated a foreclosure action that is discussed in Item 3 of Part I, Legal Proceedings of this Form 10-K.

On a combined basis, the five largest non-performing loan relationships account for 48% of the non-performing assets while the combined ten largest loan relationships account for 66% of total non-performing assets. Accordingly asset quality issues are confined to a small number of relationships and management does not consider them to be systemic. All of the ten largest non-performing relationships are secured by real estate and seven of these are actively moving through the legal process. Salisbury endeavors to work constructively to resolve its non-performing loan issues with customers. Substantially all non-performing loans are collateralized with real estate and the repayment of such loans is largely dependent on the return of such loans to performing status or the liquidation of the underlying real estate collateral.

#### Troubled Debt Restructured Loans

Troubled debt restructured loans increased \$0.2 million in 2015 to \$10.6 million, or 1.50% of gross loans receivable, from \$10.4 million, or 1.54% of gross loans receivable at December 31, 2014. The components of troubled debt restructured loans are as follows:

December 31, (in thousands)	2015	2014	2013
Residential 1-4 family	\$4,351	\$4,748	\$4,956
Home equity lines of credit	118	48	48
Personal	222	—	22
Vacant land	122	235	225
Commercial	2,666	4,065	2,691
Real estate secured	7,479	9,096	7,942
Commercial and industrial	65	664	558
Accruing troubled debt restructured loans	7,544	9,760	8,500
Residential 1-4 family	1,149	295	999
Home equity lines of credit	—	88	40
Commercial	1,554	235	608
Vacant land	—	—	—
Real estate secured	2,703	618	1,647



Edgar Filing: SALISBURY BANCORP INC - Form 10-K

Commercial and Industrial	341	10	106
Non-accrual troubled debt restructured loans	3,044	628	1,753
Troubled debt restructured loans	\$10,588	\$10,388	\$10,253

38

The past due status of troubled debt restructured loans is as follows:

December 31, (in thousands)	2015	2014	2013
Current	\$6,771	\$6,514	\$6,559
Past due 1-29 days	453	2,704	1,490
Past due 30-59 days	320	542	95
Past due 60-89 days	—	—	356
Accruing troubled debt restructured loans	7,544	9,760	8,500
Current	1,810	49	999
Past due 1-29 days	—	—	241
Past due 30-59 days	28	—	64
Past due 60-89 days	—	10	—
Past due 90-179 days	1,206	333	449
Past due 180 days and over	—	236	—
Non-accrual troubled debt restructured loans	3,044	628	1,753
Total troubled debt restructured loans	\$10,588	\$10,388	\$10,253

At December 31, 2015, 81.04% of troubled debt restructured loans were current with respect to loan payments, as compared with 63.18% at December 31, 2014.

#### Past Due Loans

Loans past due 30 days or more increased \$3.7 million during 2015 to \$15.9 million, or 2.26% of gross loans receivable at December 31, 2015, compared with \$12.2 million, or 1.80% of gross loans receivable at December 31, 2014. The components of loans past due 30 days or greater are as follows:

December 31, (in thousands)	2015	2014	2013
Past due 30-59 days	\$3,533	\$2,295	\$2,535
Past due 60-89 days	966	1,834	2,840
Past due 90-179 days	—	17	—
Past due 180 days+	90	—	—
Accruing loans	4,589	4,146	5,375
Past due 30-59 days	306	54	133
Past due 60-89 days	27	214	254
Past due 90-179 days	1,320	1,447	588
Past due 180 days and over	9,663	6,305	4,681
Non-accrual loans	11,316	8,020	5,656
Total loans past due 30 days and over	\$15,905	\$12,166	\$11,031

#### Potential Problem Loans

Potential problem loans decreased \$8.8 million during 2015 to \$3.3 million or 0.48% of gross loans receivable at December 31, 2015, compared with \$12.1 million, or 1.78% of gross loans receivable at December 31, 2014. The components of potential problem loans are as follows:

December 31, (in thousands)	2015	2014	2013
Residential 1-4 family	\$655	\$2,829	\$1,528
Residential 5+ multifamily	—	975	975
Construction of residential 1-4 family	—	—	—
Home equity lines of credit	150	786	890
Residential real estate	805	4,590	3,393
Commercial	2,030	5,139	4,036

Edgar Filing: SALISBURY BANCORP INC - Form 10-K

Construction of commercial	—	450	589
Commercial real estate	2,030	5,589	4,625
Farm land	—	723	751
Vacant land	23	66	44
Real estate secured	2,858	10,968	8,813
Commercial and industrial	478	1,146	288
Consumer	6	28	15
Other classified loans receivable	\$3,342	\$12,142	\$9,116

The past due status of potential problem loans is as follows:

December 31, (in thousands)	2015	2014	2013
Current	\$2,716	\$8,302	\$7,646
Past due 1-29 days	229	2,416	189
Past due 30-59 days	150	100	298
Past due 60-89 days	247	1,324	983
Total potential problem loans	\$3,342	\$12,142	\$9,116

At December 31, 2015, 81.27% of potential problem loans were current with respect to loan payments, as compared with 68.08% at December 31, 2014.

Management cannot predict the extent to which economic or other factors may impact such borrowers' future payment capacity, and there can be no assurance that such loans will not be placed on nonaccrual status, restructured, or require increased provision for loan losses.

### Deposits and Borrowings

Deposits during 2015 increased \$39.1 million, or 5.5%, to \$754.5 million at December 31, 2015, compared with \$715.4 million at December 31, 2014. Retail repurchase agreements decreased \$0.2 million during 2015 to \$3.9 million at December 31, 2015, compared with \$4.2 million at December 31, 2014. Total deposits at December 31, 2015 include a single relationship totaling \$28.5 million, or 3.78% of total deposits.

Scheduled maturities of time certificates of deposit in denominations of \$250,000 or more are as follows:

December 31, 2015 (in thousands)	Within 3 months	Within 3-6 months	Within 6-12 months	Over 1 year	Total
Certificates of deposit \$250,000 and over	\$2,520	\$2,624	\$2,929	\$3,195	\$11,268

FHLBB advances decreased \$1.8 million during 2015 to \$27.0 million at December 31, 2015, compared with \$28.8 million at December 31, 2014. The decreases were due to amortizing payments of advances, maturities of advances that were not renewed, and in accordance with ASC 470-50 for two advances which were modified during the quarter ending September 30, 2015. The modification extended \$21 million in advances a weighted average 39 months.

### Subordinated Debentures

In December 2015, Salisbury completed the issuance of \$10.0 million in aggregate principal amount of 6.00% Fixed to Floating Rate Subordinated Notes Due 2025 (the "Notes") in a private placement transaction to various accredited investors including \$500 thousand to certain of Salisbury's related parties. The Notes have a maturity date of December 15, 2025 and bear interest at an annual rate of 6.00% from and including the original issue date of the Notes to, but excluding, December 15, 2020 or the earlier redemption date payable semi-annually in arrears on June 15 and December 15 of each year. Thereafter, from and including December 15, 2020 to, but excluding, December 15, 2025, the annual interest rate will be reset quarterly and equal to the three-month LIBOR, plus 430 basis points, as described in the Notes, payable quarterly, in arrears, on March 15, June 15, September 15 and December 15 of each year during the time that the Notes remain outstanding through December 15, 2025 or earlier redemption date. The notes are redeemable, without penalty, on or after December 15, 2020 and, in certain limited circumstances, prior to that date. As more completely described in the Notes, the indebtedness evidenced by the Notes, including principal and interest, is unsecured and subordinate and junior in right of Salisbury's payments to general and secured creditors and depositors of the Bank. The Notes also contain provisions with respect to redemption features and other matters pertaining to the Notes. The Notes have been structured to qualify as Tier 2 capital for regulatory capital purposes, subject to applicable limitations.

Subordinated debentures totaled \$9.764 million at December 31, 2015, which includes \$236 thousand of remaining unamortized debt issuance costs. The debt issuance costs are being amortized to maturity. The effective interest rate of the subordinated debentures is 6.24%.

#### OFF-BALANCE SHEET ARRANGEMENTS AND CONTRACTUAL CASH OBLIGATIONS

In the normal course of business, Salisbury enters into various contractual obligations that may require future cash payments. Contractual obligations at December 31, 2015 include operating leases, a capital lease, contractual purchases and certain other benefit plans. For further discussion regarding leases see Note 18 to the Consolidated Financial Statements.

The accompanying table summarizes Salisbury's off-balance sheet lending-related financial instruments and significant cash obligations, by remaining maturity, at December 31, 2015. Salisbury's lending-related financial instruments include commitments that have maturities over one year. Contractual purchases include commitments for future cash expenditures, primarily for services and contracts that reflect the minimum contractual obligation under legally enforceable contracts with contract terms that are both fixed and determinable. Excluded from the following table are a number of obligations to be settled in cash, primarily in under one year. These obligations are reflected in Salisbury's Consolidated Balance Sheets and include deposits, FHLBB advances and repurchase agreements that settle within standard market timeframes.

December 31, 2015 (in thousands) By Remaining Maturity	Within 1 year	Within 1-3 years	Within 4-5 years	After 5 years	Total
Residential	\$819	\$1,033	\$500	\$4,268	\$6,620
Home equity lines of credit	86	90	250	25,486	25,912
Commercial	7,891	479	845	4,707	13,922
Land	—	—	—	218	218
Real estate secured	8,796	1,602	1,595	34,679	46,672
Commercial and industrial	37,976	7,732	955	21,062	67,725
Municipal	540	—	—	250	790
Consumer	—	—	—	1,507	1,507
Unadvanced portions of loans	47,312	9,334	2,550	57,498	116,694
Commitments to originate loans	37,688	—	—	—	37,688
Standby letters of credit	1,304	96	—	1	1,401
Total	\$86,304	\$9,430	\$2,550	\$57,499	\$155,783

#### LIQUIDITY

Salisbury manages its liquidity position to ensure it has sufficient funding availability at all times to meet both anticipated and unanticipated deposit withdrawals, loan originations and advances, securities purchases and other operating cash outflows. Salisbury's primary source of liquidity is deposits and though its preferred funding strategy is to attract and retain low cost deposits, its ability to do so is affected by competitive interest rates and terms in its marketplace, and other financial market conditions. Other sources of funding include cash flows from loan and securities principal payments and maturities, funds provided by operations, and discretionary use of national market certificates of deposit and FHLBB advances. Liquidity can also be provided through sales of securities and loans.

Salisbury manages its liquidity in accordance with a liquidity funding policy, and also maintains a contingency funding plan that provides for the prompt and comprehensive response to unexpected demands for liquidity. At December 31, 2015, Salisbury's liquidity ratio, as represented by cash, short term available-for-sale securities and marketable assets to net deposits and short term unsecured liabilities, was 22.67%, up from 17.95% at December 31, 2014. Management believes Salisbury's funding sources will meet anticipated funding needs.

Operating activities for 2015 provided net cash of \$8.4 million. Investing activities utilized net cash of \$10.3 million, principally from sales, calls and maturities of securities of \$29.8 million, offset by purchases of securities available-for-sale of \$16.4 million and net loan originations and purchases of \$24.5 million. Financing activities provided net cash of \$28.0 million, principally from a net deposit and issuance of subordinated debt increase of \$49.5 million, offset by payoff of SBLF preferred stock, repurchase agreements, repayment, modifications, and maturities of FHLBB advances of \$18.0 million and cash dividend payments, on common and preferred stock, of \$3.3 million.

Operating activities for 2014 provided net cash of \$4.5 million. Investing activities provided net cash of \$12.2 million, principally from cash acquired, calls and maturities of securities of \$53.9 million, offset by net loan originations and purchases of \$40.6 million. Financing activities provided net cash of \$6.7 million, principally from a net deposit and

repurchase agreement increase of \$10.4 million, offset by repayment and maturities of FHLBB advances of \$1.6 million and cash dividend payments, on common and preferred stock, of \$2.1 million.

Operating activities for 2013 provided net cash of \$9.7 million. Investing activities utilized net cash of \$23.8 million, principally from net loan advances and sales of OREO of \$50.6 million, partially offset by calls and maturities of securities of \$27.7 million. Financing activities utilized net cash of \$16.7 million, principally from a net deposit and repurchase agreement decline of \$13.1 million, repayment and maturities of FHLBB advances of \$1.6 million and cash dividend payments, on common and preferred stock, of \$2.1 million.

## CAPITAL RESOURCES

## Shareholders' Equity

Shareholders' equity decreased \$11.2 million in 2015 to \$90.6 million at December 31, 2015. Contributing to the decrease in shareholders' equity for 2015 was an other comprehensive loss of \$1.0 million, retirement of SBLF preferred stock of \$16.0 million, and common and preferred stock dividends of \$3.0 million and \$0.2 million, respectively. The decrease was offset in part by net income of \$8.5 million, and common stock issuance of \$0.5 million.

## Preferred Stock

In August 2011, Salisbury issued to the Treasury \$16 million of its Series B Preferred Stock under the SBLF program. The SBLF program is a \$30 billion fund established under the Small Business Jobs Act of 2010 to encourage lending to small businesses by providing Tier 1 capital to qualified community banks with assets of less than \$10 billion. The Preferred Stock qualifies as Tier 1 capital for regulatory purposes and ranks senior to the Common Stock.

The Series B Preferred Stock paid noncumulative dividends. The dividend rate on the Series B Preferred Stock for the initial quarterly dividend period ended September 30, 2011 and each of the next nine quarterly dividend periods the Series B Preferred Stock is outstanding was determined each quarter based on the increase in the Bank's Qualified Small Business Lending. The dividend rate for the quarterly dividend period ended December 31, 2015, was 1.0%. For the eleventh quarterly dividend period through four and one-half years after its issuance, the dividend rate on the Series B Preferred Stock will be 1.0% and after four and one-half years from its issuance the dividend rate would have been fixed at 9.0% per annum. In December 2015, Salisbury issued \$10 million of subordinated debentures and used the proceeds along with other cash-on-hand to redeem all of the Series B Preferred Stock.

## Capital Requirements

Salisbury and the Bank are subject to various regulatory capital requirements administered by the federal banking agencies. Under current regulatory definitions, Salisbury and the Bank meet all capital adequacy requirements to which they are subject and the Bank is considered to be well-capitalized. As a result, the Bank pays lower federal deposit insurance premiums than those banks that are not "well capitalized." Requirements for classification as a well-capitalized institution and for minimum capital adequacy along with Salisbury's and the Bank's regulatory capital ratios are as follows at December 31, 2015 and 2014 under the regulatory capital rules then in effect:

	Minimum for Capital Adequacy		Well Capitalized		December 31, 2015		December 31, 2014	
	2015	2014	2015	2014	Salisbury Bank	Salisbury Bank	Salisbury Bank	Salisbury Bank
Total Capital (to risk-weighted assets)	8.00%	8.00%	10.00%	10.00%	13.51%	13.10%	14.27%	12.75%
Common Equity Tier 1 Capital	4.50	N/A	6.50	N/A	11.17	12.23	N/A	N/A
Tier 1 Capital (to risk-weighted assets)	6.00	4.00	8.00	6.00	11.17	12.23	13.38	11.86
Tier 1 Capital (to average assets)	4.00	4.00	5.00	5.00	8.56	9.37	12.31	10.95

A well-capitalized institution, which is the highest capital category for an institution as defined by the Prompt Corrective Action regulations issued by the FDIC and the FRB, is one which maintains a Total Risk-Based ratio of 10% or above, a Tier 1 Risk-Based ratio of 8% or above, a Common Equity to Tier 1 ratio of 6.5% or above, and a Leverage ratio of 5% or above, and is not subject to any written order, written agreement, capital directive, or prompt corrective action directive to meet and maintain a specific capital level. Maintaining strong capital is essential to



Salisbury and the Bank's safety and soundness. However, the effective management of capital resources requires generating attractive returns on equity to build value for shareholders while maintaining appropriate levels of capital to fund growth, meet regulatory requirements and be consistent with prudent industry practices.

In July 2013, the Federal Reserve Bank (FRB) approved the final rules implementing the Basel Committee on Banking Supervision's capital guidelines for bank holding companies and their bank subsidiaries. On July 9, 2013, the FDIC also approved, as an interim final rule, the regulatory capital requirements for U.S. banks, following the actions of the FRB. On April 8, 2014, the FDIC adopted as final its interim final rule, which is identical in substance to the final rules issued by the FRB in July 2013. Under the final rules, minimum requirements will increase for both the quantity and quality of capital held by the Bank and Company. The rules include a new common equity Tier 1 capital to risk-weighted assets minimum ratio of 4.5%, raise the minimum ratio of Tier 1 capital to risk-weighted assets from 4.0% to 6.0%, require a minimum ratio of Total capital to risk-weighted assets of 8.0%, and require a minimum Tier 1 leverage ratio of 4.0%. A new capital conservation buffer, comprised of common equity Tier 1 capital, is also established above the regulatory minimum capital requirements. This capital conservation buffer is being phased in beginning January 1, 2016 at 0.625% of risk-weighted assets and increases each subsequent year by an additional 0.625% until reaching its final level of 2.50% on January 1, 2019. Strict eligibility criteria for regulatory capital instruments were also implemented under the final rules.

The phase-in period for the final rules began for Salisbury and the Bank on January 1, 2015. As of December 31, 2015, the Company and the Bank met each of their capital requirements and the most recent notification from the FDIC categorized the Bank as "well-capitalized." There are no conditions or events since that notification that management believes have changed the Bank's category.

## Dividends

During 2015 and 2014, Salisbury declared and paid four quarterly common stock dividends of \$0.28 per common share each quarter, totaling \$3,054,000 and \$1,918,000, respectively. The Board of Directors of Salisbury declared a common stock dividend of \$0.28 per common share payable on February 26, 2016 to shareholders of record on February 12, 2016. Common stock dividends, when declared, will generally be paid the last business day of February, May, August and November, although Salisbury is not obligated to pay dividends on those dates or at any other time.

During 2015, Salisbury declared Series B Preferred Stock dividends of \$158,000 to the Treasury. In December 2015, Salisbury redeemed all \$16 million shares of its Series B Preferred Stock and, therefore, will not have to pay future dividends to the Treasury with respect to such stock.

Salisbury's ability to pay cash dividends is dependent on the Bank's ability to pay cash dividends to Salisbury. There are certain restrictions on the payment of cash dividends and other payments by the Bank to Salisbury. Under Connecticut law, the Bank cannot declare a cash dividend except from net profits, defined as the remainder of all earnings from current operations. The total of all cash dividends declared by the Bank in any calendar year shall not, unless specifically approved by the Banking Commissioner, exceed the total of its net profits of that year combined with its retained net profits of the preceding two years.

FRB Supervisory Letter SR 09-4, February 24, 2009, revised March 30, 2009, states that, as a general matter, the Board of Directors of a Bank Holding Company ("BHC") should inform the Federal Reserve and should eliminate, defer, or significantly reduce dividends if (1) net income available to shareholders for the past four quarters, net of dividends previously paid during that period, is not sufficient to fully fund the dividends; (2) the prospective rate of earnings retention is not consistent with capital needs and overall current and prospective financial condition; or (3) the BHC will not meet, or is in danger of not meeting, its minimum regulatory capital adequacy ratios. Moreover, a BHC should inform the Federal Reserve reasonably in advance of declaring or paying a dividend that exceeds earnings for the period (e.g., quarter) for which the dividend is being paid or that could result in a material adverse change to the BHC capital position.

Salisbury believes that the payment of common stock cash dividends is appropriate, provided that such payment considers Salisbury's capital needs, asset quality, and overall financial condition and does not adversely affect the financial stability of Salisbury or the Bank. The continued payment of common stock cash dividends by Salisbury will be dependent on Salisbury's future core earnings, financial condition and capital needs, regulatory restrictions, and other factors deemed relevant by the Board of Directors of Salisbury.

## RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

See Note 1 to the Consolidated Financial Statements for details of recently issued accounting pronouncements and their expected impact on Salisbury's consolidated financial statements.

## IMPACT OF INFLATION AND CHANGING PRICES

Salisbury's consolidated financial statements and related notes thereto presented elsewhere in this Form 10-K are prepared in conformity with GAAP, which require the measurement of financial condition and operating results in terms of historical dollars without considering changes in the relative purchasing power of money, over time, due to inflation. Unlike some other types of companies, the financial nature of Salisbury's consolidated financial statements is more clearly affected by changes in interest rates than by inflation. Interest rates do not necessarily fluctuate in the same direction or in the same magnitude as the prices of goods and services. However, inflation does affect Salisbury to some extent because, as prices increase, the money supply grows and interest rates are affected by inflationary expectations. There is no precise method, however, to measure the effects of inflation on the Company's consolidated

financial statements. Accordingly, any examination or analysis of the financial statements should take into consideration the possible effects of inflation. Although not a material factor in recent years, inflation could impact earnings in future periods.

**Item 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

Salisbury manages its exposure to interest rate risk through its Asset/Liability Management Committee (“ALCO”) using risk limits and policy guidelines to manage assets and funding liabilities to produce financial results that are consistent with Salisbury’s liquidity, capital adequacy, growth, risk and profitability targets. Interest rate risk is the risk of a negative impact to future earnings due to changes in interest rates.

The ALCO manages interest rate risk using income simulation to measure interest rate risk inherent in Salisbury's financial instruments at a given point in time by showing the effect of interest rate shifts on net interest income over a 24-month horizon. In management's December 31, 2015 analysis, three of the simulations incorporate static growth assumptions over the simulation horizons, with allowances made for loan, deposit and security product mix shifts in selected interest rate scenarios, such as movements between lower rate savings and money market deposit accounts and higher rate time deposits, and changes in the reinvestment of loan and securities cash flows. The fourth simulation incorporates management's balance sheet growth assumptions. Additionally, the simulations take into account the specific re-pricing, maturity and prepayment characteristics of differing financial instruments that may vary under different interest rate scenarios.

The ALCO reviews the simulation results to determine whether Salisbury's exposure to change in net interest income remains within established tolerance levels over the simulation horizons and to develop appropriate strategies to manage this exposure. Salisbury's tolerance levels for changes in net interest income in its income simulations varies depending on the magnitude of interest rate changes and level of risk-based capital. All changes are measured in comparison to the projected net interest income that would result from an "unchanged" rate scenario where interest rates remain stable over the forecast horizon. The ALCO also evaluates the directional trends of net interest income, net interest margin and other financial measures over the forecast horizon for consistency with its liquidity, capital adequacy, growth, risk and profitability targets.

ALCO uses four interest rate scenarios to evaluate interest risk exposure and may vary these interest rate scenarios to show the effect of steepening or flattening changes in yield curves as well as parallel changes in interest rates. At December 31, 2015, ALCO used the following interest rate scenarios: (1) unchanged interest rates; (2) immediately rising interest rates – immediate parallel upward shift in market interest rates ranging from 300 basis points for short term rates to 300 basis points for the 10-year Treasury; (3) immediately falling interest rates – immediate non-parallel downward shift in market interest rates ranging from 50 basis points for short term rates to 127 basis points for the 10-year Treasury; and (4) immediately rising interest rates – immediate parallel upward shift in market interest rates ranging from 200 basis points for short term rates to 200 basis points for the 10-year Treasury. Deposit rates are assumed to shift by lesser amounts due to their relative historical insensitivity to market interest rate movements. Further, deposits are assumed to have certain minimum rate levels below which they will not fall. Income simulations do not reflect adjustments in strategy that the ALCO could implement in response to rate shifts.

As of December 31, 2015, net interest income simulations indicated that Salisbury's exposure to changing interest rates over the simulation horizons remained within its tolerance levels. The following table sets forth the estimated change in net interest income from an unchanged interest rate scenario over the periods indicated for changes in market interest rates using Salisbury's financial instruments as of December 31, 2015.

December 31, 2015 (in thousands)	Months 1-12	Months 13-24
Immediately rising interest rates +300bp (static growth assumptions)	(2.41 )%	4.56 %
Immediately falling interest rates (static growth assumptions)	(2.17 )	(4.47 )
Immediately rising interest rates +200bp (static growth assumptions)	(0.87 )	4.74

The negative exposure of net interest income to immediately and gradually rising rates as compared to the unchanged rate scenario results from a faster projected rise in the cost of funds versus income from earning assets, as relatively rate-sensitive money market and time deposits re-price faster than longer duration earning assets. The negative exposure of net interest income to immediately falling rates as compared to an unchanged rate scenario results from a greater decline in earning asset yields compared to rates paid on funding liabilities, as a result of faster prepayments on existing assets and lower reinvestment rates on future loans originated and securities purchased.

While the ALCO reviews simulation assumptions and back-tests simulation results to ensure that they are reasonable and current, income simulation may not always prove to be an accurate indicator of interest rate risk or future net interest margin. Over time, the re-pricing, maturity and prepayment characteristics of financial instruments and the

composition of Salisbury's balance sheet may change to a different degree than estimated. Simulation modeling assumes Salisbury's expectation for future balance sheet growth, which is a function of the business environment and customer behavior. Another significant simulation assumption is the sensitivity of core savings deposits to fluctuations in interest rates. Income simulation results assume that changes in both core savings deposit rates and balances are related to changes in short-term interest rates. The relationship between short-term interest rate changes and core deposit rate and balance changes may differ from those used in ALCO's estimates for income simulation. Lastly, mortgage-backed securities and mortgage loans involve a level of risk that unforeseen changes in prepayment speeds may cause related cash flows to vary significantly in differing rate environments. Such changes could affect the level of reinvestment risk associated with cash flow from these instruments, as well as their market value. Changes in prepayment speeds could also increase or decrease the amortization of premium or accretion of discounts related to such instruments, thereby affecting interest income.

Salisbury also monitors the potential change in market value of its available-for-sale debt securities in changing interest rate environments. The purpose is to determine market value exposure that may not be captured by income simulation, but which might result in changes to Salisbury's capital and liquidity position. Results are calculated using industry-standard analytical techniques and securities data. Available-for-sale equity securities are excluded from this analysis because the market value of such securities cannot be directly correlated with changes in interest rates. The following table summarizes the potential change in market value of available-for-sale debt securities resulting from immediate parallel rate shifts:

December 31, 2015 (in thousands)	Rates up 100bp	Rates up 200bp
U.S. Treasury notes	\$(19 )	\$(30 )
U.S. Government agency notes	(9 )	(19 )
Municipal bonds	(1,133 )	(2,163 )
Mortgage backed securities	(838 )	(1,862 )
Collateralized mortgage obligations	(123 )	(271 )
SBA pools	(13 )	(27 )
Other	(11 )	(21 )
Total available-for-sale debt securities	\$(2,146 )	\$(4,393 )

#### Item 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

##### **Index to Consolidated Financial Statements**

	Page
Reports of Independent Registered Public Accounting Firms	46-47
Consolidated Balance Sheets	48
Consolidated Statements of Income	49
Consolidated Statements of Comprehensive Income	50
Consolidated Statements of Changes in Shareholders' Equity	50
Consolidated Statements of Cash Flows	51-52
Notes to Consolidated Financial Statements	53-95

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the Board of Directors and Shareholders

Salisbury Bancorp, Inc.

Lakeville, Connecticut

We have audited the accompanying consolidated balance sheet of Salisbury Bancorp, Inc. and Subsidiary (the Company) as of December 31, 2015, and the related consolidated statements of income, comprehensive income, changes in shareholders' equity and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit 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 is 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 effectiveness of 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 audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Salisbury Bancorp, Inc. and Subsidiary as of December 31, 2015, and the results of their operations and their cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

/s/ Baker Newman & Noyes

Limited Liability Company

Peabody, Massachusetts

March 30, 2016

46



**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the Board of Directors and Shareholders

Salisbury Bancorp, Inc.

Lakeville, Connecticut

We have audited the accompanying consolidated balance sheet of Salisbury Bancorp, Inc. and Subsidiary (the Company) as of December 31, 2014, and the related consolidated statements of income, comprehensive income, changes in shareholders' equity and cash flows for the years ended December 31, 2014 and 2013. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these 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 audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits 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 effectiveness of 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 financial position of Salisbury Bancorp, Inc. and Subsidiary as of December 31, 2014, and the results of their operations and their cash flows for the years ended December 31, 2014 and 2013, in conformity with accounting principles generally accepted in the United States of America.

/s/ Shatswell, MacLeod & Company, P.C.

Shatswell, MacLeod & Company, P.C.

Peabody, Massachusetts

March 30, 2015

47

## Salisbury Bancorp, Inc. and Subsidiary

**CONSOLIDATED BALANCE SHEETS**

Years ended December 31, (dollars in thousands, except par value)	2015	2014
<b>ASSETS</b>		
Cash and due from banks	\$14,891	\$13,280
Interest bearing demand deposits with other banks	47,227	22,825
Total cash and cash equivalents	62,118	36,105
Securities		
Available-for-sale at fair value	76,694	91,312
Federal Home Loan Bank of Boston stock at cost	3,176	3,515
Loans held-for-sale	763	568
Loans receivable, net (allowance for loan losses: \$5,716 and \$5,358)	699,018	673,330
Other real estate owned	—	1,002
Bank premises and equipment, net	14,307	14,431
Goodwill	12,552	12,552
Intangible assets (net of accumulated amortization: \$2,910 and \$2,258)	2,338	2,990
Accrued interest receivable	2,307	2,334
Cash surrender value of life insurance policies	13,685	13,314
Deferred taxes	1,989	2,428
Other assets	2,245	1,546
<b>Total Assets</b>	<b>\$891,192</b>	<b>\$855,427</b>
<b>LIABILITIES and SHAREHOLDERS' EQUITY</b>		
Deposits		
Demand (non-interest bearing)	\$201,340	\$161,386
Demand (interest bearing)	125,465	117,169
Money market	183,783	174,274
Savings and other	119,651	121,387
Certificates of deposit	124,294	141,210
Total deposits	754,533	715,426
Repurchase agreements	3,914	4,163
Federal Home Loan Bank of Boston advances	26,979	28,813
Subordinated debt <sup>(1)</sup>	9,764	—
Note payable	376	—
Capital lease liability	422	424
Accrued interest and other liabilities	4,630	4,780
<b>Total Liabilities</b>	<b>800,618</b>	<b>753,606</b>
Shareholders' Equity		
Preferred stock - \$.01 per share par value		
Authorized: 25,000; Issued: 16,000 (Series B); Outstanding: 0 and 16,000;		
Liquidation preference: \$1,000 per share	—	16,000
Common stock - \$.10 per share par value		
Authorized: 5,000,000;		
Issued: 2,733,576 and 2,720,766	273	272
Unearned compensation - restricted stock awards	(110 )	(313 )
Paid-in capital	41,364	41,077
Retained earnings	47,922	42,677

Accumulated other comprehensive income, net	1,125	2,108
<b>Total Shareholders' Equity</b>	<b>90,574</b>	<b>101,821</b>
<b>Total Liabilities and Shareholders' Equity</b>	<b>\$891,192</b>	<b>\$855,427</b>

<sup>(1)</sup>Net of issuance costs, which are capitalized and amortized as a component of interest expense over a period of 10 years.

**Salisbury Bancorp, Inc. and Subsidiary****CONSOLIDATED STATEMENTS OF INCOME**

Years ended December 31, (in thousands except per share amounts)	2015	2014	2013
<b>Interest and dividend income</b>			
Interest and fees on loans	\$31,752	\$19,616	\$17,978
Interest on debt securities			
Taxable	1,179	1,406	1,757
Tax exempt	1,431	1,704	1,948
Other interest and dividends	209	129	67
Total interest and dividend income	34,571	22,855	21,750
<b>Interest expense</b>			
Deposits	1,844	1,465	1,813
Repurchase agreements	7	8	6
Federal Home Loan Bank of Boston advances	1,064	1,184	1,243
Capital lease	70	47	—
Note payable	6	—	—
Subordinated debt	35	—	—
Total interest expense	3,026	2,704	3,062
Net interest and dividend income	31,545	20,151	18,688
<b>Provision for loan losses</b>	917	1,134	1,066
Net interest and dividend income after provision for loan losses	30,628	19,017	17,622
<b>Non-interest income</b>			
Gains on securities, net	192	—	—
Trust and wealth advisory	3,265	3,295	3,074
Service charges and fees	3,070	2,473	2,298
Gains on sales of mortgage loans, net	274	64	579
Mortgage servicing, net	1	94	35
Other	510	326	319
Total non-interest income	7,312	6,252	6,305
<b>Non-interest expense</b>			
Salaries	10,301	8,029	7,467
Employee benefits	3,729	3,136	2,804
Premises and equipment	3,541	2,831	2,398
Data processing	1,677	1,502	1,514
Professional fees	2,150	1,331	1,212
Collections, OREO, and appraisals	505	458	519
FDIC insurance	658	461	470
Marketing and community support	593	396	393
Amortization of intangibles	652	291	222
Merger and acquisition related expenses	—	1,974	312
Other	2,114	1,729	1,624
Total non-interest expense	25,920	22,138	18,935
Income before income taxes	12,020	3,131	4,992
<b>Income tax provision</b>	3,563	610	909
<b>Net income</b>	\$8,457	\$2,521	\$4,083

Edgar Filing: SALISBURY BANCORP INC - Form 10-K

<b>Net income available to common shareholders</b>	\$8,299	\$2,355	\$3,922
Basic earnings per common share	\$3.04	\$1.32	\$2.30
Diluted earnings per common share	3.02	1.32	2.30
Common dividends per share	1.12	1.12	1.12

**Salisbury Bancorp, Inc. and Subsidiary****CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**

Years ended December 31, (in thousands)	2015	2014	2013
Net income	\$8,457	\$2,521	\$4,083
Other comprehensive (loss) income			
Net unrealized (losses) gains on securities available-for-sale	(1,297)	2,534	(3,743)
Reclassification of net realized gains in net income	(192 )	—	—
Unrealized (losses) gains on securities available-for-sale	(1,489)	2,534	(3,743)
Income tax benefit (expense)	506	(862 )	1,273
Unrealized (losses) gains on securities available-for-sale, net of tax	(983 )	1,672	(2,470)
Change in unrecognized pension plan (expense) income	—	(924 )	1,635
Income tax benefit (expense)	—	314	(556 )
Change in unrecognized pension plan (expense) income, net of tax	—	(610 )	1,079
Other comprehensive (loss) income, net of tax	(983 )	1,062	(1,391)
Comprehensive income	\$7,474	\$3,583	\$2,692

## Salisbury Bancorp, Inc. and Subsidiary

**CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY**

(in thousands, except share amounts)	Common Stock		Preferred Stock	Paid-in capital	Retained earnings	Unearned compensation- restricted stock awards	Accumulated other comp- rehensive income (loss)	Total share- holders' equity
	Shares	Amount						
Balances at December 31, 2012	1,689,691	\$ 169	\$16,000	\$13,158	\$40,233	\$—	\$2,437	\$71,9
Net income for year	—	—	—	—	4,083	—	—	4,08
Other comprehensive loss, net of tax	—	—	—	—	—	—	(1,391 )	(1,3
Common stock dividends declared (\$1.12 per share)	—	—	—	—	(1,915 )	—	—	(1,9
Preferred stock dividends declared	—	—	—	—	(161 )	—	—	(16
Issuance of restricted common stock	19,600	2	—	488	—	(490 )	—	—
Forfeiture of restricted common stock	(500 )	—	—	(12 )	—	12	—	—
Stock based compensation-restricted								

Edgar Filing: SALISBURY BANCORP INC - Form 10-K

stock awards	—	—	—	—	—	143	—	143
Issuance of common stock for director fees	1,330	—	—	34	—	—	—	34
Balances at December 31, 2013	1,710,121	\$171	\$16,000	\$13,668	\$42,240	\$(335)	) \$1,046	\$72,7
Net income for year	—	—	—	—	2,521	—	—	2,52
Other comprehensive income, net of tax	—	—	—	—	—	—	1,062	1,06
Common stock dividends declared (\$1.12 per share)	—	—	—	—	(1,918)	) —	—	(1,9
Preferred stock dividends declared	—	—	—	—	(166)	) —	—	(166
Acquisition of Riverside Bank	1,001,485	100	—	27,151	—	—	—	27,2
Issuance of common stock for executives	2,250	—	—	61	—	—	—	61
Issuance of restricted common stock	6,750	1	—	182	—	(183)	) —	—
Forfeiture of restricted common stock	(2,000)	) —	—	(50)	) —	50	—	—
Stock based compensation-restricted stock awards	—	—	—	—	—	155	—	155
Issuance of common stock for director fees	2,160	—	—	65	—	—	—	65
Balances at December 31, 2014	2,720,766	\$272	\$16,000	\$41,077	\$42,677	\$(313)	) \$2,108	\$101
Net income for year	—	—	—	—	8,457	—	—	8,45
Other comprehensive loss, net of tax	—	—	—	—	—	—	(983)	) (983
Common stock dividends declared (\$1.12 per share)	—	—	—	—	(3,054)	) —	—	(3,0
Preferred stock dividends declared	—	—	—	—	(158)	) —	—	(158
Stock options exercised	9,450	1	—	182	—	—	—	183
Issuance of common stock for executives	1,000	—	—	29	—	—	—	29
Forfeiture of restricted common stock	(300)	) —	—	(7)	) —	7	—	—
Issuance of common stock for directors fees	2,660	—	—	81	—	—	—	81
Stock based compensation-restricted stock awards	—	—	—	2	—	196	—	198
Redemption of preferred stock	—	—	(16,000)	) —	—	—	—	(16,
Balances at December 31, 2015	2,733,576	\$273	\$—	\$41,364	\$47,922	\$(110)	) \$1,125	\$90,5





Salisbury Bancorp, Inc. and Subsidiary

**CONSOLIDATED STATEMENTS OF CASH FLOWS**

Years ended December 31, (in thousands)	2015	2014	2013
<b>Operating Activities</b>			
Net income	\$8,457	\$2,521	\$4,083
Adjustments to reconcile net income to net cash provided by operating activities:			
(Accretion), amortization and depreciation			
Securities	240	198	365
Bank premises and equipment	1,234	1,031	856
Core deposit intangible	652	291	222
Mortgage servicing rights	356	303	389
Fair value adjustment on loans	(2,725 )	(181 )	32
Fair value adjustment on deposits	(417 )	(69 )	—
(Gains) and losses, including write-downs			
Sales and calls of securities available-for-sale, net	(192 )	—	—
Gain on sales of loans, excluding capitalized servicing rights	(125 )	(54 )	(285 )
Loss on other real estate owned	81	99	133
Loss on sale/disposals of premises and equipment	45	6	34
Provision for loan losses	917	1,134	1,066
Proceeds from loans sold	8,549	4,449	18,693
Loans originated for sale	(8,619 )	(4,790 )	(16,702)
Decrease (increase) in deferred loan origination fees and costs, net	14	(21 )	(150 )
Mortgage servicing rights originated	(148 )	(17 )	(294 )
Increase (decrease) in mortgage servicing rights impairment reserve	3	(15 )	(23 )
Decrease (increase) in interest receivable	27	(162 )	58
Deferred tax expense (benefit)	945	(673 )	(134 )
(Increase) decrease in prepaid expenses	(295 )	(57 )	706
Increase in cash surrender value of life insurance policies	(371 )	(245 )	(234 )
(Increase) decrease in income tax receivable	(512 )	—	311
(Decrease) increase in income taxes payable	(86 )	64	—
(Increase) decrease in other assets	(103 )	41	(637 )
Decrease (increase) in accrued expenses	(155 )	269	734
Decrease in interest payable	(16 )	(3 )	(55 )
Increase in other liabilities	107	80	346
Stock options exercised	183	—	—
Issuance of shares for directors' fees	81	65	34
Stock based compensation-restricted stock awards	227	216	143
Net cash provided by operating activities	8,354	4,480	9,691
<b>Investing Activities</b>			
Maturity (purchase) of interest-bearing time deposits with other banks	—	738	(738 )
Redemption of Federal Home Loan Bank of Boston stock	339	1,825	407
Purchases of securities available-for-sale	(16,373)	(502 )	—
Proceeds from sales of securities available-for-sale	3,861	—	—
Proceeds from calls of securities available-for-sale	10,925	8,115	3,800
Proceeds from maturities of securities available-for-sale	14,668	9,644	23,888
Loan originations and principal collections, net	(24,481)	(37,872)	(52,088)

Edgar Filing: SALISBURY BANCORP INC - Form 10-K

Loans purchased	—	(2,711 )	—
Recoveries of loans previously charged off	653	101	31
Proceeds from sales of other real estate owned	855	40	1,423
Purchase of life insurance policies	—	(1,100 )	—
Capital expenditures	(779 )	(2,156 )	(556 )
Cash and cash equivalents acquired	—	17,462	—
Union Savings Bank branch acquisition	—	18,650	—
Riverside Bank acquisition	—	18,650	—
Net cash (utilized) provided by investing activities	(10,332)	12,234	(23,833)

51

Salisbury Bancorp, Inc. and Subsidiary

**CONSOLIDATED STATEMENTS OF CASH FLOWS (Continued)**

Years ended December 31, (in thousands)	2015	2014	2013
<b>Financing Activities</b>			
Increase (decrease) in deposit transaction accounts, net	56,023	16,306	(2,997 )
Decrease in time deposits, net	(16,499)	(7,552 )	(10,849)
(Decrease) increase in securities sold under agreements to repurchase, net	(249 )	1,609	770
Principal payments on Federal Home Loan Bank of Boston advances	(791 )	(1,598 )	(1,569 )
Modification fees on Federal Home Loan Bank of Boston advances	(1,043 )	—	—
Decrease in capital lease obligation	(2 )	(1 )	—
Payoff of preferred stock	(16,000)	—	—
Issuance of subordinated debt, net of issuance costs	9,764	—	—
Common stock dividends paid	(3,054 )	(1,918 )	(1,915 )
Series B preferred stock dividends paid	(158 )	(166 )	(161 )
Net cash provided (utilized) by financing activities	27,991	6,680	(16,721)
Net increase (decrease) in cash and cash equivalents	26,013	23,394	(30,863)
Cash and cash equivalents, beginning of year	36,105	12,711	43,574
Cash and cash equivalents, end of year	\$62,118	\$36,105	\$12,711
<b>Operating Activities</b>			
Interest	\$3,460	\$2,477	\$3,117
Income taxes	3,216	1,258	732
<b>Non-cash transfers</b>			
Note payable to finance building purchase	376	—	—
From loans to other real estate owned	101	764	1,689
From other real estate owned to loans	167	—	—
The Company recorded a capital lease asset and incurred a capital lease obligation in connection with the lease of a building	—	—	425
Union Savings Bank, N.A. branch acquisition 2014			
Cash and cash equivalents acquired	—	17,462	—
Net loans acquired	—	63	—
Fixed assets acquired	—	158	—
Core deposit intangible	—	490	—
Deposits assumed	—	18,172	—
Accrued interest payable assumed	—	1	—
Riverside Bank acquisition 2014			
Cash and cash equivalents acquired	—	18,650	—
Investments acquired	—	11,742	—
Net loans acquired	—	196,305	—
Fixed assets acquired	—	1,543	—
Accrued interest receivable acquired	—	412	—
Cash surrender value of life insurance policies acquired	—	4,440	—
Other assets acquired	—	2,154	—
Core deposit intangible	—	2,215	—
Deposits assumed	—	211,200	—

Accrued interest payable assumed	—	28	—
Other liabilities assumed	—	1,705	—

52

## **Salisbury Bancorp, Inc. and Subsidiary**

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

#### NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Salisbury is the bank holding company for Salisbury Bank (the "Bank"), a State chartered commercial bank. Salisbury's activity is currently limited to the holding of the Bank's outstanding capital stock and the Bank is Salisbury's only subsidiary and its primary investment. The Bank is a Connecticut chartered and Federal Deposit Insurance Corporation (the "FDIC") insured commercial bank headquartered in Lakeville, Connecticut. The Bank's principal business consists of attracting deposits from the public and using such deposits, with other funds, to make various types of loans and investments. The Bank conducts its business through thirteen full-service offices located in Litchfield, Berkshire and Dutchess and Orange Counties in Connecticut, Massachusetts and New York, respectively.

The accompanying consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America. The following is a summary of significant accounting policies:

#### Principles of Consolidation

The consolidated financial statements include those of Salisbury and its subsidiary after elimination of all inter-company accounts and transactions.

#### Basis of Financial Statement Presentation

The financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America. In preparing the financial statements, management is required to make extensive use of estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the statement of condition, and revenues and expenses for the period. Actual results could differ significantly from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses, expected cash flows from loans acquired in a business combination, other-than-temporary impairment of securities and impairment of goodwill and intangibles.

Certain reclassifications have been made to the 2014 and 2013 financial statements to make them consistent with the 2015 presentation.

#### **Cash and Cash Equivalents**

Cash and cash equivalents include cash and balances due from banks. Due to the nature of cash and cash equivalents, Salisbury estimated that the carrying amount of such instruments approximated fair value. The nature of the Bank's business requires that it maintain amounts due from banks which, at times, may exceed federally insured limits. The Bank has not experienced any losses on such amounts and all amounts are maintained with well-capitalized institutions. In 2015, a 3% reserve ratio was assessed on net transaction accounts over \$14.5 million, up to and including \$103.6 million (which may be adjusted by the FRB). A 10% reserve ratio was assessed on net transaction accounts in excess of \$103.6 million (which may be adjusted by the FRB). In 2014, a 3% reserve ratio was assessed on net transaction accounts over \$13.3 million up to and including \$89.0 million. A 10% reserve ratio was assessed on net transaction accounts in excess of \$89.0 million.

#### **Securities**

Securities that may be sold as part of Salisbury's asset/liability or liquidity management or in response to or in anticipation of changes in interest rates and resulting prepayment risk, or for other similar factors, are classified as available-for-sale and carried at their fair market value. Unrealized holding gains and losses on such securities are reported net of related taxes, if applicable, as a separate component of shareholders' equity. Securities that Salisbury has the ability and positive intent to hold to maturity are classified as held-to-maturity and carried at amortized cost. Realized gains and losses on the sales of all securities are reported in earnings and computed using the specific identification cost basis. Securities are reviewed regularly for other-than-temporary impairment ("OTTI"). Premiums and discounts are amortized or accreted utilizing the interest method over the life or call of the term of the investment security. For any debt security with a fair value less than its amortized cost basis, Salisbury will determine whether it has the intent to sell the debt security or whether it is more likely than not it will be required to sell the debt security before the recovery of its amortized cost basis. If either condition is met, Salisbury will recognize a full impairment charge to earnings. For all other debt securities that are considered OTTI and do not meet either condition, the credit loss portion of impairment will be recognized in earnings as realized losses. The OTTI related to all other factors will be recorded in other comprehensive income. Declines in marketable equity securities below their cost that are deemed other than temporary are reflected in earnings as realized losses.

### **Federal Home Loan Bank of Boston Stock**

The Bank is a member of the Federal Home Loan Bank of Boston (“FHLBB”). The FHLBB is a cooperative that provides services, including funding in the form of advances, to its member banking institutions. As a requirement of membership, the Bank must own a minimum amount of FHLBB stock, calculated periodically based primarily on its level of borrowings from the FHLBB. No market exists for shares of the FHLBB and therefore, they are carried at par value. FHLBB stock may be redeemed at par value five years following termination of FHLBB membership, subject to limitations which may be imposed by the FHLBB or its regulator, the Federal Housing Finance Board, to maintain capital adequacy of the FHLBB. While the Bank currently has no intentions to terminate its FHLBB membership, the ability to redeem its investment in FHLBB stock would be subject to the conditions imposed by the FHLBB. Based on the capital adequacy and the liquidity position of the FHLBB, management believes there is no impairment related to the carrying amount of the Bank’s FHLBB stock as of December 31, 2015. Deterioration of the FHLBB’s capital levels may require the Bank to deem its restricted investment in FHLBB stock to be OTTI. If evidence of impairment exists in the future, the FHLBB stock would reflect fair value using either observable or unobservable inputs. The Bank will continue to monitor its investment in FHLBB stock.

### **Loans**

Loans receivable consist of loans that management has the intent and ability to hold for the foreseeable future or until maturity or pay-off. Loans receivable are reported at their outstanding principal balance, net of unamortized deferred loan origination fees and costs. Interest income is accrued on the unpaid principal balance. Deferred loan origination fees and costs are amortized as an adjustment to yield over the lives of the related loans.

Loans held-for-sale consist of residential mortgage loans that management has the intent to sell. Loans held-for-sale are valued at the lower of cost or market as determined by outstanding commitments from investors or current investor yield requirements calculated on the aggregate loan basis, net of deferred loan origination fees and costs. Changes in the carrying value, deferred loan origination fees and costs, and realized gains and losses on sales of loans held-for-sale are reported in earnings as gains and losses on sales of mortgage loans, net, when the proceeds are received from investors.

The accrual of interest on loans, including troubled debt restructured loans, is generally discontinued when principal or interest is past due by 90 days or more, or earlier when, in the opinion of management, full collection of principal or interest is unlikely, except for loans that are well collateralized, in the process of collection and where full collection of principal and interest is assured. When a loan is placed on non-accrual status, interest previously accrued but not collected is reversed against current income. Income on such loans, including impaired loans, is then recognized only to the extent that cash is received and future collection of principal is probable. Loans, including troubled debt restructured loans, are restored to accrual status when principal and interest payments are brought current and future payments are reasonably assured, following a sustained period of repayment performance by the borrower in accordance with the loan's contractual terms.

Troubled debt restructured loans include those for which concessions such as reduction of interest rates, other than normal market rate adjustments, or deferral of principal or interest payments, extension of maturity dates, or reduction of principal balance or accrued interest, have been granted due to a borrower’s financial condition. The decision to restructure a loan, versus aggressively enforcing the collection of the loan, may benefit Salisbury by increasing the ultimate probability of collection.

Troubled debt restructured loans are classified as accruing or non-accruing based on management’s assessment of the collectability of the loan. Loans which are already on non-accrual status at the time of the troubled debt restructuring generally remain on non-accrual status for approximately six months before management considers such loans for return to accruing status. Accruing troubled debt restructured loans are generally placed into non-accrual status if and



when the borrower fails to comply with the restructured terms.

### **Acquired Loans**

Loans that Salisbury acquired through business combinations are initially recorded at fair value with no carryover of the related allowance for credit losses. Determining the fair value of the loans involves estimating the amount and timing of principal and interest cash flows initially expected to be collected on the loans and discounting those cash flows at an appropriate market rate of interest.

For loans that meet the criteria stipulated in Accounting Standards Codification (ASC) 310-30, "Loans and Debt Securities Acquired with Deteriorated Credit Quality," Salisbury recognizes the accretable yield, which is defined as the excess of all cash flows expected to be collected at acquisition over the initial fair value of the loan, as interest income on a level-yield basis over the expected remaining life of the loan. The excess of the loan's contractually required payments over the cash flows expected to be collected is the nonaccretable difference. The nonaccretable difference is not recognized as an adjustment of yield, a loss accrual, or a valuation allowance. Going forward, Salisbury continues to evaluate whether the timing and the amount of cash to be collected are reasonably expected. Subsequent significant increases in cash flows Salisbury expects to collect will first reduce any previously recognized valuation allowance and then be reflected prospectively as an increase to the level yield. Subsequent decreases in expected cash flows may result in the loan being considered impaired. Interest income is not recognized to the extent that the net investment in the loan would increase to an amount greater than the estimated payoff amount.

For ASC 310-30 loans, the expected cash flows reflect anticipated prepayments, determined on a loan by loan basis according to the anticipated collection plan of these loans. The expected prepayments used to determine the accretable yield are consistent between the cash flows expected to be collected and projections of contractual cash flows so as to not affect the nonaccretable difference. For ASC 310-30 loans, prepayments result in the recognition of the nonaccretable balance as current period yield. Changes in prepayment assumptions may change the amount of interest income and principal expected to be collected.

For loans that do not meet the ASC 310-30 criteria, Salisbury accretes interest income on a level yield basis using the contractually required cash flows. Salisbury subjects loans that do not meet the ASC 310-30 criteria to ASC Topic 450, "Contingencies" by collectively evaluating these loans for an allowance for loan losses.

Acquired loans that met the criteria for nonaccrual of interest prior to the acquisition are considered performing upon acquisition, regardless of whether the customer is contractually delinquent, if Salisbury can reasonably estimate the timing and amount of the expected cash flows on such loans and if Salisbury expects to fully collect the new carrying value of the loans. As such, Salisbury may no longer consider the loan to be nonaccrual or nonperforming and may accrue interest on these loans, including the impact of any accretable yield.

#### Allowance for Loan Losses

The allowance for loan losses represents management's estimate of the probable credit losses inherent in the loan portfolio as of the reporting date. The allowance is increased by provisions charged to earnings and by recoveries of amounts previously charged off, and is reduced by loan charge-offs. Loan charge-offs are recognized when management determines a loan or portion of a loan to be uncollectible.

The determination of the adequacy of the allowance is based on management's ongoing review of numerous factors, including the growth and composition of the loan portfolio, historical loss experience over an economic cycle, probable credit losses based upon internal and external portfolio reviews, credit risk concentrations, changes in lending policy, current economic conditions, analysis of current levels and asset quality, delinquency levels and trends, estimates of the current value of underlying collateral, the performance of individual loans in relation to contract terms, and other pertinent factors.

While management believes that the allowance for loan losses is adequate, the allowance is an estimate, and ultimate losses may vary from management's estimate. Future additions to the allowance may also be necessary based on changes in assumptions and economic conditions. In addition, various regulatory agencies periodically review the allowance for loan losses. Such agencies may require additions to the allowance based on their judgments about information available to them at the time of their examination.

Changes in the estimate are recorded in the results of operations in the period in which they become known, along with provisions for estimated losses incurred during that period.

The allowance for loan losses is computed by segregating the portfolio into three components: (1) loans collectively evaluated for impairment: general loss allocation factors for non-impaired loans based on loan product, collateral type and abundance, loan risk rating, historical loss experience, delinquency factors and other similar economic indicators, (2) loans individually evaluated for impairment: individual loss allocations for loans deemed to be impaired based on discounted cash flows or collateral value, and (3) unallocated: general loss allocations for other environmental factors.

#### Loans collectively evaluated for impairment

This component of the allowance for loan losses is stratified by the following loan segments: residential real estate secured (residential 1-4 family and 5+ multifamily, construction of residential 1-4 family, and home equity lines of

credit), commercial real estate secured (commercial and construction of commercial), secured by land (farm and vacant land), commercial and industrial, municipal and consumer. Management's general loss allocation factors are based on expected loss experience adjusted for historical loss experience and other qualitative factors, including levels/trends in delinquencies; trends in volume and terms of loans; effects of changes in risk selection and underwriting standards and other changes in lending policies, procedures and practices; experience/ability/depth of lending management and staff; and national and local economic trends and conditions. There were no changes in Salisbury's policies or methodology pertaining to the general component of the allowance for loan losses during 2015.

The qualitative factors are determined based on the various risk characteristics of each loan segment. Risk characteristics relevant to each portfolio segment are as follows:

Residential real estate - Salisbury generally does not originate loans with a loan-to-value ratio greater than 80 percent and does not grant subprime loans. All loans in this segment are collateralized by owner-occupied residential real estate and repayment is dependent on the credit quality of the individual borrower. The overall health of the economy, including unemployment rates and housing prices, will have an effect on the credit quality in this segment.

Commercial real estate - Loans in this segment are primarily income-producing properties throughout Salisbury's market area. The underlying cash flows generated by the properties are adversely impacted by a downturn in the economy as evidenced by increased vacancy rates which, in turn, will have an effect on the credit quality in this segment. For commercial loans management annually obtains business and personal financial statements, tax returns, and, where applicable, rent rolls, and continually monitors the repayment of these loans.

Construction loans - Loans in this segment are primarily residential construction loans which typically roll into a permanent residential mortgage loan when construction is completed, or commercial construction which consist primarily of owner occupied commercial construction projects.

Commercial and industrial loans - Loans in this segment are made to businesses and are generally secured by assets of the business. Repayment is expected from the cash flows of the business. A weakened economy, and resultant decreased consumer spending, has an effect on the credit quality in this segment.

Municipal loans – Loans in this segment are extensions of credit to municipal and other governmental entities throughout Salisbury's market area. The bank-qualified, tax-exempt loans are backed by the full faith and credit of the borrowing entity with taxing or appropriating authority, as appropriate. Maturities range from one year for bond anticipation notes to twenty years for long-term project finance. The ability of the borrower to pay may be affected by an economic downturn resulting in a severe reduction in tax or other revenues coupled with the depletion of an entity's reserve liquidity. Historical default rates for bank-qualified (small issuer) general obligation municipal credit facilities are near 0%.

Consumer loans - Loans in this segment are generally unsecured and repayment is dependent on the credit quality of the individual borrower.

#### Loans individually evaluated for impairment

This component relates to loans that are classified as impaired. Impairment is measured on a loan by loan basis for all portfolio loans (except consumer loans and homogeneous residential real estate loans) by either the present value of expected future cash flows discounted at the loan's effective interest rate or the fair value of the collateral if the loan is collateral dependent. An allowance is established when the discounted cash flows (or collateral value) of the impaired loan are lower than the carrying value of that loan.

A loan is considered impaired when, based on current information and events, it is probable that Salisbury will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed.

Salisbury periodically may agree to modify the contractual terms of loans. When a loan is modified and a concession is made to a borrower experiencing financial difficulty, the modification is considered a troubled debt restructuring ("TDR"). All TDRs are classified as impaired.

#### Unallocated

An unallocated component is maintained to cover uncertainties that could affect management's estimate of probable losses. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying

assumptions used in the methodologies for estimating allocated and general reserves in the portfolio.

#### Other Real Estate Owned (“OREO”)

Salisbury's loans collateralized by real estate and all other real estate owned (“OREO”) are located principally in northwestern Connecticut and New York and Massachusetts towns, which constitute Salisbury's service area. Accordingly, the collectability of a substantial portion of the loan portfolio and OREO is susceptible to changes in market conditions in Salisbury’s service area. While management uses available information to recognize losses on loans and OREO, future additions to the allowance or write-downs of OREO may be necessary based on changes in local economic conditions, particularly in Salisbury’s service area. In addition, various regulatory agencies, as an integral part of their examination process, periodically review Salisbury's allowance for loan losses and valuation of OREO. Such agencies may require Salisbury to recognize additions to the allowance or write-downs based on their judgments of information available to them at the time of their examination.

As of December 31, 2015 the recorded investment in residential mortgage loans collateralized by residential real estate that were in the process of foreclosure was \$2.9 million.

OREO consists of properties acquired through foreclosure or a deed in lieu of foreclosure. These properties are initially transferred at fair value less estimated costs to sell. Any write-down from cost to estimated fair value required at the time of foreclosure is charged to the allowance for loan losses. A valuation allowance is maintained for declines in market value and for estimated selling expenses. Increases to the valuation allowance, expenses associated with ownership of these properties, and gains and losses from their sale are included in OREO expense.

#### Income Taxes

Deferred income taxes are provided for differences arising in the timing of income and expenses for financial reporting and for income tax purposes using the asset/liability method of accounting for income taxes. Deferred income taxes and tax benefits are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. Salisbury provides deferred taxes for the estimated future tax effects attributable to temporary differences and carry-forwards when realization is assured beyond a reasonable doubt. A valuation allowance is established against deferred tax assets when, based upon all available evidence, it is determined that it is more likely than not that some or all of the deferred tax assets will not be realized.

#### Bank Premises and Equipment

Bank premises, furniture and equipment are carried at cost, less accumulated depreciation and amortization computed on the straight-line method over the estimated useful lives of the assets. Leasehold improvements are amortized on the straight-line basis over the shorter of the estimated useful lives of the improvements or the term of the related leases. Guidelines for expected useful life are as follows:

- Building /Improvements – 39 years
- Land Improvements – 15 years
- Furniture and Fixtures – 7 years
- Computer Equipment – 5 years
- Software – 3 years

#### Intangible Assets

Intangible assets consist of core deposit intangibles and goodwill. Intangible assets equal the excess of the purchase price over the fair value of the tangible net assets acquired in business combinations accounted for using the acquisition method of accounting. Salisbury's assets at December 31, 2015, and 2014, include goodwill of \$2,358,000 arising from the purchase of a branch office in 2001, \$7,152,000 arising from the 2004 acquisition of Canaan National Bancorp, Inc., \$319,000 arising from the 2007 purchase of a branch office in New York State, and \$2,723,000 arising from the acquisition of Riverside Bank in December 2014. See Note 8.

On an annual basis management assesses intangible assets for impairment, and for the year ending December 31, 2015, concluded there was no impairment. If a permanent loss in value is indicated, an impairment charge to income will be recognized.

#### Statements of Cash Flows

For the purpose of the Consolidated Statements of Cash Flows, cash and cash equivalents include cash and due from banks and interest-bearing demand deposits with other financial institutions.

### Computation of Earnings per Share

The Company defines unvested share-based payment awards that contain non-forfeitable rights to dividends as participating securities that are included in computing earnings per share (EPS) using the two-class method.

The two-class method is an earnings allocation formula that determines earnings per share for each share of common stock and participating securities according to dividends declared and participation rights in undistributed earnings. Under this method, all earnings (distributed and undistributed) are allocated to common shares and participating securities based on their respective rights to receive dividends. Basic EPS excludes dilution and is computed by dividing income allocated to common stockholders by the weighted-average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that then shared in the earnings of the entity.

## Recent Accounting Pronouncements

In May 2014 and August 2015, respectively, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2014-09 and 2015-14, "Revenue from Contracts with Customers (Topic 606)." The objective of ASU 2014-09 is to clarify principles for recognizing revenue and to develop a common revenue standard for GAAP and International Financial Reporting Standards. The guidance in ASU 2014-09 affects any entity that either enters into contracts with customers to transfer goods or services or enters into contracts for the transfer of nonfinancial assets unless those contracts are within the scope of other standards. The core principal of the guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. For public entities, the amendments in ASU 2015-14 defer the effective date of ASU 2014-09 to interim and annual reporting periods beginning after December 15, 2017. Early adoption is permitted, but not before the original effective date (i.e. interim and annual reporting periods beginning after December 15, 2016). Salisbury is currently reviewing ASU 2014-09 and 2015-14 to determine if they will have an impact on its consolidated financial statements.

In April 2015, the FASB issued ASU 2015-03, "Interest - Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs." The amendments in this ASU require that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The recognition and measurement guidance for debt issuance costs are not affected by the amendments in this ASU. The standard is effective for interim and annual reporting periods beginning after December 15, 2015, with early adoption permitted. The guidance should be applied on a retrospective basis. Salisbury adopted this guidance in 2015 and presented the costs related to the issuance of subordinated debt as a direct reduction of the carrying amount of the debt.

In April 2015, the FASB issued ASU 2015-05, "Intangibles – Goodwill and Other - Internal-Use Software (Subtopic 350-40): Customer's Accounting for Fees Paid in a Cloud Computing Arrangement." This ASU provides guidance to customers about whether a cloud computing arrangement includes a software license. If a cloud computing arrangement includes a software license, the customer should account for the software license element of the arrangement consistent with the acquisition of other software licenses. If a cloud computing arrangement does not include a software license, the customer should account for the arrangement as a service contract. The new guidance does not change the accounting for a customer's accounting for service contracts. ASU 2015-05 is effective for interim and annual reporting periods beginning after December 15, 2015. Salisbury anticipates that the adoption of this ASU will not have a material impact on its consolidated financial statements.

In September 2015, the FASB issued ASU 2015-16, "Simplifying the Accounting for Measurement-Period Adjustments." Under the ASU, an acquirer must recognize adjustments to provisional amounts that are identified during the measurement period in the reporting period in which the adjustment amounts are determined. The effect on earnings of changes in depreciation or amortization, or other income effects (if any) as a result of the change to the provisional amounts, calculated as if the accounting had been completed as of the acquisition date, must be recorded in the reporting period in which the adjustment amounts are determined rather than retrospectively. The ASU also requires that the acquirer present separately on the face of the income statement, or disclose in the notes, the portion of the amount recorded in current-period earnings by line item that would have been recorded in previous reporting periods if the adjustment to the provisional amounts had been recognized as of the acquisition date. ASU 2015-16 is effective for fiscal years beginning after December 15, 2015, including interim periods within those fiscal years. Early application is permitted for financial statements that have not been issued. Salisbury anticipates that the adoption of this ASU will not have a material impact on its consolidated financial statements.

In January 2016, the FASB issued ASU 2016-01, "Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities." This ASU requires an entity to: i) measure equity investments at fair value through net income, with certain exceptions; (ii) present in other comprehensive income the



changes in instrument-specific credit risk for financial liabilities measured using the fair value option; (iii) present financial assets and financial liabilities by measurement category and form of financial asset; (iv) calculate the fair value of financial instruments for disclosure purposes based on an exit price and; (v) assess a valuation allowance on deferred tax assets related to unrealized losses of AFS debt securities in combination with other deferred tax assets. The guidance provides an election to subsequently measure certain nonmarketable equity investments at cost less any impairment and adjusted for certain observable price changes. The guidance also requires a qualitative impairment assessment of such equity investments and amends certain fair value disclosure requirements. The guidance is effective for interim and annual reporting periods beginning after December 15, 2017. Early adoption is only permitted for the provision related to instrument-specific credit risk. Salisbury is currently evaluating the impact of the new standard on the consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, "Leases (Topic 842)," which provides new guidance related to accounting for leases.

The ASU requires that an entity recognize substantially all leasing activities on its balance sheet. Specifically, a lessee will be required to recognize a liability to make lease payments (the lease liability) and a “right-of-use” asset representing the right to use the underlying asset for the lease term. The asset and liability will initially be measured at the present value of the future lease payments. The new guidance will be effective for public business entities for annual periods beginning after December 15, 2018, and interim periods therein. For all other entities, the ASU will be effective for annual periods beginning after December 15, 2019, and interim periods thereafter. Early adoption will be permitted for all entities. Salisbury anticipates that the adoption of this ASU will not have a material impact on its consolidated financial statements.

## NOTE 2 – MERGERS AND ACQUISITIONS

On December 5, 2014, the Company acquired Riverside Bank. Riverside Bank operated four banking offices serving Dutchess, Ulster and Orange Counties in New York, and was merged with and into the Bank. This business combination is an extension of the Salisbury franchise and the goodwill recognized results from the expected synergies and earnings accretion from this combination, including future cost savings related to Riverside’s operations. The combination was negotiated between the companies and was approved unanimously by their respective boards of directors.

Riverside Bank shareholders received 1,001,485 shares of the Company common stock. On the acquisition date, Riverside Bank had 741,876 outstanding common shares. Salisbury exchanged its stock in a ratio of 1.35 shares of the Company’s common stock for each share of Riverside Bank stock. The 1,001,485 shares of Salisbury common stock issued in this exchange were valued at \$27.19 per share based on the closing price of Salisbury posted on December 5, 2014 resulting in consideration paid of \$27 million. Salisbury paid \$1.0 thousand in cash consideration to settle all fractional shares outstanding of Riverside Bank.

The results of Riverside Bank’s operations are included in Salisbury’s Consolidated Statements of Income from the date of acquisition.

The assets and liabilities in the Riverside Bank acquisition were recorded at their fair value based on the utilization of third party specialists and management’s best estimate using information available at the date of acquisition. Consideration paid, and fair values of Riverside Bank’s assets acquired and liabilities assumed are summarized in the following tables:

Consideration Paid: (In thousands)	Amount
Salisbury Bancorp common stock issued to Riverside Bank common stockholders	\$27,230
Cash consideration paid for fractional shares	1
Riverside stock options, vested upon acquisition	20
Total consideration paid	\$27,251

Recognized amounts of identifiable assets acquired and liabilities		Fair Value	As Recorded
assumed, at fair value:		Adjustment	at Acquisition
Cash and cash equivalents	\$18,650	\$—	\$18,650
Investment securities	11,820	(78 ) <sup>(a)</sup>	11,742
Loans	204,398	(8,093 ) <sup>(b)</sup>	196,305
Premises and equipment	1,046	497 (c)	1,543
Other assets	7,006	—	7,006

Core deposit intangible	—	2,215	2,215
Deposits	(210,559 )	(641 ) <sup>(d)</sup>	(211,200 )
Other liabilities	(1,733 )	—	(1,733 )
Total identifiable net assets	\$30,628	\$(6,100 )	\$24,528
Goodwill	—	—	\$2,723

#### Explanation of Certain Fair Value Adjustments

- (a) The adjustment represents the decrease in the book value of investments to their estimated fair value based on fair values on the date of acquisition.  
The adjustment represents the write down of the book value of loans to their estimated fair value based on current interest rates and expected cash flows, which includes an estimate of expected loan loss inherent in the portfolio. Loans that met the criteria and are being accounted for in accordance with ASC 310-30 had a carrying amount of \$13.7 million at acquisition. Non-impaired loans not accounted for under ASU 310-30 had a carrying value of \$190.7 million at acquisition.
- (b) The adjustment represents the appraised value of the land and building acquired in the acquisition. The land and building were recorded as fixed assets and the building will be amortized over its remaining useful life.
- (c) The adjustment is necessary because the weighted average interest rate of deposits exceeded the cost of similar funding at the time of acquisition.
- (d)

Except for collateral dependent loans with deteriorated credit quality, the fair values for loans acquired from Riverside Bank were estimated using cash flow projections based on the remaining maturity and repricing terms. Cash flows were adjusted by estimating future credit losses and the rate of prepayments. Projected monthly cash flows were then discounted to present value using a risk-adjusted market rate for similar loans. For collateral dependent loans with deteriorated credit quality, to estimate the fair value, Salisbury analyzed the value of the underlying collateral of the loans, assuming the fair values of the loans were derived from the eventual sale of the collateral. Those values were discounted using market derived rates of return, with consideration given to the period of time and costs associated with the foreclosure and disposition of the collateral. There was no carryover of Riverside Bank's allowance for credit losses associated with the loans that were acquired as the loans were recorded at fair value upon acquisition.

Information about the acquired loan portfolio subject to purchased credit impaired loan accounting guidance (ASC 310-30) as of December 5, 2014 (acquisition date) is as follows (in thousands):

(In thousands)	ASC 310-30 Loans
Contractually required principal and interest at acquisition	\$16,209
Contractual cash flows not expected to be collected (nonaccretable discount)	(4,288 )
Expected cash flows at acquisition	11,921
Interest component of expected cash flows (accretable discount)	(1,293 )
Fair value of acquired loans	\$10,628

The following table summarizes activity in the accretable yield for the acquired loan portfolio that falls under the purview of ASC 310-30, *Loans and Debt Securities Acquired with Deteriorated Credit Quality*.

(In thousands)	2015	2014
Balance at beginning of period	\$1,242	\$—
Acquisitions	—	1,293
Accretion	(1,109)	(51 )
Reclassification from non-accretable to accretable	1,768	—
Balance at end of period	\$1,901	\$1,242

At December 31, 2015 and 2014, Salisbury ASC 310-30 loans had an outstanding balance totaling \$10.9 million and \$13.3 million, respectively. The carrying value was \$8.9 million and \$10.6 million, respectively.

The results of operations of Riverside Bank since the acquisition date of December 5, 2014, have been included in Salisbury's consolidated financial statements.

The following pro forma information assumes that the acquisition occurred at the beginning of the earliest period presented.

Years ended December 31, (in thousands)	2014	2013
Total revenue	\$39,841	\$39,640
Net income	6,411	7,136
Net income available to common shareholders	6,245	6,975
Earnings per share		
Basic	\$2.26	\$2.59
Diluted	2.24	2.57

The goodwill is not amortized for book purposes, and is not deductible for tax purposes.

The fair value of savings and transaction deposit accounts acquired from Riverside Bank was assumed to approximate the carrying value as these accounts have no stated maturity and are payable on demand. The fair value of time deposits was estimated by discounting the contractual future cash flows using market rates offered for time deposits of similar remaining maturities.

Direct merger, acquisition and integration costs of the Riverside Bank acquisition were expensed as incurred, and totaled \$2.0 million in 2014 and \$312,000 in 2013.

## NOTE 3 - SECURITIES

The composition of securities is as follows:

(in thousands)	Amortized cost (1)	Gross un- realized gains	Gross un- realized losses	Fair value
December 31, 2015				
<b>Available-for-sale</b>				
U.S. Treasury notes	\$ 2,499	\$ 42	\$ —	\$ 2,541
U.S. Government agency notes	498	—	—	498
Municipal bonds	29,752	633	—	30,385
Mortgage-backed securities				
U.S. Government agencies and U.S. Government-sponsored enterprises	31,900	385	(83 )	32,202
Collateralized mortgage obligations				
U.S. Government agencies	2,002	12	—	2,014
Non-agency	4,487	468	(7 )	4,948
SBA bonds	3,065	31	—	3,096
CRA mutual funds	766	—	(2 )	764
Preferred stock	20	226	—	246
Total securities available-for-sale	\$ 74,989	\$ 1,797	\$ (92 )	\$ 76,694
<b>Non-marketable securities</b>				
Federal Home Loan Bank of Boston stock	\$ 3,176	\$ —	\$ —	\$ 3,176

(in thousands)	Amortized cost (1)	Gross un- realized gains	Gross un- realized losses	Fair value
December 31, 2014				
<b>Available-for-sale</b>				
U.S. Treasury notes	\$ 2,699	\$ 107	\$ —	\$ 2,806
U.S. Government agency notes	5,850	24	—	5,874
Municipal bonds	38,962	1,455	(65 )	40,352
Mortgage-backed securities				
U.S. Government agencies and U.S. Government-sponsored enterprises	27,036	688	(15 )	27,709
Collateralized mortgage obligations				
U.S. Government agencies	2,657	22	—	2,679
Non-agency	6,056	552	(12 )	6,596
SBA bonds	4,336	129	—	4,465
CRA mutual funds	502	2	—	504
Preferred stock	20	307	—	327
Total securities available-for-sale	\$ 88,118	\$ 3,286	\$ (92 )	\$ 91,312
<b>Non-marketable securities</b>				
Federal Home Loan Bank of Boston stock	\$ 3,515	\$ —	\$ —	\$ 3,515

(1) Net of other-than-temporary impairment write-downs recognized in prior years.

Sales of securities available-for-sale and gains realized are as follows:

Edgar Filing: SALISBURY BANCORP INC - Form 10-K

Years ended December 31, (in thousands)	2015	2014	2013
Proceeds	\$3,861	\$—	\$—
Gains realized	180	—	—
Losses realized	(27 )	—	—
Net gains realized	153	—	—
Income tax provision	52	—	—

Edgar Filing: SALISBURY BANCORP INC - Form 10-K

The following table summarizes the aggregate fair value and gross unrealized loss of securities that have been in a continuous unrealized loss position as of the dates presented:

(in thousands)	Less than 12 Months		12 Months or Longer		Total	
	Fair value	Unrealized losses	Fair value	Unrealized losses	Fair Value	Unrealized losses
December 31, 2015						
<b>Available-for-sale</b>						
Mortgage-backed securities	\$14,750	\$ 83	\$53	\$ —	\$14,803	\$ 83
Collateralized mortgage obligations						
Non-agency	237	—	226	7	463	7
CRA mutual funds	764	2	—	—	764	2
Total temporarily impaired securities	\$15,751	\$ 85	\$279	\$ 7	\$16,030	\$ 92
December 31, 2014						
<b>Available-for-sale</b>						
Municipal bonds	\$177	\$ 1	\$1,589	\$ 64	\$1,766	\$ 65
Mortgage-backed securities	56	1	1,885	14	1,941	15
Collateralized mortgage obligations						
Non-agency	441	7	164	5	605	12
Total temporarily impaired securities	\$674	\$ 9	\$3,638	\$ 83	\$4,312	\$ 92

The amortized cost, fair value and tax equivalent yield of securities, by maturity, are as follows:

December 31, 2015 (dollars in thousands)		Amortized cost	Fair value	Yield(1)	
U.S. Treasury notes	Within 1 year	\$ 2,499	\$2,541	3.00	%
	Total	2,499	2,541	3.00	%
U.S. Government agency notes	After 1 year but within 5 years	498	498	0.88	%
	Total	498	498	0.88	%
Municipal bonds	Within 1 year	254	254	5.60	%
	After 1 year but within 5 years	1,217	1,225	5.57	%
	After 5 years but within 10 years	1,894	1,922	6.38	%
	After 10 years but within 15 years	2,632	2,708	6.30	%
	After 15 years	23,755	24,276	6.68	%
	Total	29,752	30,385	6.57	%
Mortgage-backed securities	U.S. Government agency and U.S. Government-sponsored enterprises	31,900	32,202	2.96	%
Collateralized mortgage obligations	U.S. Government agency and U.S. Government-sponsored enterprises	2,002	2,014	1.02	%
	Non-agency	4,487	4,948	4.20	%
SBA bonds		3,065	3,096	2.93	%
CRA mutual funds		766	764	2.07	%
Preferred stock		20	246	2.26	%
Securities available-for-sale		\$ 74,989	\$76,694	4.47	%

(1) Yield is based on amortized cost.



Salisbury evaluates securities for OTTI where the fair value of a security is less than its amortized cost basis at the balance sheet date. As part of this process, Salisbury considers whether it has the intent to sell each debt security and whether it is more likely than not that it will be required to sell the security before its anticipated recovery. If either of these conditions is met, Salisbury recognizes an OTTI charge to earnings equal to the entire difference between the security's amortized cost basis and its fair value at the balance sheet date. For securities that meet neither of these conditions, an analysis is performed to determine if any of these securities are at risk for OTTI.

The following summarizes, by security type, the basis for evaluating if the applicable securities were OTTI at December 31, 2015.

U.S. Government agency mortgage-backed securities: The contractual cash flows are guaranteed by U.S. government agencies and U.S. government-sponsored enterprises. Changes in fair values are a function of changes in investment spreads and interest rate movements and not changes in credit quality. Management expects to recover the entire amortized cost basis of these securities. Furthermore, Salisbury evaluates these securities for strategic fit and may reduce its position in these securities, although it is not more likely than not that Salisbury will be required to sell these securities before recovery of their cost basis, which may be maturity, and does not intend to sell these securities. Therefore, management does not consider the sixteen securities with unrealized losses at December 31, 2015 to be OTTI.

Non-agency CMOs: Salisbury performed a detailed cash flow analysis of its non-agency CMOs at December 31, 2015, to assess whether any of the securities were OTTI. Salisbury uses cash flow forecasts for each security based on a variety of market driven assumptions and securitization terms, including prepayment speed, default or delinquency rate, and default severity for losses including interest, legal fees, property repairs, expenses and realtor fees, that, together with the loan amount are subtracted from collateral sales proceeds to determine severity. In 2009, Salisbury determined that five non-agency CMO securities reflected OTTI and recognized losses for deterioration in credit quality of \$1,128,000. Salisbury judged the four remaining securities not to have additional OTTI and all other CMO securities not to be OTTI as of December 31, 2015. It is possible that future loss assumptions could change necessitating Salisbury to recognize future OTTI for further deterioration in credit quality. Salisbury evaluates these securities for strategic fit and depending upon such factor could reduce its position in these securities, although it has no present intention to do so, and it is not more likely than not that Salisbury will be required to sell these securities before recovery of their cost basis.

CRA mutual funds consist of an investment in a fixed income mutual fund (\$764,000 in total fair value and \$2,000 in total unrealized losses). The severity of the impairment (fair value is approximately 0.26% less than cost) and the duration of the impairment correlates with interest rates in 2015. Salisbury evaluated the near-term prospects of this fund in relation to the severity and duration of the impairment. Based on that evaluation, Salisbury does not consider this investment to be other-than-temporarily impaired at December 31, 2015.

The Company did not recognize any OTTI during the years ended December 31, 2015, 2014 and 2013.

#### NOTE 4 - LOANS

The composition of loans receivable and loans held-for-sale is as follows:

Years ended December 31, (In thousands)	2015 Business			2014 Business		
	Activities	Acquired Loans	Total	Activities	Acquired Loans	Total
Residential 1-4 family	\$261,495	\$7,799	\$269,294	\$252,258	\$9,223	\$261,481
Residential 5+ multifamily	6,411	6,136	12,547	5,556	8,735	14,291
Construction of residential 1-4 family	7,998	—	7,998	2,004	—	2,004
Home equity lines of credit	35,017	—	35,017	34,627	—	34,627
Residential real estate	310,921	13,935	324,856	294,445	17,958	312,403
Commercial	129,446	88,829	218,275	98,498	97,899	196,397
Construction of commercial	6,525	4,874	11,399	18,602	9,045	27,647
Commercial real estate	135,971	93,703	229,674	117,100	106,944	224,044
Farm land	3,193	—	3,193	3,239	—	3,239
Vacant land	8,563	—	8,563	9,342	—	9,342
Real estate secured	458,648	107,638	566,286	424,126	124,902	549,028
Commercial and industrial	74,657	46,764	121,421	49,204	68,714	117,918
Municipal	9,566	—	9,566	6,083	—	6,083
Consumer	6,195	77	6,272	4,334	122	4,456
Loans receivable, gross	549,066	154,479	703,545	483,747	193,738	677,485
Deferred loan origination fees and costs, net	1,189	—	1,189	1,203	—	1,203
Allowance for loan losses	(5,481 )	(235 )	(5,716 )	(5,337 )	(21 )	(5,358 )
Loans receivable, net	\$544,774	\$154,244	\$699,018	\$479,613	\$193,717	\$673,330
Loans held-for-sale						

Residential 1-4 family	\$763	\$—	\$763	\$568	\$—	\$568
------------------------	-------	-----	-------	-------	-----	-------

Salisbury has entered into loan participation agreements with other banks and transferred a portion of its originated loans to the participating banks. Transferred amounts are accounted for as sales and excluded from Salisbury's loans receivable. Salisbury and its participating lenders share ratably in any gains or losses that may result from a borrower's lack of compliance with contractual terms of the loan. Salisbury services the loans on behalf of the participating lenders and, as such, collects cash payments from the borrowers, remits payments (net of servicing fees) to participating lenders and disburses required escrow funds to relevant parties.

Salisbury also has entered into loan participation agreements with other banks and purchased a portion of the other banks' originated loans. Purchased amounts are accounted for as loans without recourse to the originating bank. Salisbury and its originating lenders share ratably in any gains or losses that may result from a borrower's lack of compliance with contractual terms of the loan. The originating banks service the loans on behalf of the participating lenders and, as such, collect cash payments from the borrowers, remit payments (net of servicing fees) to participating lenders and disburse required escrow funds to relevant parties.

At December 31, 2015 and 2014, Salisbury serviced commercial loans for other banks under loan participation agreements totaling \$63.0 million and \$48.0 million, respectively. During 2015, Salisbury sold participation interests in 3 loans with gross outstanding loan balances of \$37.3 million; retaining \$13.8 million in net balances. Additionally, Salisbury purchased a participant share in 11 loans with outstanding balances of \$9.4 million. There are construction loans in the portfolio that have not been fully drawn as of December 31, 2015.

#### Concentrations of Credit Risk

Salisbury's loans consist primarily of residential and commercial real estate loans located principally in northwestern Connecticut, New York and Massachusetts towns, which constitute Salisbury's service area. Salisbury offers a broad range of loan and credit facilities to borrowers in its service area, including residential mortgage loans, commercial real estate loans, construction loans, working capital loans, equipment loans, and a variety of consumer loans, including home equity lines of credit, and installment and collateral loans. All residential and commercial mortgage loans are collateralized by first or second mortgages on real estate. The ability of single family residential and consumer borrowers to honor their repayment commitments is generally dependent on the level of overall economic activity within the market area and real estate values. The ability of commercial borrowers to honor their repayment commitments is dependent on the general economy as well as the health of the real estate economic sector in Salisbury's market area.

#### Credit Quality

Salisbury uses credit risk ratings to determine its allowance for loan losses. Credit risk ratings categorize loans by common financial and structural characteristics that measure the credit strength of a borrower. The rating model has eight risk rating grades, with each grade corresponding to a progressively greater risk of default. Grades 1 through 4 are pass ratings and 5 through 8 are criticized as defined by the regulatory agencies. Risk ratings are assigned to differentiate risk within the portfolio and are reviewed on an ongoing basis and revised, if needed, to reflect changes in the borrowers' current financial position and outlook, risk profiles and the related collateral and structural positions.

Loans rated as "special mention" possess credit deficiencies or potential weaknesses deserving management's close attention that if left uncorrected may result in deterioration of the repayment prospects for the loans at some future date.

Loans rated as "substandard" are loans where the Bank's position is clearly not protected adequately by borrower current net worth or payment capacity. These loans have well defined weaknesses based on objective evidence and include loans where future losses to the Bank may result if deficiencies are not corrected, and loans where the primary source of repayment such as income is diminished and the Bank must rely on sale of collateral or other secondary sources of collection.

Loans rated "doubtful" have the same weaknesses as substandard loans with the added characteristic that the weakness makes collection or liquidation in full, given current facts, conditions, and values, to be highly improbable. The possibility of loss is high, but due to certain important and reasonably specific pending factors, which may work to strengthen the loan, its reclassification as an estimated loss is deferred until its exact status can be determined.

Loans classified as "loss" are considered uncollectible and of such little value that continuance as Bank assets is unwarranted. This classification does not mean that the loan has absolutely no recovery or salvage value, but rather, it is not practical or desirable to defer writing off this loan even though partial recovery may be made in the future.

Management actively reviews and tests its credit risk ratings against actual experience and engages an independent third-party to annually validate its assignment of credit risk ratings. In addition, the Bank's loan portfolio is examined periodically by its regulatory agencies, the FDIC and the Connecticut Department of Banking.

The composition of loans receivable by risk rating grade is as follows:

Business Activities Loans

(in thousands)	Pass	Special mention	Substandard	Doubtful	Loss	Total
December 31, 2015						
Residential 1-4 family	\$248,027	\$6,933	\$ 6,444	\$ 91	\$ —	\$261,495
Residential 5+ multifamily	4,507	1,815	89	—	—	6,411
Construction of residential 1-4 family	7,111	887	—	—	—	7,998
Home equity lines of credit	33,687	545	785	—	—	35,017
Residential real estate	293,332	10,180	7,318	91	—	310,921
Commercial	120,903	4,801	3,742	—	—	129,446
Construction of commercial	6,525	—	—	—	—	6,525
Commercial real estate	127,428	4,801	3,742	—	—	135,971
Farm land	2,162	—	1,031	—	—	3,193
Vacant land	5,567	69	2,927	—	—	8,563
Real estate secured	428,489	15,050	15,018	91	—	458,648
Commercial and industrial	72,887	1,214	555	1	—	74,657
Municipal	9,566	—	—	—	—	9,566
Consumer	6,171	18	6	—	—	6,195
Loans receivable, gross	\$517,113	\$16,282	\$ 15,579	\$ 92	\$ —	\$549,066
Acquired Loans						

(in thousands)	Pass	Special mention	Substandard	Doubtful	Loss	Total
December 31, 2015						
Residential 1-4 family	\$6,824	\$ 199	\$ 776	\$ —	\$ —	\$7,799
Residential 5+ multifamily	6,136	—	—	—	—	6,136
Construction of residential 1-4 family	—	—	—	—	—	—
Home equity lines of credit	—	—	—	—	—	—
Residential real estate	12,960	199	776	—	—	13,935
Commercial	80,406	4,005	4,418	—	—	88,829
Construction of commercial	4,612	—	262	—	—	4,874
Commercial real estate	85,018	4,005	4,680	—	—	93,703
Farm land	—	—	—	—	—	—
Vacant land	—	—	—	—	—	—
Real estate secured	97,978	4,204	5,456	—	—	107,638
Commercial and industrial	45,363	875	443	83	—	46,764
Municipal	—	—	—	—	—	—
Consumer	71	6	—	—	—	77
Loans receivable, gross	\$143,412	\$ 5,085	\$ 5,899	\$ 83	\$ —	\$154,479

## Business Activities Loans

(in thousands)	Pass	Special mention	Substandard	Doubtful	Loss	Total
December 31, 2014						
Residential 1-4 family	\$232,628	\$12,350	\$ 7,187	\$ 93	\$ —	\$252,258
Residential 5+ multifamily	3,420	1,072	1,064	—	—	5,556
Construction of residential 1-4 family	2,004	—	—	—	—	2,004
Home equity lines of credit	32,639	807	1,181	—	—	34,627
Residential real estate	270,691	14,229	9,432	93	—	294,445
Commercial	79,975	10,728	7,795	—	—	98,498
Construction of commercial	18,024	—	578	—	—	18,602
Commercial real estate	97,999	10,728	8,373	—	—	117,100
Farm land	772	1,361	1,106	—	—	3,239
Vacant land	6,039	140	3,163	—	—	9,342
Real estate secured	375,501	26,458	22,074	93	—	424,126
Commercial and industrial	44,903	3,527	774	—	—	49,204
Municipal	6,083	—	—	—	—	6,083
Consumer	4,271	53	10	—	—	4,334
Loans receivable, gross	\$430,758	\$30,038	\$ 22,858	\$ 93	\$ —	\$483,747
Acquired Loans						

(in thousands)	Pass	Special mention	Substandard	Doubtful	Loss	Total
December 31, 2014						
Residential 1-4 family	\$8,661	\$—	\$ 562	\$ —	\$ —	\$9,223
Residential 5+ multifamily	8,735	—	—	—	—	8,735
Construction of residential 1-4 family	—	—	—	—	—	—
Home equity lines of credit	—	—	—	—	—	—
Residential real estate	17,396	—	562	—	—	17,958
Commercial	89,820	3,830	3,723	526	—	97,899
Construction of commercial	9,045	—	—	—	—	9,045
Commercial real estate	98,865	3,830	3,723	526	—	106,944
Farm land	—	—	—	—	—	—
Vacant land	—	—	—	—	—	—
Real estate secured	116,261	3,830	4,285	526	—	124,902
Commercial and industrial	66,098	1,675	941	—	—	68,714
Municipal	—	—	—	—	—	—
Consumer	96	7	19	—	—	122
Loans receivable, gross	\$182,455	\$ 5,512	\$ 5,245	\$ 526	\$ —	\$193,738

The significant decrease, totaling \$14.6 million, in Special Mention loans resulted primarily from various relationship upgrades to a pass rating. The largest relationship upgraded was \$4.9 million, or 33%, of the total. The ten largest upgraded relationships equaled \$10.8 million or 74% of total upgrades. Additionally, approximately \$1.9 million of Special Mention loans paid off in 2015. Upgrades of smaller balance relationships, less than \$300,000 each, accounted for the remainder of the change.

The composition of loans receivable by delinquency status is as follows:

Business Activities Loans

(In thousands)	Current	Past due					180 days and over	30 days and over	Accruing 90 days and over	Non-accrual
		1-29 days	30-59 days	60-89 days	90-179 days					
December 31, 2015										
Residential 1-4 family	\$254,152	\$1,781	\$1,931	\$683	\$973	\$1,975	\$5,562	\$—	\$5,671	
Residential 5+ multifamily	6,254	—	68	—	—	89	157	—	89	
Construction of residential 1-4 family	7,826	172	—	—	—	—	—	—	—	
Home equity lines of credit	33,744	363	306	101	113	390	910	—	601	
Residential real estate	301,976	2,316	2,305	784	1,086	2,454	6,629	—	6,361	
Commercial Construction of commercial	126,440	1,618	474	—	233	681	1,388	—	2,349	
Commercial real estate	6,525	—	—	—	—	—	—	—	—	
Farm land	132,965	1,618	474	—	233	681	1,388	—	2,349	
Vacant land	2,172	298	—	—	—	723	723	—	1,031	
Real estate secured	5,734	—	6	—	—	2,823	2,829	—	2,855	
Commercial and industrial	442,847	4,232	2,785	784	1,319	6,681	11,569	—	12,596	
Municipal	73,698	906	35	—	—	18	53	—	461	
Consumer	9,566	—	—	—	—	—	—	—	—	
Loans receivable, gross	6,096	61	21	17	—	—	38	—	80	
Acquired Loans	\$532,207	\$5,199	\$2,841	\$801	\$1,319	\$6,699	\$11,660	\$—	\$13,137	

(In thousands)	Current	Past due					180 days and over	30 days and over	Accruing 90 days and over	Non-accrual
		1-29 days	30-59 days	60-89 days	90-179 days					
December 31, 2015										
Residential 1-4 family	\$6,823	\$—	\$—	\$110	\$—	\$866	\$976	\$90	\$776	
	6,136	—	—	—	—	—	—	—	—	



Residential 5+ multifamily									
Construction of residential 1-4 family	—	—	—	—	—	—	—	—	—
Home equity lines of credit	—	—	—	—	—	—	—	—	—
Residential real estate	12,959	—	—	110	—	866	976	90	776
Commercial	81,140	4,848	916	—	—	1,925	2,841	—	2,000
Construction of commercial	4,612	—	—	—	—	262	262	—	262
Commercial real estate	85,752	4,848	916	—	—	2,187	3,103	—	2,262
Farm land	—	—	—	—	—	—	—	—	—
Vacant land	—	—	—	—	—	—	—	—	—
Real estate secured	98,711	4,848	916	110	—	3,053	4,079	90	3,038
Commercial and industrial	46,128	471	83	82	—	—	165	—	—
Municipal	—	—	—	—	—	—	—	—	—
Consumer	77	—	—	—	—	—	—	—	—
Loans receivable, gross	\$144,916	\$5,319	\$999	\$192	\$—	\$3,053	\$4,244	\$90	\$3,038

## Business Activities Loans

(In thousands)	Current	Past due					180 days and over	30 days and over	Accruing 90 days and over	Non-accrual
		1-29 days	30-59 days	60-89 days	90-179 days					
December 31, 2014										
Residential 1-4 family	\$241,567	\$7,299	\$1,250	\$555	\$976	\$611	\$3,392	\$—		\$2,445
Residential 5+ multifamily	5,467	—	—	—	89	—	89	—		89
Construction of residential 1-4 family	2,004	—	—	—	—	—	—	—		—
Home equity lines of credit	33,488	387	122	528	39	63	752	—		348
Residential real estate	282,526	7,686	1,372	1,083	1,104	674	4,233	—		2,882
Commercial	94,598	2,079	602	—	—	1,219	1,821	—		1,219
Construction of commercial	18,602	—	—	—	—	—	—	—		—
Commercial real estate	113,200	2,079	602	—	—	1,219	1,821	—		1,219
Farm land	2,119	—	13	723	—	384	1,120	—		384
Vacant land	6,422	51	7	—	39	2,823	2,869	—		2,862
Real estate secured	404,267	9,816	1,994	1,806	1,143	5,100	10,043	—		7,347
Commercial and industrial	48,478	582	91	17	36	—	144	17		33
Municipal	6,083	—	—	—	—	—	—	—		—
Consumer	4,274	47	8	5	—	—	13	—		—
Loans receivable, gross	\$463,102	\$10,445	\$2,093	\$1,828	\$1,179	\$5,100	\$10,200	\$17		\$7,380

(In thousands)	Current	Past due					180 days and over	30 days and over	Accruing 90 days and over	Non-accrual
		1-29 days	30-59 days	60-89 days	90-179 days					
December 31, 2014										
Residential 1-4 family	\$8,661	\$—	\$—	\$—	\$—	\$562	\$562	\$—		\$562
Residential 5+ multifamily	8,735	—	—	—	—	—	—	—		—
	—	—	—	—	—	—	—	—		—

Construction of residential 1-4 family									
Home equity lines of credit	—	—	—	—	—	—	—	—	—
Residential real estate	17,396	—	—	—	—	562	562	—	562
Commercial	95,695	1,109	167	—	285	643	1,095	—	1,931
Construction of commercial	9,045	—	—	—	—	—	—	—	—
Commercial real estate	104,740	1,109	167	—	285	643	1,095	—	1,931
Farm land	—	—	—	—	—	—	—	—	—
Vacant land	—	—	—	—	—	—	—	—	—
Real estate secured	122,136	1,109	167	—	285	1,205	1,657	—	2,493
Commercial and industrial	67,665	740	89	220	—	—	309	—	—
Municipal	—	—	—	—	—	—	—	—	—
Consumer	117	5	—	—	—	—	—	—	—
Loans receivable, gross	\$189,918	\$1,854	\$256	\$220	\$285	\$1,205	\$1,966	\$—	\$2,493

Interest on non-accrual loans that would have been recorded as additional interest income for the years ended December 31, 2015, 2014 and 2013 had the loans been current in accordance with their original terms totaled \$1,089,000, \$632,000 and \$487,000, respectively.

Troubled Debt Restructurings (TDRs)

Troubled debt restructurings occurring during the periods are as follows:

Business Activities Loans (in thousands)	December 31, 2015			December 31, 2014		
	Quantity	Pre-modification balance	Post-modification balance	Quantity	Pre-modification balance	Post-modification balance
Residential real estate	3	\$ 1,071	\$ 1,071	4	\$ 308	\$ 308
Land						
Commercial real estate	1	294	294	4	1,076	1,076
Construction of commercial				1	131	131
Consumer						
Commercial and industrial						
HELOC	1	35	35			
Troubled debt restructurings	5	\$ 1,400	\$ 1,400	9	\$ 1,515	\$ 1,515
Rate reduction and term extension	1	\$ 294	\$ 294		\$	\$
Interest only pursuant to sale				1	24	24
Interest only and term extension				1	48	48
Interest only pursuant to sale and term extension				1	230	230
Interest only				1	30	30
Debt consolidation and term extension	1	148	148	2	447	447
Rate reduction						
Rate reduction interest only						
Debt consolidation, rate reduction, term extension and note bifurcation	1	48	48	1	399	399
Rate reduction and debt consolidation						
Term extension	2	910	910	2	337	337
Troubled debt restructurings	5	\$ 1,400	\$ 1,400	9	\$ 1,515	\$ 1,515
Acquired Loans						
(in thousands)	December 31, 2015			December 31, 2014		
	Quantity	Pre-modification balance	Post-modification balance	Quantity	Pre-modification balance	Post-modification balance
Residential real estate		\$	\$		\$	\$
Land						
Commercial real estate	1	184	184	1	571	571
Construction of commercial						
Consumer						
Commercial and industrial						
HELOC						
Troubled debt restructurings	1	\$ 184	\$ 184	1	\$ 571	571
Rate reduction and term extension	1	\$ 184	\$ 184		\$	\$
Interest only pursuant to sale						
Interest only and term extension						
Interest only pursuant to sale and term extension						
Interest only						
Debt consolidation and term extension						
Rate reduction				1	571	571
Rate reduction interest only						
Debt consolidation, rate reduction, term extension and note bifurcation						
Rate reduction and debt consolidation						

Term extension

Troubled debt restructurings	1	\$ 184	\$ 184	1	\$ 571	\$ 571
------------------------------	---	--------	--------	---	--------	--------

Six loans were restructured during 2015. No concessions have been made with respect to loans that subsequently defaulted in the current reporting period. Salisbury currently does not have any commitments to lend additional funds to TDR loans.

The following table discloses the recorded investment and number of modifications for TDRs within the last year where a concession has been made, that then defaulted in the current reporting period. All TDR loans are included in the Impaired Loan schedule and are individually evaluated.

There were no modifications made in 2015 that subsequently defaulted in 2015.

	Quantity	Balance	Modifications that Subsequently Defaulted For the twelve months ending December 31, 2014
Troubled Debt Restructurings			
Residential 1-4 family	2	\$38	
Commercial real estate <sup>(1)</sup>	1	—	
Total	3	\$38	
	(1)		Loan paid off as of December 31, 2014

#### Impaired loans

Loans individually evaluated for impairment (impaired loans) are loans for which Salisbury does not expect to collect all principal and interest in accordance with the contractual terms of the loan. Impaired loans include all modified loans classified as TDRs and loans on non-accrual status. The components of impaired loans are as follows:

#### Business Activities Loans

Years ended December 31, (in thousands)	2015	2014
Non-accrual loans, excluding troubled debt restructured loans	\$10,093	\$6,752
Non-accrual troubled debt restructured loans	3,044	628
Accruing troubled debt restructured loans	6,802	9,189
Total impaired loans	\$19,939	\$16,569
Commitments to lend additional amounts to impaired borrowers	\$—	\$—

Years ended December 31, (in thousands)	2015	2014
Non-accrual loans, excluding troubled debt restructured loans	\$3,038	\$2,493
Non-accrual troubled debt restructured loans	—	—
Accruing troubled debt restructured loans	742	571
Total impaired loans	\$3,780	\$3,064
Commitments to lend additional amounts to impaired borrowers	\$—	\$—

Allowance for Loan Losses

Changes in the allowance for loan losses are as follows:

(In thousands)	Business Activities Loans December 31, 2015					Acquired Loans December 31, 2015				
	Beginning balance	Provision	Charge- offs	Reco- veries	Ending balance	Beginning balance	Provision	Charge- offs	Reco- veries	Ending balance
Residential	\$2,306	\$746	\$(698)	\$123	\$2,477	\$—	\$79	\$—	\$—	\$2,556
Commercial	1,697	(18)	(214)	1	1,466	7	136	(16)	5	1,592
Land	164	157	(133)	—	188	—	—	—	—	188
Real estate	4,167	885	(1,045)	124	4,131	7	215	(16)	5	4,342
Commercial and industrial	583	(295)	(69)	464	683	14	(24)	—	34	707
Municipal	61	—	—	—	61	—	—	—	—	61
Consumer	117	71	(82)	18	124	—	(8)	—	8	124
Unallocated	409	73	—	—	482	—	—	—	—	482
Totals	\$5,337	\$734	\$(1,196)	\$606	\$5,481	\$21	\$183	\$(16)	\$47	\$5,615

  

(In thousands)	December 31, 2014					December 31, 2014				
	Beginning balance	Provision	Charge- offs	Reco- veries	Ending balance	Beginning balance	Provision	Charge- offs	Reco- veries	Ending balance
Residential	\$1,938	\$657	\$(307)	\$18	\$2,306	\$—	\$—	\$—	\$—	\$2,306
Commercial	1,385	355	(84)	41	1,697	—	7	—	—	1,704
Land	226	58	(121)	1	164	—	—	—	—	164
Real estate	3,549	1,070	(512)	60	4,167	—	7	—	—	4,174
Commercial and industrial	561	25	(19)	16	583	—	14	—	—	597
Municipal	43	18	—	—	61	—	—	—	—	61
Consumer	105	16	(28)	24	117	—	—	—	—	117
Unallocated	425	(16)	—	—	409	—	—	—	—	409
Totals	\$4,683	\$1,113	\$(559)	\$100	\$5,337	\$—	\$21	\$—	\$—	\$5,358

The composition of loans receivable and the allowance for loan losses is as follows:

Business Activities Loans

(in thousands)	Collectively evaluated		Individually evaluated		Total portfolio	
	Loans	Allowance	Loans	Allowance	Loans	Allowance
December 31, 2015						
Residential 1-4 family	\$253,156	\$1,415	\$8,339	\$610	\$261,495	\$2,025
Residential 5+ multifamily	4,640	33	1,771	—	6,411	33
Construction of residential 1-4 family	7,998	65	—	—	7,998	65
Home equity lines of credit	34,298	286	719	68	35,017	354
Residential real estate	300,092	1,799	10,829	678	310,921	2,477
Commercial	125,173	1,265	4,273	113	129,446	1,378
Construction of commercial	6,403	87	122	1	6,525	88
Commercial real estate	131,576	1,352	4,395	114	135,971	1,466
Farm land	2,162	23	1,031	14	3,193	37
Vacant land	5,486	122	3,077	29	8,563	151

Edgar Filing: SALISBURY BANCORP INC - Form 10-K

Real estate secured	439,316	3,296	19,332	835	458,648	4,131
Commercial and industrial	74,131	673	526	10	74,657	683
Municipal	9,566	61	—	—	9,566	61
Consumer	6,115	124	80	—	6,195	124
Unallocated allowance	—	482	—	—	—	482
Totals	\$529,128	\$4,636	\$19,938	\$845	\$549,066	\$5,481



## Acquired Loans

(in thousands)	Collectively evaluated		Individually evaluated		ASC 310-30 loans		Total portfolio	
	Loans	Allowance	Loans	Allowance	Loans	Allowance	Loans	Allowance
December 31, 2015								
Residential 1-4 family	\$7,023	\$—	\$776	\$79	\$—	\$—	\$7,799	\$79
Residential 5+ multifamily	6,136	—	—	—	—	—	6,136	—
Construction of residential 1-4 family	—	—	—	—	—	—	—	—
Home equity lines of credit	—	—	—	—	—	—	—	—
Residential real estate	13,159	—	776	79	—	—	13,935	79
Commercial	81,300	19	2,742	107	4,787	2	88,829	128
Construction of commercial	4,612	4	262	—	—	—	4,874	4
Commercial real estate	85,912	23	3,004	107	4,787	2	93,703	132
Farm land	—	—	—	—	—	—	—	—
Vacant land	—	—	—	—	—	—	—	—
Real estate secured	99,071	23	3,780	186	4,787	2	107,638	211
Commercial and industrial	45,650	24	—	—	1,114	—	46,764	24
Municipal	—	—	—	—	—	—	—	—
Consumer	61	—	—	—	16	—	77	—
Unallocated allowance	—	—	—	—	—	—	—	—
Totals	\$144,782	\$47	\$3,780	\$186	\$5,917	\$2	\$154,479	\$235

## Business Activities Loans

(in thousands)	Collectively evaluated		Individually evaluated		Total portfolio	
	Loans	Allowance	Loans	Allowance	Loans	Allowance
December 31, 2014						
Residential 1-4 family	\$245,997	\$1,316	\$6,261	\$549	\$252,258	\$1,865
Residential 5+ multifamily	4,536	66	1,020	3	5,556	69
Construction of residential 1-4 family	2,004	13	—	—	2,004	13
Home equity lines of credit	34,231	350	396	9	34,627	359
Residential real estate	286,768	1,745	7,677	561	294,445	2,306
Commercial	93,784	1,018	4,714	486	98,498	1,504
Construction of commercial	18,474	193	128	—	18,602	193
Commercial real estate	112,258	1,211	4,842	486	117,100	1,697
Farm land	2,855	59	384	—	3,239	59
Vacant land	6,245	67	3,097	38	9,342	105
Real estate secured	408,126	3,082	16,000	1,085	424,126	4,167
Commercial and industrial	48,635	532	569	51	49,204	583
Municipal	6,083	61	—	—	6,083	61
Consumer	4,334	117	—	—	4,334	117

Edgar Filing: SALISBURY BANCORP INC - Form 10-K

Unallocated allowance	—	—	—	—	—	409
Totals	\$467,178	\$3,792	\$16,569	\$1,136	\$483,747	\$5,337

72

## Acquired Loans

(in thousands)	Collectively evaluated		Individually evaluated		ASC 310-30 loans		Total portfolio	
	Loans	Allowance	Loans	Allowance	Loans	Allowance	Loans	Allowance
December 31, 2014								
Residential 1-4 family	\$8,661	\$—	\$562	\$—	\$—	\$—	\$9,223	\$—
Residential 5+ multifamily	8,735	—	—	—	—	—	8,735	—
Construction of residential 1-4 family	—	—	—	—	—	—	—	—
Home equity lines of credit	—	—	—	—	—	—	—	—
Residential real estate	17,396	—	562	—	—	—	17,958	—
Commercial	89,820	—	2,502	—	5,577	—	97,899	—
Construction of commercial	9,045	7	—	—	—	—	9,045	7
Commercial real estate	98,865	7	2,502	—	5,577	—	106,944	7
Farm land	—	—	—	—	—	—	—	—
Vacant land	—	—	—	—	—	—	—	—
Real estate secured	116,261	7	3,064	—	5,577	—	124,902	7
Commercial and industrial	66,874	14	—	—	1,840	—	68,714	14
Municipal	—	—	—	—	—	—	—	—
Consumer	103	—	—	—	19	—	122	—
Unallocated allowance	—	—	—	—	—	—	—	—
Totals	\$183,238	\$21	\$3,064	\$—	\$7,436	\$—	\$193,738	\$21

The credit quality segments of loans receivable and the allowance for loan losses are as follows:

## Business Activities Loans

December 31, 2015 (in thousands)	Collectively evaluated		Individually evaluated		Total portfolio	
	Loans	Allowance	Loans	Allowance	Loans	Allowance
Performing loans	\$527,905	\$4,110	\$—	\$—	\$527,905	\$4,110
Potential problem loans	1,223	44	—	—	1,223	44
Impaired loans	—	—	19,938	845	19,938	845
Unallocated allowance	—	482	—	—	—	482
Totals	\$529,128	\$4,636	\$19,938	\$845	\$549,066	\$5,481

## Acquired Loans

December 31, 2015 (in thousands)	Collectively evaluated		Individually evaluated		Total portfolio	
	Loans	Allowance	Loans	Allowance	Loans	Allowance
Performing loans	\$148,580	\$46	\$—	\$—	\$148,580	\$46
Potential problem loans	2,119	2	—	—	2,119	2
Impaired loans	—	—	3,780	187	3,780	187
Unallocated allowance	—	—	—	—	—	—

Edgar Filing: SALISBURY BANCORP INC - Form 10-K

Totals	\$150,699	\$48	\$3,780	\$187	\$154,479	\$235
Business Activities Loans						

December 31, 2014 (in thousands)	Collectively evaluated		Individually evaluated		Total portfolio	
	Loans	Allowance	Loans	Allowance	Loans	Allowance
Performing loans	\$457,744	\$3,283	\$—	\$—	\$457,744	\$3,283
Potential problem loans	9,423	509	11	—	9,434	509
Impaired loans	—	—	16,569	1,136	16,569	1,136
Unallocated allowance	—	409	—	—	—	409
Totals	\$467,167	\$4,201	\$16,580	\$1,136	\$483,747	\$5,337

73

## Acquired Loans

December 31, 2014 (in thousands)	Collectively evaluated		Individually evaluated		Total portfolio	
	Loans	Allowance	Loans	Allowance	Loans	Allowance
Performing loans	\$187,966	\$21	\$—	\$—	\$187,966	\$21
Potential problem loans	2,708	—	—	—	2,708	—
Impaired loans	—	—	3,064	—	3,064	—
Unallocated allowance	—	—	—	—	—	—
Totals	\$190,674	\$21	\$3,064	\$—	\$193,738	\$21

A specific valuation allowance is established for the impairment amount of each impaired loan, calculated using the fair value of expected cash flows or collateral, in accordance with the most likely means of recovery. Certain data with respect to loans individually evaluated for impairment is as follows:

## Business Activities Loans

(In thousands)	Impaired loans with specific allowance					Impaired loans with no specific allowance			
	Loan balance		Average	Specific allowance	Income recognized	Loan balance			Income Recognized
	Book	Note				Book	Note	Average	
December 31, 2015									
Residential	\$7,482	\$8,094	\$6,449	\$610	\$167	\$2,628	\$2,770	\$3,089	\$98
Home equity lines of credit	535	659	260	68	9	184	199	423	2
Residential real estate	8,017	8,753	6,709	678	176	2,812	2,969	3,512	100
Commercial Construction of commercial	3,131	3,405	2,850	113	123	1,142	1,393	1,624	49
Farm land	122	128	9	1	7	—	—	116	—
Vacant land	733	773	400	14	25	298	352	461	—
Real estate secured	2,870	3,836	3,015	29	3	207	241	72	9
Commercial and industrial	14,873	16,895	12,983	835	334	4,459	4,955	5,785	158
Consumer	95	98	145	10	4	431	481	383	22
Totals	\$14,968	\$16,993	\$13,128	\$845	\$338	\$4,970	\$5,544	\$6,180	\$181

## Acquired Loans

(In thousands)	Impaired loans with specific allowance					Impaired loans with no specific allowance			
	Loan balance		Average	Specific allowance	Income recognized	Loan balance			Income Recognized
	Book	Note				Book	Note	Average	
December 31, 2015									
Residential Home equity lines of credit	\$599	\$716	\$273	\$79	\$—	\$177	\$177	\$376	\$7
	—	—	—	—	—	—	—	—	—

Edgar Filing: SALISBURY BANCORP INC - Form 10-K

Residential real estate	599	716	273	79	—	177	177	376	7
Commercial	675	826	698	107	34	2,067	2,843	2,011	32
Construction of commercial	—	—	—	—	—	262	273	167	22
Farm land	—	—	—	—	—	—	—	—	—
Vacant land	—	—	—	—	—	—	—	—	—
Real estate secured	1,274	1,542	971	186	34	2,506	3,293	2,554	61
Commercial and industrial	—	—	6	—	—	—	4	—	—
Consumer	—	—	—	—	—	—	—	—	—
Totals	\$1,274	\$1,542	\$977	\$186	\$34	\$2,506	\$3,297	\$2,554	\$61

Business Activities Loans

(In thousands)	Impaired loans with specific allowance					Impaired loans with no specific allowance			
	Loan balance		Average	Specific allowance	Income recognized	Loan balance		Income	
	Book	Note				Book	Note	Average	Recognized
December 31, 2014									
Residential Home equity lines of credit	\$5,008	\$5,157	\$4,547	\$552	\$128	\$2,273	\$2,395	\$2,703	\$57
Residential real estate	9	24	91	9	—	387	405	441	4
Commercial	5,017	5,181	4,638	561	128	2,660	2,800	3,144	61
Construction of commercial	3,383	3,563	3,262	486	108	1,331	1,520	1,468	54
Farm land	—	—	—	—	—	128	134	123	—
Vacant land	—	—	—	—	—	384	384	384	—
Real estate secured	3,097	3,996	3,090	38	12	—	—	—	—
Commercial and industrial	11,497	12,740	10,990	1,085	248	4,503	4,838	5,119	115
Consumer	102	161	106	51	2	467	469	516	30
Totals	—	—	—	—	—	—	—	19	—
	\$11,599	\$12,901	\$11,096	\$1,136	\$250	\$4,970	\$5,307	\$5,654	\$145

## Acquired Loans

(In thousands)	Impaired loans with specific allowance				Income recognized	Impaired loans with no specific allowance			
	Loan balance		Average	Specific allowance		Loan balance		Average	Income Recognized
	Book	Note				Book	Note		
December 31, 2014									
Residential	\$—	\$—	\$—	\$—	\$—	\$562	\$716	\$562	\$3
Home equity lines of credit	—	—	—	—	—	—	—	—	—
Residential real estate	—	—	—	—	—	562	716	562	3
Commercial	—	—	—	—	—	2,502	4,014	2,502	12
Construction of commercial	—	—	—	—	—	—	—	—	—
Farm land	—	—	—	—	—	—	—	—	—
Vacant land	—	—	—	—	—	—	—	—	—
Real estate secured	—	—	—	—	—	3,064	4,730	3,064	15
Commercial and industrial	—	—	—	—	—	—	4	—	—
Consumer	—	—	—	—	—	—	—	—	—
Totals	\$—	\$—	\$—	\$—	\$—	\$3,064	\$4,734	\$3,064	\$15

## NOTE 5 - MORTGAGE SERVICING RIGHTS

Loans serviced for others are not included in the consolidated balance sheets. Balances of loans serviced for others and the fair value of mortgage servicing rights are as follows:

December 31, (in thousands)	2015	2014
Residential mortgage loans serviced for others	\$130,816	\$138,106
Fair value of mortgage servicing rights	1,315	1,568

Changes in mortgage servicing rights are as follows:

Years ended December 31, (in thousands)	2015	2014	2013
<b>Mortgage Servicing Rights</b>			
Balance, beginning of period	\$694	\$980	\$1,075
Originated	148	17	294
Amortization (1)	(356 )	(303 )	(389 )
Balance, end of period	486	694	980
<b>Valuation Allowance</b>			
Balance, beginning of period	—	(15 )	(38 )
(Increase) decrease in impairment reserve (1)	(3 )	15	23
Balance, end of period	(3 )	—	(15 )
Mortgage servicing rights, net	\$483	\$694	\$965

(1) Amortization expense and changes in the impairment reserve are recorded in loan servicing fee income.

## NOTE 6 - PLEDGED ASSETS

The following securities and loans were pledged to secure public and trust deposits, securities sold under agreements to repurchase, FHLBB advances and credit facilities available.

Edgar Filing: SALISBURY BANCORP INC - Form 10-K

December 31, (in thousands)	2015	2014
Securities available-for-sale (at fair value)	\$67,750	\$69,055
Loans receivable	153,269	157,581
Total pledged assets	\$221,019	\$226,636

At December 31, 2015 securities were pledged as follows: \$60.4 million to secure public deposits, \$7.3 million to secure repurchase agreements and \$0.1 million to secure FHLBB and FRB advances. Additionally, loans receivable are pledged to secure FHLBB advances and credit facilities.

75



**NOTE 7 - BANK PREMISES AND EQUIPMENT**

The components of premises and equipment are as follows:

December 31, (in thousands)	2015	2014
Land	\$2,593	\$2,237
Buildings and improvements	11,514	11,070
Leasehold improvements	1,682	1,953
Capital lease	425	425
Furniture, fixtures, equipment and software	6,220	5,869
Construction in progress, including land acquisition and development	185	257
Total cost	22,619	21,811
Accumulated depreciation and amortization	(8,312 )	(7,380 )
Bank premises and equipment, net	\$14,307	\$14,431

**NOTE 8 - GOODWILL AND INTANGIBLE ASSETS**

Changes in the carrying values of goodwill and intangible assets were as follows:

Years ended December 31, (in thousands)	2015	2014	2013
Goodwill (1)			
Balance, beginning of period	\$12,552	\$9,829	\$9,829
Additions	—	2,723	—
Impairment	—	—	—
Balance, end of period	\$12,552	\$12,552	\$9,829
Core Deposit Intangibles			
Cost, beginning of period	\$5,248	\$2,543	\$2,543
Union Savings branch purchase	—	490	—
Riverside Bank merger	—	2,215	—
Impairment	—	—	—
Cost, end of period	5,248	5,248	2,543
Amortization, beginning of period	(2,258 )	(1,967 )	(1,745 )
Amortization	(652 )	(291 )	(222 )
Amortization, end of period	(2,910 )	(2,258 )	(1,967 )
Core deposit intangibles, net	\$2,338	\$2,990	\$576

(1) Not subject to amortization.

In June 2014, Salisbury acquired the Sharon, Connecticut branch office of Union Savings Bank, and assumed approximately \$18.2 million in deposits and acquired approximately \$63,000 in loans secured by deposits. Salisbury realized no goodwill and assigned a core deposit intangible of \$490,000 to the acquisition. In December 2014, Salisbury acquired Riverside Bank of Poughkeepsie, NY, which had approximately \$211.2 million in deposits and \$196.3 million in loans, and a property located at 11 Garden Street, Poughkeepsie, NY. Salisbury realized goodwill of \$2.7 million and assigned a core deposit intangible of \$2.2 million to the acquisition.

Salisbury evaluated its goodwill and intangible assets as of December 31, 2015 and 2014, and found no impairment.

The core deposit intangibles were recorded as identifiable intangible assets and are being amortized over ten years using the sum-of-the-years' digits method. Estimated annual amortization expense of core deposit intangibles is as follows:

Years ended December 31, (in thousands)	CDI amortization
---	---------------------

	\$ N01
2016	
2017	461
2018	342
2019	288
2020	234
2021	180
2022	130
2023	78
2024	24

76

## NOTE 9 - DEPOSITS

Scheduled maturities of time certificates of deposit are as follows:

Years ended December 31, (in thousands)	CD maturities
2016	\$71,932
2017	20,124
2018	10,319
2019	12,220
2020	7,900
2021	1,799
Total	\$124,294

The total amount and scheduled maturities of time certificates of deposit in denominations of \$250,000 or more were as follows:

Years ended December 31, (in thousands)	2015	2014
Within three months	\$2,520	\$2,406
After three through six months	2,624	3,568
After six through twelve months	2,929	2,900
Over one year	3,195	4,248
Total	\$11,268	\$13,122

## NOTE 10 – SECURITIES SOLD UNDER AGREEMENTS TO REPURCHASE

Salisbury enters into overnight and short-term repurchase agreements with its customers. Securities sold under repurchase agreements are as follows:

December 31, (in thousands)	2015	2014
Repurchase agreements, ending balance	\$3,914	\$4,163
Repurchase agreements, average balance during period	4,111	4,598
Book value of collateral	7,287	10,034
Market value of collateral	7,349	10,729
Weighted average rate during period	0.17 %	0.18 %
Weighted average maturity	I day	I day

## NOTE 11 – FEDERAL HOME LOAN BANK OF BOSTON ADVANCES AND OTHER BORROWED FUNDS

Federal Home Loan Bank of Boston (“FHLBB”) advances are as follows:

Years ended December 31, (dollars in thousands)	December 31, 2015			December 31, 2014		
	Total	Callable (1)	Rate (2)	Total	Callable (1)	Rate (2)
2015	\$—	\$—	— %	\$791	\$—	3.88 %
2016	21	—	5.06	15,022	15,000	4.05

Edgar Filing: SALISBURY BANCORP INC - Form 10-K

2017	—	—	—	6,000	6,000	3.99	
2018	7,000	—	3.69	7,000	—	3.69	
2019	—	—	—	—	—	—	
2020	14,337	—	2.08	—	—	—	
2021	5,621	—	2.39	—	—	—	
Total	\$26,979	\$	—	2.58%	\$28,813	\$21,000	3.95%

(1) Net of modification costs

(2) Represents the portion of advances that are callable. Callable advances are presented by scheduled maturity.

(2) Callable advances are callable quarterly or one time callable by the FHLBB.

(3) Weighted average rate based on scheduled maturity dates.

In addition to outstanding FHLBB advances, Salisbury has additional available borrowing capacity, based on current capital stock levels, of \$75.6 million and access to an unused FHLBB line of credit of \$3.5 million at December 31, 2015. Advances from the FHLBB are secured by a blanket lien on qualified collateral, consisting primarily of loans with first mortgages secured by one-to-four family properties, certain unencumbered investment securities and other qualified assets.

In accordance with ASC 470-50, two advances were modified during the third quarter 2015. The modification extended \$21 million in advances a weighted average 39 months.

The following table sets forth certain information concerning short-term FHLBB advances:

December 31, (dollars in thousands)	2015	2014
Highest month-end balance during period	\$—	\$5,545
Ending balance	—	—
Average balance during period	—	664
Weighted average rate during period	0.00 %	0.29 %

Subordinated Debentures:

In December 2015, Salisbury completed the issuance of \$10.0 million in aggregate principal amount of 6.00% Fixed to Floating Rate Subordinated Notes Due 2025 (the “Notes”) in a private placement transaction to various accredited investors including \$500 thousand to certain of Salisbury’s related parties. The Notes have a maturity date of December 15, 2025 and bear interest at an annual rate of 6.00% from and including the original issue date of the Notes to, but excluding, December 15, 2020 or the earlier redemption date payable semi-annually in arrears on June 15 and December 15 of each year. Thereafter, from and including December 15, 2020 to, but excluding, December 15, 2025, the annual interest rate will be reset quarterly and equal to the three-month LIBOR, plus 430 basis points, as described in the Notes, payable quarterly, in arrears, on March 15, June 15, September 15 and December 15 of each year during the time that the Notes remain outstanding through December 15, 2025 or earlier redemption date. The notes are redeemable, without penalty, on or after December 15, 2020 and, in certain limited circumstances, prior to that date. As more completely described in the Notes, the indebtedness evidenced by the Notes, including principal and interest, is unsecured and subordinate and junior in right of Salisbury’s payments to general and secured creditors and depositors of the Bank. The Notes also contain provisions with respect to redemption features and other matters pertaining to the Notes. The Notes have been structured to qualify as Tier 2 capital for regulatory capital purposes, subject to applicable limitations.

Subordinated debentures totaled \$9.764 million at December 31, 2015, which includes \$236 thousand of remaining unamortized debt issuance costs. The debt issuance costs are being amortized to maturity. The effective interest rate of the subordinated debentures is 6.24%.

#### NOTE 12 – NET DEFERRED TAX ASSET AND INCOME TAXES

Salisbury provides deferred taxes for the estimated future tax effects attributable to temporary differences and carry-forwards when realization is more likely than not. The components of the income tax provision were as follows:

Years ended December 31, (in thousands)	2015	2014	2013
Federal	\$2,186	\$1,057	\$940
State	432	226	103
Current provision	2,618	1,283	1,043
Federal	896	(553 )	215
State	49	(120 )	—
Change in valuation allowance	—	—	(349 )
Deferred expense (benefit)	945	(673 )	(134 )
Income tax provision	\$3,563	\$610	\$909

The following is a reconciliation of the expected federal statutory tax to the income tax provision:

Years ended December 31,	2015	2014	2013
--------------------------	------	------	------

Edgar Filing: SALISBURY BANCORP INC - Form 10-K

Income tax at statutory federal tax rate	34.00%	34.00 %	34.00 %
State tax, net of federal tax benefit	2.63	2.23	1.35
Tax exempt income and dividends received deduction	(7.38 )	(30.22)	(18.18)
Expiration of capital loss carry forward	0.00	0.00	7.00
Merger/acquisition related costs	0.00	7.77	0.00
Other	0.39	5.71	1.04
Change in valuation allowance	0.00	0.00	(7.00 )
Effective income tax rates	29.64%	19.49 %	18.21 %

78

The components of Salisbury's net deferred tax assets are as follows:

Years ended December 31, (in thousands)	2015	2014
Allowance for loan losses	\$1,877	\$1,373
Interest on non-performing loans	343	236
Accrued deferred compensation	153	301
Post-retirement benefits	17	17
Other real estate owned write-downs	—	72
Restricted stock awards	147	111
Mark-to-market purchase accounting adjustments	1,109	2,180
Write-down of securities	1,497	1,497
Alternative minimum tax	—	540
Other	22	10
Gross deferred tax assets	5,165	6,337
Deferred loan costs, net	(436 )	(538 )
Goodwill and core deposit intangible asset	(853 )	(821 )
Accelerated depreciation	(1,130)	(1,209)
Mortgage servicing rights	(177 )	(255 )
Net unrealized holding gain on available-for-sale securities	(580 )	(1,086)
Gross deferred tax liabilities	(3,176)	(3,909)
Net deferred tax asset	\$1,989	\$2,428

Salisbury will only recognize a deferred tax asset when, based upon available evidence, realization is more likely than not.

At December 31, 2012, a valuation allowance was maintained for the entire amount of the state deferred tax assets as a result of Connecticut legislation that permits banks to shelter certain mortgage income from the Connecticut corporation business tax through the use of a special purpose entity called a Passive Investment Company (“PIC”). In accordance with this legislation, in 2004, Salisbury formed a PIC, SBT Mortgage Service Corporation. Salisbury does not expect to pay state income tax in the foreseeable future unless there is a change in Connecticut law. Accordingly, Salisbury did not expect to be able to utilize the net operating losses generated by the PIC and established a valuation allowance. The capital loss carry-forwards generated by the PIC expired during 2013 and, as a result, the previously established valuation allowance was reversed.

Salisbury’s policy is to provide for uncertain tax positions and the related interest and penalties (recorded as a component of income tax expense, if any) based upon management’s assessment of whether a tax benefit is more likely than not to be sustained upon examination by tax authorities. As of December 31, 2015 and 2014, there were no material uncertain tax positions related to federal and state tax matters. Salisbury is currently open to audit under the statute of limitations by the Internal Revenue Service and state taxing authorities for the years ended December 31, 2012 through December 31, 2015.

#### NOTE 13 – SHAREHOLDERS’ EQUITY

##### Capital Requirements

Salisbury and the Bank are subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional and discretionary actions by the regulators that, if undertaken, could have a direct material effect on Salisbury’s and the Bank’s financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, Salisbury and the Bank must meet specific guidelines that involve quantitative measures of their assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting practices. Salisbury and the

Bank's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

In July 2013, the Federal Reserve Bank (FRB) approved the final rules implementing the Basel Committee on Banking Supervision's capital guidelines for bank holding companies and their bank subsidiaries. On July 9, 2013, the FDIC also approved, as an interim final rule, the regulatory capital requirements for U.S. banks, following the actions of the FRB. On April 8, 2014, the FDIC adopted as final its interim final rule, which is identical in substance to the final rules issued by the FRB in July 2013. Under the final rules, minimum requirements will increase for both the quantity and quality of capital held by the Bank and Company. The rules include a new common equity Tier 1 capital risk-weighted assets minimum ratio of 4.5%, raise the minimum ratio of Tier 1 capital to risk-weighted assets from 4.0% to 6.0%, require a minimum ratio of Total capital to risk-weighted assets of 8.0%, and require a minimum Tier 1 leverage ratio of 4.0%. A new capital conservation buffer, comprised of common equity Tier 1 capital, is also established above the regulatory minimum capital requirements. The implementation of the capital conservation buffer is being phased in effective January 1, 2016 at 0.625% of risk-weighted assets and increase each subsequent January 1, by an additional 0.625% until reaching its final level of 2.5% on January 1, 2019. Strict eligibility criteria for regulatory capital instruments were also implemented under the final rules.



Edgar Filing: SALISBURY BANCORP INC - Form 10-K

The phase-in period for the final rules began for Salisbury on January 1, 2015. As of December 31, 2015, the Company and the Bank met each of their capital requirements and the most recent notification from the FDIC categorized the Bank as “well-capitalized.” There are no conditions or events since that notification that management believes have changed the Bank’s category.

	Actual		To be Well Capitalized			
			For Capital Adequacy		Under Prompt Corrective	
(dollars in thousands)	Amount	Ratio	Purposes Amount	Ratio	Action Provisions Amount	Ratio
December 31, 2015						
Total Capital (to risk-weighted assets)						
Salisbury	\$92,030	13.51 %	\$54,509	8.0 %	n/a	—
Bank	89,249	13.10	54,504	8.0	\$68,131	10.0 %
Tier 1 Capital (to risk-weighted assets)						
Salisbury	76,120	11.17	40,878	6.0	n/a	—
Bank	83,340	12.23	40,878	6.0	54,504	8.0
Common Equity Tier 1 Capital (to risk-weighted assets)						
Salisbury	76,120	11.17	30,659	4.5	n/a	—
Bank	83,340	12.23	30,659	4.5	44,285	6.5
Tier 1 Capital (to average assets)						
Salisbury	76,120	8.56	36,102	4.0	n/a	—
Bank	83,340	9.37	35,593	4.0	44,491	5.0
December 31, 2014						
Total Capital (to risk-weighted assets)						
Salisbury	\$89,783	14.27 %	\$50,334	8.0 %	n/a	—
Bank	80,492	12.75	50,492	8.0	\$63,116	10.0 %
Tier 1 Capital (to risk-weighted assets)						
Salisbury	84,171	13.38	25,167	4.0	n/a	—
Bank	74,881	11.86	25,246	4.0	37,869	6.0
Tier 1 Capital (to average assets)						
Salisbury	84,171	12.31	27,344	4.0	n/a	—
Bank	74,881	10.95	27,345	4.0	34,181	5.0
Restrictions on Cash Dividends to Common Shareholders						

Salisbury's ability to pay cash dividends is substantially dependent on the Bank's ability to pay cash dividends to Salisbury. There are certain restrictions on the payment of cash dividends and other payments by the Bank to Salisbury. Under Connecticut law, the Bank cannot declare a cash dividend except from net profits, defined as the remainder of all earnings from current operations. The total of all cash dividends declared by the Bank in any calendar year shall not, unless specifically approved by the Banking Commissioner, exceed the total of its net profits of that year combined with its retained net profits of the preceding two years.

FRB Supervisory Letter SR 09-4, February 24, 2009, revised March 30, 2009, notes that, as a general matter, the Board of Directors of a Bank Holding Company (“BHC”) should inform the Federal Reserve and should eliminate, defer, or significantly reduce dividends if (1) net income available to shareholders for the past four quarters, net of dividends previously paid during that period, is not sufficient to fully fund the dividends; (2) the prospective rate of earnings retention is not consistent with capital needs and overall current and prospective financial condition; or (3) the BHC will not meet, or is in danger of not meeting, its minimum regulatory capital adequacy ratios. Moreover, a

BHC should inform the Federal Reserve reasonably in advance of declaring or paying a dividend that exceeds earnings for the period (e.g., quarter) for which the dividend is being paid or that could result in a material adverse change to the BHC capital structure.

#### Preferred Stock

In August 2011, Salisbury issued to the U.S. Secretary of the Treasury (the “Treasury”) \$16 million of its Series B Preferred Stock under the Small Business Lending Fund (the “SBLF”) program. The SBLF program is a \$30 billion fund established under the Small Business Jobs Act of 2010 to encourage lending to small businesses by providing Tier 1 capital to qualified community banks with assets of less than \$10 billion. The Preferred Stock qualified as Tier 1 capital for regulatory purposes and ranked senior to the Common Stock.

During fourth quarter 2015, the Company completed an offering of \$10 million of unsecured 6.00% fixed-to-floating rate subordinated notes due in 2025. The notes qualify as Tier II capital and are included as such within the Company's total risk-based capital ratio.

The net proceeds of the offering, along with cash on hand, were used during the fourth quarter 2015 to redeem the \$16 million of Senior Non-Cumulative Perpetual Preferred Stock issued in conjunction with the Company's participation in the U.S. Treasury's SBLF program.

## NOTE 14 – PENSION AND OTHER BENEFITS

Salisbury had an insured noncontributory defined benefit retirement plan which was available to employees prior to December 31, 2012 based upon age and length of service. Effective December 31, 2012, the pension plan was frozen, by amending the plan to freeze retirement benefits at current levels and discontinue future benefit accruals. The plan was terminated effective October 15, 2014. During 2012, Salisbury decided to complete its transition from providing retirement benefits under a defined benefit pension plan to a defined contribution 401(k) plan which is discussed below.

Years ended December 31, (in thousands)	2014	2013
Change in projected benefit obligation		
Benefit obligation at beginning of year	\$5,250	\$6,039
Actuarial gain	(977 )	(860 )
Service cost	—	—
Interest cost	277	255
Curtailments and settlements	—	—
Benefits paid	(4,550)	(184 )
Benefit obligation at end of year	—	5,250
Change in plan assets		
Plan assets at estimated fair value at beginning of year	6,868	6,019
Actual return on plan assets	(2,318)	1,033
Contributions by employer	—	—
Curtailments and settlements	—	—
Benefits paid	(4,550)	(184 )
Fair value of plan assets at end of year	—	6,868
Funded status and recognized asset included in other assets on the balance sheet	\$—	\$1,618

The components of amounts recognized in accumulated other comprehensive income, before tax effect, are as follows:

Years ended December 31, (in thousands)	2014	2013
Unrecognized gain (loss)	\$—	\$924
Total	\$—	\$924

The accumulated benefit obligation for the plan was \$5,250,000 at December 31, 2013. The discount rate used in determining the actuarial present value of the projected benefit obligation was 5.10% for 2013.

The components of net periodic cost are as follows:

Years ended December 31, (in thousands)	2014	2013
Service cost	\$—	\$—
Interest cost on benefit obligation	277	255
Expected return on plan assets	(297 )	(258 )
Amortization of net gain (loss)	(1 )	—
Net periodic benefit cost	(21 )	(3 )
Additional amount recognized due to settlement or curtailment	—	—
	(21 )	(3 )
Other changes in plan assets and benefit obligations recognized in other comprehensive loss (income):		
Net actuarial loss (gain)	923	(1,635)
Amortization of net gain (loss)	1	—
Total recognized in other comprehensive loss (income)	924	(1,635)

Total recognized in net periodic cost and other comprehensive loss (income)   \$903   \$(1,638)

The discount rate used to determine the net periodic benefit cost was 5.10% for 2014 and 4.35% for 2013; and the expected return on plan assets was 4.35% for 2014 and 2013.

In 2014, Salisbury terminated the Defined Benefit Pension Plan. Excess assets in the amount of \$1,018,000 were distributed to the Bank's Defined Contribution Plan (401k) and the Employee Stock Ownership Plan (ESOP) for future allocations to employees. The division of the excess pension assets was 66.67% to the 401k account (or \$679,000) and 33.33% to the ESOP account (or \$339,000).

#### 401(k) Plan

Salisbury offers a 401(k) Plan to eligible employees. Under the Plan, eligible participants may contribute a percentage of their pay subject to IRS limitations. Salisbury may make discretionary contributions to the Plan. Effective December 31, 2012, and simultaneously with the freezing of the pension plan, the 401(k) Plan was amended to include a safe harbor contribution of 4% for all qualifying employees. The Bank's safe harbor contribution percentage is reviewed annually and, under provisions of the plan, is subject to change in the future. An additional discretionary match may also be made for all employees that meet the plan's qualifying requirements for such a match. This discretionary matching percentage, if any, is also subject to review under the provisions of the plan.

Both the safe harbor and additional discretionary match, if any, vest immediately.

Salisbury's 401(k) Plan contribution expense for 2015, 2014 and 2013 was \$679,000, \$331,000 and \$657,000, respectively.

#### Employee Stock Ownership Plan (ESOP)

Salisbury offers an Employee Stock Ownership Plan (ESOP) to eligible employees. Under the Plan, Salisbury may make discretionary contributions to the Plan. Discretionary contributions vest in full upon six years and reflect the following schedule of qualified service:

20% after the second year, 20% per year thereafter, vesting at 100% after six full years of service. Benefit expenses totaled \$323,000, \$15,000, and \$160,000 in 2015, 2014, and 2013, respectively.

#### Other Retirement Plans

Salisbury adopted ASC 715-60, "Compensation - Retirement Benefits - Defined Benefit Plans - Other Postretirement" and recognized a liability for Salisbury's future postretirement benefit obligations under endorsement split-dollar life insurance arrangements. The total liability for the arrangements included in other liabilities was \$672,000 and \$581,000 at December 31, 2015, and 2014, respectively. Expense under this arrangement was \$91,000 for 2015, \$53,000 for 2014, and \$49,000 for 2013.

The Bank entered into a Supplemental Retirement Plan Agreement with its former Chief Executive Officer that provides for supplemental post retirement payments for a ten year period as described in the agreement. The related liability was \$88,000 and \$105,000 at December 31, 2015, and 2014, respectively. The related expense amounted to \$7,000, \$8,000 and \$9,000 for 2015, 2014 and 2013, respectively.

The Bank assumed a Supplemental Retirement Plan Agreement with a former Chief Executive Officer of Riverside Bank that provides for supplemental post retirement payments for a fifteen year period as described in the agreement. The related liability was \$629,000 and \$668,000 at December 31, 2015 and December 31, 2014, respectively. The related expense amounted to \$21,000 and \$2,000 for 2015 and 2014, respectively.

A Non-Qualified Deferred Compensation Plan (the "Plan") was adopted effective January 1, 2013. This Plan was adopted by the Bank for the benefit of certain key employees ("Executive" or "Executives") who have been selected and approved by the Bank to participate in this Plan and who have evidenced their participation by execution of a

Non-Qualified Deferred Compensation Plan Participation Agreement ("Participation Agreement") in a form provided by the Bank. This Plan is intended to comply with Internal Revenue Code ("Code") Section 409A and any regulatory or other guidance issued under such Section.

In 2015, 2014, and 2013, the Bank awarded six (6), seven (7) and six (6) Executives, respectively, with discretionary contributions to the plan. Expenses related to this plan amounted to \$39,000 in 2015, \$0 in 2014, and \$60,000 for 2013. In 2014, there was also a recovery of \$8,000 of prior expenses from contributions in 2013. Based on the Executive's date of retirement, the vesting schedule ranges from 7.7% per year to 50% per year.

NOTE 15 - LONG TERM INCENTIVE PLAN

The Board of Directors adopted the 2011 Long Term Incentive Plan (the “Plan”) on March 25, 2011, and the shareholders approved the Plan at the 2011 Annual Meeting. The Plan was amended on January 18, 2013 and again on January 29, 2016. The purpose of the Plan is to assist Salisbury and the Bank in attracting, motivating, retaining and rewarding employees, officers and directors by enabling such persons to acquire or increase a proprietary interest in Salisbury in order to strengthen the mutuality of interests between such persons and our shareholders, and providing such persons with stock-based long-term performance incentives to expend their maximum efforts in the creation of shareholder value.

The terms of the Plan provide for grants of Directors Stock Retainer Awards, Stock Options, Stock Appreciation Rights (“SARs”), Restricted Stock, Restricted Stock Units, Performance Awards, Deferred Stock, Dividend Equivalents, and Stock or Other Stock-Based Awards that may be settled in shares of Common Stock, cash, or other property (collectively, “Awards”).

On January 2, 2015, the Compensation Committee granted a total of 48,894 Phantom Stock Appreciation Units pursuant to the 2013 Phantom Stock Appreciation Unit and Long-Term Incentive Plan (the “Plan”), including 23,012 units to three Named Executive Officers. Mr. Cantele received 11,484 units, Mr. Davies received 5,963 units and Mr. White received 5,565 units. The units will vest on the third anniversary of the grant date.

Under the Plan, the total number of shares of Common Stock reserved and available for issuance in the ten years following adoption of the Plan in connection with Awards under the Plan is 84,000 shares of Common Stock, which represented less than 5% of Salisbury’s outstanding shares of Common Stock at the time the Plan was adopted. Shares of Common Stock with respect to Awards previously granted under the Plan that are cancelled, terminate without being exercised, expire, are forfeited or lapse will again be available for issuance as Awards. Also, shares of Common Stock subject to Awards settled in cash and shares of Common Stock that are surrendered in payment of any Award or any tax withholding requirements will again be available for issuance as Awards. No more than 30,000 shares of Common Stock may be issued pursuant to Awards in any one calendar year. In addition, the Plan limits the total number of shares of Common Stock that may be awarded as Incentive Stock Options (“ISOs”) to 42,000 and the total number of shares of Common Stock that may be issued as Directors Stock Retainer Awards to 15,000. The Directors stock retainer awards were increased from 120 shares per year to 240 shares per year effective January 25, 2013. Effective January 29, 2016, the Directors stock retainer award was increased from 240 shares to 340 shares annually.

In 2015, 2014, and 2013, there were 2,660, 2,160 and 1,330 shares issued, respectively, and the related compensation expense was \$81,000, \$65,000 and \$34,000, respectively.

The persons eligible to receive awards under the Plan are the officers, directors and employees of Salisbury and the Bank. The Plan is administered by the Human Resources and Compensation Committee (“Compensation Committee”) appointed by the Board. However, the Board may exercise any power or authority granted to the Compensation Committee. Subject to the terms of the Plan, the Compensation Committee or the Board is authorized to select eligible persons to receive Awards, determine the type and number of Awards to be granted and the number of shares of Common Stock to which Awards will relate, specify times at which Awards will be exercisable or settleable, including performance conditions that may be required as a condition thereof, set other terms and conditions of Awards, prescribe forms of Award agreements, interpret and specify rules and regulations relating to the Plan, and make all other determinations that may be necessary or advisable for the administration of the Plan.

The Compensation Committee or the Board is authorized to grant (i) stock options, including (a) ISOs which can result in potentially favorable tax treatment to the participant, and (b) non-qualified stock options, and (ii) SARs entitling the participant to receive the amount by which the fair market value of a share of Common Stock on the date of exercise exceeds the grant price of the SAR. The exercise price per share subject to an option and the grant price of

a SAR are determined by the Compensation Committee or the Board, but shall not be less than the fair market value of a share of Common Stock on the date of grant.

The Compensation Committee or the Board is authorized, subject to limitations under applicable law, to grant to participants such other Awards that are payable in, valued in whole or in part by reference to, or otherwise based on or related to, shares of Common Stock, as deemed to be consistent with the purposes of the Plan. These could include shares of Common Stock awarded purely as a “bonus” and not subject to any restrictions or conditions, other rights convertible or exchangeable into shares of Common Stock and Awards valued by reference to book value of the Common Stock or the performance of Salisbury or the Bank. The Compensation Committee or the Board may determine the terms and conditions of such Awards.



The Compensation Committee or the Board may amend, modify or terminate the Plan or the Compensation Committee's authority to grant Awards without further shareholder approval, except shareholder approval must be obtained for any amendment that would (a) materially increase the number of shares of Common Stock available under the Plan; (b) expand the types of awards under the Plan; (c) materially expand the class of persons eligible to participate in the Plan; (d) materially expand the term of the Plan; or (e) be of a nature that would require shareholder approval pursuant to any law or regulation or under the rules of the NASDAQ Capital Market.

Unless earlier terminated by the Board, the Plan will terminate on the tenth anniversary of the effective date of the Plan (March 25, 2021) or, if the shareholders approve an amendment that increases the number of shares of Common Stock subject to the Plan, the tenth anniversary of such approval. The termination of the Plan on such date will not affect the validity of any Award outstanding on the date of termination, and any such Awards will continue to be governed by the applicable terms and conditions of the Plan.

The Plan provides that award agreements for any Awards that the Committee or the Board reasonably determines to constitute a "non-qualified deferred compensation plan" subject to the requirements of Section 409A of the Internal Revenue Code of 1986, as amended (the "Code"), will be construed in a manner consistent with the requirements of Section 409A and that the Committee or the Board may amend any Award agreement (and the provisions of the Plan) if and to the extent that the Committee or the Board determines that the amendment is necessary or appropriate to comply with the requirements of Section 409A of the Code. The Plan also provides that any such Award will be subject to certain additional requirements specified in the Plan if and to the extent required to comply with Section 409A of the Code.

### **Grants of Restricted Stock and Options**

On March 27, 2015, Salisbury granted a total of 1,000 shares of restricted stock, pursuant to its 2011 Long Term Incentive Plan, to one (1) Named Executive Officer, Richard J. Cantele, Jr., President and Chief Executive Officer. The fair value of the stock as of the grant date was determined to be \$29,000 and the stock vested immediately. On January 3, 2014, Salisbury granted a total of 3,000 shares of restricted stock, pursuant to its 2011 Long Term Incentive Plan, to two (2) employees, including 2,000 shares to Donald E. White, Chief Financial Officer, and 1,000 shares to Richard P. Kelly, Executive Vice President and Chief Credit Officer. The stock will be vested three years from the grant date.

On December 5, 2014, Salisbury granted a total of 6,000 shares of restricted stock pursuant to its 2011 Long Term Incentive Plan, to three (3) employees, including 1,000 shares to Richard J. Cantele, Jr., President and Chief Executive Officer, 3,000 shares to John Davies, New York Regional President and Chief Lending Officer, and 2,000 shares to Todd Rubino, Senior Vice President and Senior Commercial Loan Officer. Of these 6,000 shares, 2,250 immediately vested and the remaining 3,750 shares vest over a period of 36 months.

On February 8, 2013, Salisbury granted a total of 19,600 shares of restricted stock pursuant to its 2011 Long Term Incentive Plan, which was approved by shareholders at the 2011 Annual Meeting, to 22 employees, including 5,000 shares to one Named Executive Officer, Richard J. Cantele, Jr., President and Chief Executive Officer. The fair value of the stock as of the grant date was determined to be \$490,000 and the stock will be vested three years from the grant date.

The remaining weighted average vesting period on restricted shares as of December 31, 2015, over which unrecognized compensation cost is expected to be recognized, is 0.5 years.

Expense in 2015, 2014, and 2013 totaled \$222,000, \$216,000 and \$142,000, respectively. Unrecognized compensation cost relating to the awards as of December 31, 2015 and 2014 totaled \$110,000 and \$313,000, respectively. Forfeitures in 2015, 2014, and 2013 totaled 300, 2,000, and 500 shares, respectively.

## NOTE 16 - RELATED PARTY TRANSACTIONS

In the normal course of business the Bank has granted loans to executive officers, directors, principal shareholders and associates of the foregoing persons considered to be related parties. Changes in loans to executive officers, directors and their related associates are as follows (there are no loans to principal shareholders):

Years ended December 31, (in thousands)	2015	2014
Balance, beginning of period	\$8,060	\$1,279
Additional related party loans acquired pursuant to Riverside Bank merger	—	6,828
Advances	5,045	271
Repayments	(4,985)	(318 )
Balance, end of period	\$8,120	\$8,060

## NOTE 17 - COMPREHENSIVE INCOME

Comprehensive income includes net income and any changes in equity from non-owner sources that are not recorded in the income statement (such as changes in net unrealized gains (losses) on securities). The purpose of reporting comprehensive income is to report a measure of all changes in shareholders' equity that result from recognized transactions and other economic events of the period other than transactions with owners in their capacity as owners. The components of comprehensive income are as follows:

Years ended December 31, (in thousands)	2015	2014	2013
Net income	\$8,457	\$2,521	\$4,083
Other comprehensive (loss) income			
Net unrealized (losses) gains on securities available-for-sale	(1,297)	2,534	(3,743)
Reclassification of net realized gains in net income <sup>(1)</sup>	(192 )	—	—
Unrealized (losses) gains on securities available-for-sale	(1,489 )	2,534	(3,743)
Income tax benefit (expense)	506	(862 )	1,273
Unrealized (losses) gains on securities available-for-sale, net of tax	(983 )	1,672	(2,470)
Pension plan (expense) income (see Note 14)	—	(924 )	1,635
Income tax benefit (expense)	—	314	(556 )
Pension plan (expense) income, net of tax	—	(610 )	1,079
Other comprehensive (loss) income, net of tax	(983 )	1,062	(1,391)
Comprehensive income	\$7,474	\$3,583	\$2,692

(1) Reclassification adjustments include realized security gains and losses. The gains and losses have been reclassified out of other comprehensive income (loss) and have affected certain lines in the consolidated statements of income as follows: the pretax amount is reflected as gain on securities, net; the tax effect is included in the income tax provision; and the after tax amount is included in net income.

The components of accumulated other comprehensive income is as follows:

December 31, (in thousands)	2015	2014
Unrealized gains on securities available-for-sale, net of tax	\$1,125	\$2,108
Accumulated other comprehensive income	\$1,125	\$2,108

## NOTE 18 - COMMITMENTS AND CONTINGENT LIABILITIES

## Commitments

The Bank has entered into an agreement pursuant to which a third party is to provide the Bank with account processing services and other miscellaneous services. Under the agreement, the Bank is obligated to pay monthly processing fees through August 5, 2016. In the event the Bank chooses to cancel the agreement prior to the end of the contract term a lump sum termination fee will have to be paid. The fee shall be calculated as the average monthly billing, exclusive of pass through costs for the past twelve months, multiplied by the number of months and any portion of a month remaining in the contract term plus the total of any promotional or monthly allowances (as applicable), or discounted monthly fees, which were provided to the Bank for the affected processing services in consideration of the fulfillment of the entire term of the affected processing services, multiplied by the number of months the Bank was awarded each of those allowance(s) for; plus one half (1/2) of any migration allowance or installation allowance, as defined in the agreement. The Bank has decided not to renew the existing agreement and will go to a month to month processing fee arrangement with the current provider until an agreement with a new provider goes into effect.

On December 31, 2015, the Bank selected a new provider for account processing services and other miscellaneous services, and will switch over to the new provider in November of 2016. The new agreement will continue until the eighth anniversary of the commencement date. According to the agreement, "Commencement Date" means the first day on which any conversion services are completed and the Bank has the capability to input transactions or data for

processing by the third party provider.

Salisbury leases facilities and equipment under operating leases that expire at various dates through 2023. The leases have varying renewal options, generally require a fixed annual rent, and provide that real estate taxes, insurance, and maintenance are to be paid by Salisbury. Rent expense totaled \$295,000, \$147,000 and \$85,000 for 2015, 2014 and 2013, respectively.

85

Future minimum lease payments at December 31, 2015 are as follows:

Future minimum lease payments (in thousands)	
2016	\$207
2017	166
2018	93
2019	79
2020	82
2021	28
2022	28
2023	16
	\$699

Salisbury leases a facility under a capital lease that expires in 2029 with an option to terminate the lease in 2018. The lease has varying renewal options, requires a fixed annual rent, and provides that real estate taxes, insurance, and maintenance are to be paid by Salisbury. The following is a schedule by years of future minimum lease payments under the capital lease with the present value of the net minimum lease payments as of December 31, 2015.

Future minimum lease payments (in thousands)	
2016	\$73
2017	73
2018	73
2019	84
2020	84
Thereafter	693
Total minimum lease payments	1,080
Less amount representing interest	658
	\$422

#### Contingent Liabilities

The Bank is involved in various claims and legal proceedings, which are not material, arising in the ordinary course of business.

As previously disclosed, the Bank, individually and in its capacity as a former Co-Trustee of the Erling C. Christophersen Revocable Trust (the "Trust"), was named as a defendant in litigation filed in the Connecticut Complex Litigation Docket in Stamford, captioned John Christophersen v. Erling Christophersen, et al., X08-CV-08-5009597S

(the “First Action”). The Bank also was a counterclaim-defendant in related mortgage foreclosure litigation in the Connecticut Complex Litigation Docket in Stamford, captioned Salisbury Bank and Trust Company v. Erling C. Christophersen, et al., X08-CV-10-6005847-S (the “Foreclosure Action,” together with the First Action, the “Actions”). The other parties to the Actions were John R. Christophersen; Erling C. Christophersen, individually and as Co-Trustee of the Trust; Bonnie Christophersen and Elena Dreiske, individually and as Co-Trustees of the Mildred B. Blount Testamentary Trust; People’s United Bank; Law Offices of Gary Oberst, P.C.; Rhoda Rudnick; and Hinckley Allen & Snyder LLP.

The Actions involved a dispute over title to certain real property located in Westport, Connecticut that was conveyed by Erling Christophersen, as grantor, to the Trust on or about August 8, 2007. Subsequent to this conveyance, the Bank loaned \$3,387,000 to the Trust, which was secured by a commercial mortgage in favor of the Bank on the Westport property. This mortgage is the subject of the Foreclosure Action brought by the Bank.

As previously disclosed, John R. Christophersen claimed an interest in the Westport real property transferred to the Trust and sought to quiet title to the property and to recover money damages from the defendants for the alleged wrongful divestiture of his claimed interest in the property.

On June 25, 2012, the Bank and John R. Christophersen entered into a Settlement Agreement, which resolved all differences between John R. Christophersen and the Bank and resulted in the withdrawal (with prejudice) of the claims made by John R. Christophersen. All claims against the Bank have been withdrawn and the Bank is no longer a defendant or counterclaim defendant in any litigation involving the Actions. As an additional consequence of the Settlement Agreement, Bonnie Christophersen, Elena Dreiske and People’s United Bank are no longer parties to any of the litigation referenced above.

On July 27, 2012, Erling Christophersen filed a Motion to Restore the First Action, and on October 15, 2012 filed a Motion to Stay the Foreclosure Action pending resolution of the Motion to Restore. The Bank opposed both motions. On February 1, 2013, the Court issued orders denying both motions. On February 14, 2013, Erling Christophersen appealed the orders denying his Motion to Restore the First Action, and Motion to Stay the Foreclosure Action.

The Appellate Court dismissed the appeal of the Foreclosure Action in May 2013, and later denied Erling Christophersen's motion for reconsideration of its decision.

The Bank proceeded in its Foreclosure Action against Erling Christophersen. Erling Christophersen asserted two special defenses and set-off claims alleging (1) that the Bank failed to defend the title claims against the properties, and (2) that the Bank took certain trustee fees without approval. The Bank moved to strike the special defenses and set off claims. In a decision issued on November 6, 2013, the Court granted the motion to strike as to the second special defense and set off, but denied the motion as to the first special defense and set off. Trial began on February 4, 2014, and concluded on February 14, 2014.

In a decision issued on June 2, 2014, the Court dismissed Erling Christophersen's special defense, and made findings as to the amount of the debt owed by Erling Christophersen and the value of the property, reserving judgment on whether to order a strict foreclosure or foreclosure by sale pending a hearing on the amount of attorneys' fees accrued, and the debt accrued since the commencement of the trial. That hearing was held on July 29, 2014. On July 25, 2014, Erling Christophersen moved to disqualify the Bank's counsel, seeking, in part, the remedy of a new trial. The Court denied that motion in a decision dated July 30, 2014. On August 5, 2014, the Court issued a Judgment of Strict Foreclosure (the "Judgment") in favor of the Bank and set September 16, 2014 as the Law Day, which is the final date fixed by the Court on which the debtor can pay off the debt or redeem the real property, with subsequent dates for subsequent encumbrances in inverse order of priority.

On September 15, 2014, Christophersen moved to open the Judgment, which motion was denied by order of the Court dated September 30, 2014. On October 3, 2014, Christophersen filed an Appeal of the Judgment and of the denial of his motion to reopen. Salisbury Bank moved to dismiss the Appeal on October 24, 2014, on grounds that Christophersen cannot represent the Trust as he is not an attorney, and that Christophersen in his individual capacity does not have any interest in this appeal. On December 17, 2014, the motion was granted in part and dismissed in part, but the decision is moot because counsel submitted an appearance on behalf of the Trust on December 29, 2014. On January 20, 2015, Christophersen filed a motion for reconsideration, which motion was denied by order of the Appellate Court on February 10, 2015.

The parties' submitted briefs and oral arguments were heard by Appellate Court on January 7, 2016. On March 1, 2016, the Appellate Court affirmed the trial court's judgment and remanded the case for the setting of new Law Days. Subsequently, the defendant filed an application for review with the Connecticut Supreme Court, which denied Mr. Christophersen's Petition For Certification on March 23, 2016. The case will be remanded to the trial court to set new law days.

There are no other material pending legal proceedings, other than ordinary routine litigation incidental to the registrant's business, to which Salisbury is a party or to which any of its property is subject.

#### NOTE 19 - FINANCIAL INSTRUMENTS

The Bank, in the normal course of business and to meet the financing needs of its customers, is a party to financial instruments with off-balance sheet risk. These financial instruments include commitments to originate loans, letters of credit, and advance funds on loans. The instruments involve, to varying degrees, elements of credit risk in excess of the amount recognized in the balance sheets. The contract amounts of those instruments reflect the extent of involvement the Bank has in particular classes of financial instruments.

The Bank's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for loan commitments and standby letters of credit is represented by the contractual amounts of those instruments. The Bank uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments.

Commitments to originate loans are agreements to lend to a customer provided there are no violations of any conditions established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments may expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Bank evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Bank upon extension of credit, is based on management's credit evaluation of the borrower. Collateral held varies, but may include secured interests in mortgages, accounts receivable, inventory, property, plant and equipment and income producing properties.



Standby letters of credit are conditional commitments issued by the Bank to guarantee the performance by a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. As of December 31, 2015 and 2014, the maximum potential amount of the Bank's obligation was \$1,401,000 and \$3,422,000, respectively, for financial, commercial and standby letters of credit. If a letter of credit is drawn upon, the Bank may seek recourse through the customer's underlying line of credit. If the customer's line of credit is also in default, the Bank may take possession of the collateral, if any, securing the line of credit.

Financial instrument liabilities with off-balance sheet credit risk are as follows:

December 31, (in thousands)	2015	2014
Residential	\$6,620	\$3,030
Home equity lines of credit	25,912	25,882
Commercial	13,922	16,751
Land	218	5
Real estate secured	46,672	45,668
Commercial and industrial	67,725	57,905
Municipal	790	—
Consumer	1,507	1,537
Unadvanced portions of loans	116,694	105,110
Commitments to originate loans	37,688	20,953
Standby letters of credit	1,401	3,422
Total	\$155,783	\$129,485

There is no material difference between the notional amounts and the estimated fair values of the off-balance sheet liabilities.

The allowance for off balance sheet commitments is calculated by applying a reserve percentage discounted by a utilization factor to the sum of unguaranteed unused lines of credit and loan contracts that the Bank has committed to but not funded as of year-end. The allowance for off-balance sheet commitments was \$93,000 and \$115,000 as of December 31, 2015 and December 31, 2014, respectively.

#### NOTE 20 - FAIR VALUE MEASUREMENTS

Salisbury uses fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. Securities available-for-sale are recorded at fair value on a recurring basis. Additionally, from time to time, other assets are recorded at fair value on a nonrecurring basis, such as loans held for sale, collateral dependent impaired loans, property acquired through foreclosure or repossession and mortgage servicing rights. These nonrecurring fair value adjustments typically involve the application of lower-of-cost-or-market accounting or write-downs of individual assets.

Salisbury adopted ASC 820-10, "Fair Value Measurement - Overall," which provides a framework for measuring fair value under generally accepted accounting principles. This guidance permitted Salisbury the irrevocable option to elect fair value for the initial and subsequent measurement for certain financial assets and liabilities on a contract-by-contract basis. Salisbury did not elect fair value treatment for any financial assets or liabilities upon adoption.

In accordance with ASC 820-10, Salisbury groups its financial assets and financial liabilities measured at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value.

GAAP specifies a hierarchy of valuation techniques based on whether the types of valuation information (“inputs”) are observable or unobservable. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect Salisbury’s market assumptions. These two types of inputs have created the following fair value hierarchy:

Level 1. Quoted prices in active markets for identical assets. Valuations for assets and liabilities traded in active exchange markets, such as the New York Stock Exchange. Level 1 also includes U.S. Treasury, other U.S. Government and agency mortgage-backed securities that are traded by dealers or brokers in active markets. Valuations are obtained from readily available pricing sources for market transactions involving identical assets or liabilities.

Level 2. Significant other observable inputs. Valuations for assets and liabilities traded in less active dealer or broker markets. Valuations are obtained from third party pricing services for identical or comparable assets or liabilities.

Level 3. Significant unobservable inputs. Valuations for assets and liabilities that are derived from other methodologies, including option pricing models, discounted cash flow models and similar techniques, are not based on market exchange, dealer, or broker traded transactions. Level 3 valuations incorporate certain assumptions and projections in determining the fair value assigned to such assets and liabilities.

A financial instrument's level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement. Salisbury did not have any significant transfers of assets between levels 1 and 2 of the fair value hierarchy during the year ended December 31, 2015.

The following is a description of valuation methodologies for assets recorded at fair value, including the general classification of such assets and liabilities pursuant to the valuation hierarchy.

**Securities available-for-sale.** Securities available-for-sale are recorded at fair value on a recurring basis. Level 1 securities include exchange-traded equity securities. Level 2 securities include debt securities with quoted prices, which are traded less frequently than exchange-traded instruments, whose value is determined using matrix pricing with inputs that are observable in the market or can be derived principally from or corroborated by observable market data. This category generally includes obligations of the U.S. Treasury and U.S. government-sponsored enterprises, mortgage-backed securities, collateralized mortgage obligations, municipal bonds, SBA bonds, corporate bonds and certain preferred equities. Level 3 is for positions that are not traded in active markets or are subject to transfer restrictions, valuations are adjusted to reflect illiquidity and/or non-transferability, and such adjustments are generally based on available market evidence. In the absence of such evidence, management's best estimate is used. Subsequent to inception, management only changes level 3 inputs and assumptions when corroborated by evidence such as transactions in similar instruments, completed or pending third-party transactions in the underlying investment or comparable entities, subsequent rounds of financing, recapitalization and other transactions across the capital structure, offerings in the equity or debt markets, and changes in financial ratios or cash flows.

Collateral dependent loans that are deemed to be impaired are valued based upon the fair value of the underlying collateral less costs to sell. Such collateral primarily consists of real estate and, to a lesser extent, other business assets. Management may adjust appraised values to reflect estimated market value declines or apply other discounts to appraised values resulting from its knowledge of the property. Internal valuations are utilized to determine the fair value of other business assets. Collateral dependent impaired loans are categorized as Level 3.

Other real estate owned acquired through foreclosure or repossession is adjusted to fair value less costs to sell upon transfer out of loans. Subsequently, it is carried at the lower of carrying value or fair value less costs to sell. Fair value is generally based upon independent market prices or appraised values of the collateral. Management adjusts appraised values to reflect estimated market value declines or apply other discounts to appraised values for unobservable factors resulting from its knowledge of the property, and such property is categorized as Level 3. Other than discussed above, the following methods and assumptions were used by management to estimate the fair value of significant classes of financial instruments for which it is practicable to estimate that value.

*Cash and cash equivalents.* Carrying value is assumed to represent fair value for cash and cash equivalents that have original maturities of ninety days or less.

*Loans held-for-sale.* The fair value is determined using a factor based on the estimated gain on sale of the loan.

*Loans, net.* The carrying value of the loans in the loan portfolio is based on their outstanding unpaid principal balances adjusted for charge-offs, the allowance for loan losses, the unamortized balance of any deferred fees or costs on originated loans and the unamortized balance of any premiums or discounts on loans purchased or acquired through mergers. The fair value of the loans is estimated by discounting future cash flows using the current interest rates at which similar loans with similar terms would be made to borrowers of similar credit quality.

*Accrued interest receivable/payable.* Carrying value approximates fair value.

*Cash surrender value of life insurance.* The carrying value of this asset approximates its fair value.

*Deposits.* The fair value of demand, non-interest bearing checking, savings and money market deposits is determined as the amount payable on demand at the reporting date. The fair value of time deposits is estimated by discounting the

estimated future cash flows using market rates offered for deposits of similar remaining maturities.

*Borrowed funds.* Advances from Federal Home Loan Bank – The fair value of these fixed-maturity advances is estimated by discounting future cash flows using rates currently offered for advances of similar remaining maturities. Subordinated Debentures – The fair value is estimated by using a discounted cash flow approach and applying discount rates currently offered on similar remaining terms and maturities.

Assets measured at fair value are as follows:

(in thousands)	Fair Value Measurements Using			Assets at
	Level 1	Level 2	Level 3	fair value
December 31, 2015				
Assets at fair value on a recurring basis				
U.S. Treasury notes	\$—	\$2,541	\$—	\$2,541
U.S. Government agency notes	—	498	—	498
Municipal bonds	—	30,385	—	30,385
Mortgage-backed securities:				
U.S. Government agencies and U.S. Government-sponsored enterprises	—	32,202	—	32,202
Collateralized mortgage obligations:				
U.S. Government agencies	—	2,014	—	2,014
Non-agency	—	4,948	—	4,948
SBA bonds	—	3,096	—	3,096
CRA mutual funds	—	764	—	764
Preferred stock	246	—	—	246
Securities available-for-sale	\$246	\$76,448	\$—	\$76,694
Assets at fair value on a non-recurring basis				
Collateral dependent impaired loans	—	—	15,211	15,211
Mortgage servicing rights	—	1,315	—	1,315
December 31, 2014				
Assets at fair value on a recurring basis				
U.S. Treasury notes	\$—	\$2,806	\$—	\$2,806
U.S. Government agency notes	—	5,874	—	5,874
Municipal bonds	—	40,352	—	40,352
Mortgage-backed securities:				
U.S. Government agencies and U.S. Government-sponsored enterprises	—	27,709	—	27,709
Collateralized mortgage obligations:				
U.S. Government agencies	—	2,679	—	2,679
Non-agency	—	6,596	—	6,596
SBA bonds	—	4,465	—	4,465
CRA mutual funds	—	504	—	504
Preferred stock	327	—	—	327
Securities available-for-sale	\$327	\$90,985	\$—	\$91,312
Assets at fair value on a non-recurring basis				
Collateral dependent impaired loans	—	—	10,463	10,463
Mortgage servicing rights	—	1,568	—	1,568
Other real estate owned	—	—	1,002	1,002

Carrying values and estimated fair values of financial instruments are as follows:

(In thousands)	Carrying value	Estimated fair value	Fair value measurements using		
			Level 1	Level 2	Level 3
<b>December 31, 2015</b>					
<b>Financial Assets</b>					
Cash and cash equivalents	\$62,118	\$62,118	\$62,118	\$—	\$—
Securities available-for-sale	76,694	76,694	246	76,448	—
Federal Home Loan Bank stock	3,176	3,176	—	3,176	—
Loans held-for-sale	763	778	—	—	778
Loans receivable, net	699,018	707,154	—	—	707,154
Accrued interest receivable	2,307	2,307	—	—	2,307
Cash surrender value of life insurance	13,685	13,685	13,685	—	—
<b>Financial Liabilities</b>					
Demand (non-interest-bearing)	\$201,340	\$201,340	\$—	\$—	\$201,340
Demand (interest-bearing)	125,465	125,465	—	—	125,465
Money market	183,783	183,783	—	—	183,783
Savings and other	119,651	119,651	—	—	119,651
Certificates of deposit	124,294	125,437	—	—	125,437
Deposits	754,533	755,676	—	—	755,676
Repurchase agreements	3,914	3,914	—	—	3,914
FHLBB advances	26,979	28,559	—	—	28,559
Subordinated debt	9,764	9,764	—	—	9,764
Note payable	376	405	—	—	405
Capital lease liability	422	870	—	—	870
Accrued interest payable	150	150	—	—	150
<b>December 31, 2014</b>					
<b>Financial Assets</b>					
Cash and cash equivalents	\$36,105	\$36,105	\$36,105	\$—	\$—
Securities available-for-sale	91,312	91,312	327	90,985	—
Federal Home Loan Bank stock	3,515	3,515	—	3,515	—
Loans held-for-sale	568	572	—	—	572
Loans receivable, net	673,330	683,845	—	—	683,845
Accrued interest receivable	2,334	2,334	—	—	2,334
Cash surrender value of life insurance	13,314	13,314	13,314	—	—
<b>Financial Liabilities</b>					
Demand (non-interest-bearing)	\$161,386	\$161,386	\$—	\$—	\$161,386
Demand (interest-bearing)	117,169	117,169	—	—	117,169
Money market	174,274	174,274	—	—	174,274
Savings and other	121,387	121,387	—	—	121,387
Certificates of deposit	141,210	142,261	—	—	142,261
Deposits	715,426	716,477	—	—	716,477
Repurchase agreements	4,163	4,163	—	—	4,163
FHLBB advances	28,813	30,626	—	—	30,626
Capital lease liability	424	929	—	—	929
Accrued interest payable	166	166	—	—	166

## NOTE 21 – SALISBURY BANCORP, INC. (PARENT ONLY) CONDENSED FINANCIAL INFORMATION

The unconsolidated balance sheets and statements of income and cash flows of Salisbury Bancorp, Inc. are presented as follows:

Balance Sheets	2015	2014
December 31, (in thousands)		
Assets		
Cash and due from banks	\$2,612	\$9,436
Investment in bank subsidiary	97,794	92,531
Other assets	5	6
Total Assets	\$100,411	\$101,973
Liabilities and Shareholders' Equity		
Subordinated debt	\$9,764	\$—
Other liabilities	73	152
Shareholders' equity	90,574	101,821
Total Liabilities and Shareholders' Equity	\$100,411	\$101,973

Statements of Income	2015	2014	2013
Years ended December 31, (in thousands)			
Dividends from subsidiary	\$2,743	\$2,143	\$2,128
Interest income	19	21	27
Interest expense	35	—	—
Expenses	511	986	394
Income before taxes and equity in undistributed net income of subsidiary	2,216	1,178	1,761
Income tax benefit	192	91	—
Income before equity in undistributed net income of subsidiary	2,408	1,269	1,761
Equity in undistributed net income of subsidiary	6,049	1,252	2,322
Net income	\$8,457	\$2,521	\$4,083

Statements of Cash Flows	2015	2014	2013
Years ended December 31, (in thousands)			
Net income	\$8,457	\$2,521	\$4,083
Adjustments to reconcile net income to net cash provided by operating activities:			
Equity in undistributed net income of subsidiary	(6,049 )	(1,252 )	(2,322 )
Other	(275 )	85	24
Net cash provided by operating activities	2,133	1,354	1,785
Investing Activities			
Investment in bank	—	(27,251)	—
Maturities (purchases) of interest-bearing time deposits of other banks	—	738	(738 )
Maturities of securities available-for-sale	—	—	—
Net cash utilized by investing activities	—	(26,513)	(738 )
Financing Activities			
Common stock dividends paid	(3,054 )	(1,918 )	(1,915 )
Preferred stock dividends paid	(158 )	(166 )	(161 )
Proceeds from issuance of subordinated debt, net of issue cost	9,764	—	—
Payment to repurchase preferred stock	(16,000)	—	—

Edgar Filing: SALISBURY BANCORP INC - Form 10-K

Proceeds from issuance of common stock	491	126	34
Issuance of Salisbury stock to Riverside shareholders	—	27,251	—
Net cash (utilized) provided by financing activities	(8,957 )	25,293	(2,042 )
(Decrease) increase in cash and cash equivalents	(6,824 )	134	(995 )
Cash and cash equivalents, beginning of period	9,436	9,302	10,297
Cash and cash equivalents, end of period	\$2,612	\$9,436	\$9,302



## NOTE 22 – EARNINGS PER SHARE

The calculation of earnings per share is as follows:

Years ended December 31, (in thousands, except per share amounts)	2015	2014	2013
Net income	\$8,457	\$2,521	\$4,083
Less: Preferred stock dividends declared	(158 )	(166 )	(161 )
Net income available to common shareholders	8,299	2,355	3,922
Less: Undistributed earnings allocated to participating securities	(72 )	(27 )	(39 )
Net income allocated to common stock	\$8,227	\$2,328	\$3,883
Weighted average common shares issued	2,730	1,785	1,710
Less: Unvested restricted stock awards	(24 )	(21 )	(19 )
Weighted average common shares outstanding used to calculate basic earnings per common share	2,706	1,764	1,691
Add: Dilutive effect of unvested restricted stock awards	17	1	—
Weighted average common shares outstanding used to calculate diluted earnings per common share	2,723	1,765	1,691
Earnings per common share (basic)	\$3.04	\$1.32	\$2.30
Earnings per common share (diluted)	\$3.02	\$1.32	\$2.30

## NOTE 23 – SUBSEQUENT EVENTS

Salisbury has evaluated subsequent events for potential recognition and/or disclosure through the date these consolidated financial statements were issued.

The Board of Directors of Salisbury declared a \$0.28 per common share quarterly cash dividend at their January 29, 2016 meeting. The dividend was paid on February 26, 2016 to shareholders of record as of February 12, 2016.

On January 29, 2016, Salisbury granted a total of 15,800 shares of restricted stock pursuant to its 2011 Long Term Incentive Plan, which was approved by shareholders at the 2011 Annual Meeting, to 42 employees, including 6,000 shares to three Named Executive Officers. Richard J. Cantele, Jr., President and Chief Executive Officer received 5,000 and John Davies, President New York Region and Chief Lending Officer and Donald E. White, Chief Financial Officer each received 500 shares. The fair value of the stock as of the grant date was determined to be \$466,000 and the stock will be vested three years from the grant date.

On January 29, 2016, the Compensation Committee granted a total of 47,470 Phantom Stock Appreciation Units pursuant to its 2011 Long Term Incentive Plan, which was approved by shareholders at the 2011 Annual Meeting, including 23,012 units to three Named Executive Officers. Richard J. Cantele, Jr., President and Chief Executive Officer received 11,484 units, John Davies, President New York Region and Chief Lending Officer received 5,963 units and Donald E. White, Chief Financial Officer received 5,565 units. The units will vest on the third anniversary of the grant date.

## NOTE 24 – SELECTED QUARTERLY CONSOLIDATED FINANCIAL DATA (Unaudited)

Selected quarterly consolidated financial data for the years ended December 31, 2015 and 2014 is as follows:

Year ended December 31, 2015 (in thousands, except ratios and per share amounts)	Q1 2015	Q2 2015	Q3 2015	Q4 2015
<b>Statement of Income</b>				
Interest and dividend income	\$8,671	\$8,545	\$8,650	\$8,705
Interest expense	745	753	753	775
Net interest and dividend income	7,926	7,792	7,897	7,930
(Benefit) provision for loan losses	(200 )	196	655	266
Gains on securities, net	175	11	6	—
Trust and Wealth Advisory	822	890	798	755
Service charges and fees	731	778	798	763
Gains on sales of mortgage loans, net	93	87	47	47
Mortgage servicing, net	(40 )	20	5	16
Other	115	114	115	166
Non-interest income	1,896	1,900	1,769	1,747
Non-interest expense	6,835	6,539	6,202	6,344
Income before income taxes	3,187	2,957	2,809	3,067
Income tax provision	953	885	824	901
Net income	2,234	2,072	1,985	2,166
Net income available to common shareholders	2,194	2,032	1,945	2,128
<b>Financial Condition</b>				
Total assets	\$865,037	\$860,794	\$904,233	\$891,192
Loans, net	676,734	677,726	687,719	699,018
Allowance for loan losses	5,182	5,059	5,659	5,716
Securities	84,694	92,932	83,886	79,870
Deposits	724,910	720,734	761,479	754,533
Repurchase agreements	3,278	2,771	4,210	3,914
FHLBB advances	28,403	28,033	26,928	26,979
Shareholders' equity	103,211	104,104	105,450	90,574
Non-performing assets	14,875	14,995	16,602	16,264
<b>Per Common Share Data</b>				
Earnings, basic	\$0.81	\$0.74	\$0.71	\$0.78
Earnings, diluted	0.80	0.74	0.71	0.77
Cash dividends declared	0.28	0.28	0.28	0.28
Cash dividends paid	0.28	0.28	0.28	0.28
Book value	31.96	32.26	32.72	33.13
Market price: (a)				
High	30.39	32.30	31.74	33.70
Low	26.08	28.80	28.38	28.80
<b>Statistical Data</b>				
Net interest margin (fully tax equivalent)	4.11	% 4.01	% 3.91	% 3.88
Efficiency ratio (fully tax equivalent)	65.45	62.91	60.40	63.64
Return on average assets	1.03	0.94	0.87	0.94
Return on average shareholders' equity	10.22	9.26	8.64	9.34
Weighted average common shares outstanding, basic	2,699	2,706	2,708	2,710
Weighted average common shares outstanding, diluted	2,716	2,724	2,724	2,727
(a)				

The above market prices reflect inter-dealer prices, without retail markup, markdown or commissions, and may not necessarily represent actual transactions.

Salisbury Bancorp, Inc.'s Common Stock, par value \$0.10 per share ("Common Stock") trades on the NASDAQ Capital Market under the symbol: SAL. As of March 1, 2016, there were approximately 2,141 shareholders of record of the Company's Common Stock.

Selected quarterly consolidated financial data (unaudited) continued:

Year ended December 31, 2014 (in thousands, except ratios and per share amounts)	Q1 2014	Q2 2014	Q3 2014	Q4 2014
<b>Statement of Income</b>				
Interest and dividend income	\$5,443	\$5,552	\$5,444	\$6,416
Interest expense	668	647	690	699
Net interest and dividend income	4,775	4,905	4,754	5,717
Provision for loan losses	337	314	318	165
Trust and Wealth Advisory	779	939	791	786
Service charges and fees	542	626	639	666
Gains on sales of mortgage loans, net	11	32	—	21
Mortgage servicing, net	27	11	41	15
Other	79	74	82	91
Non-interest income	1,438	1,682	1,553	1,579
Non-interest expense	5,110	5,068	5,108	6,852
Income before income taxes	766	1,205	881	279
Income tax provision	215	239	113	43
Net income	551	966	768	236
Net income available to common shareholders	505	926	728	196
<b>Financial Condition</b>				
Total assets	\$589,771	\$621,476	\$638,089	\$855,427
Loans, net	446,518	456,627	461,913	673,330
Allowance for loan losses	4,894	5,102	5,384	5,358
Securities	98,015	92,884	88,960	94,827
Deposits	477,512	507,361	522,294	715,426
Repurchase agreements	2,643	4,344	6,500	4,163
FHLBB advances	30,017	29,619	29,218	28,813
Shareholders' equity	74,001	75,000	75,516	101,821
Non-performing assets	8,526	8,757	8,945	10,892
<b>Per Common Share Data</b>				
Earnings, basic and diluted	\$0.29	\$0.54	\$0.43	\$0.10
Cash dividends declared	0.28	0.28	0.28	0.28
Cash dividends paid	0.28	0.28	0.28	0.28
Book value	33.90	34.44	34.74	31.54
Market price: (a)				
High	27.58	30.98	30.70	28.39
Low	25.90	27.13	26.95	25.88
<b>Statistical Data</b>				
Net interest margin (fully tax equivalent)				
Efficiency ratio (fully tax equivalent)	3.72	% 3.74	% 3.39	% 3.68
Return on average assets	77.11	72.35	75.92	77.80
Return on average shareholders' equity	0.35	0.62	0.45	0.11
Weighted average equivalent shares outstanding, basic and diluted	1,691	1,691	1,693	1,981

(a) The above market prices reflect inter-dealer prices, without retail markup, markdown or commissions, and may not necessarily represent actual transactions.

Item CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL  
9. DISCLOSURE

None.

Item 9A. CONTROLS AND PROCEDURES

Controls and Procedures

Salisbury carried out an evaluation under the supervision and with the participation of Salisbury's management, including Salisbury's principal executive officer and principal financial officer, of the effectiveness of Salisbury's disclosure controls and procedures at and for the year ended December 31, 2015. Based upon that evaluation, management, including the principal executive officer and principal financial officer, concluded that Salisbury's disclosure controls and procedures were effective as of the end of the period covered by this report and (i) designed to ensure that information required to be disclosed by Salisbury in the reports it files or submits under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the SEC's rules and forms; and (ii) accumulated and communicated to management as appropriate to allow timely decisions regarding required disclosure.

Management's Annual Report on Internal Control Over Financial Reporting

Management of Salisbury and its subsidiary are responsible for establishing and maintaining effective internal control over financial reporting. Pursuant to the rules and regulations of the SEC, internal control over financial reporting is a process designed by, or under the supervision of, Salisbury's principal executive and principal financial officers, or persons performing similar functions, and effected by Salisbury's board of directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with U.S. generally accepted accounting principles, and includes those policies and procedures that:

Pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of Salisbury;

Provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with U.S. generally accepted accounting principles and that receipts and expenditures of Salisbury are being made only in accordance with authorizations of management and directors of Salisbury; and

Provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of Salisbury's assets that could have a material effect on the financial statements.

As of December 31, 2015, management conducted an assessment of the effectiveness of the Company's internal control over financial reporting based on the framework established in Internal Control—Integrated Framework issued in 2013, by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on this assessment, management has determined that the Company's internal control over financial reporting as of December 31, 2015 was effective.

This annual report does not include an attestation report of Salisbury's registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by Salisbury's registered public accounting firm pursuant to rules of the SEC that permit Salisbury to provide only Management's Report in this annual report.

Changes in internal control over financial reporting

There were no significant changes in internal control over financial reporting during the fourth quarter of 2015 that materially affected or are reasonably likely to materially affect Salisbury's internal control over financial reporting.

Item 9B. OTHER INFORMATION

Not Applicable.

PART III

Item 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

The information required by this item will appear in Salisbury's Proxy Statement for the 2015 Annual Meeting of Shareholders, under the captions "Executive Officers;" "Directors and Nominees for Election for a Three Year Term and Director Independence" and "Corporate Governance - Meetings and Committees of the Board of Directors." Such information is incorporated herein by reference and made a part hereof.

Salisbury maintains a Code of Ethics and Conflicts of Interest Policy that applies to all of Salisbury's directors, officers and employees, including Salisbury's principal executive officer, principal financial officer and principal accounting officer. This Code of Ethics and Conflicts of Interest Policy is available upon request, without charge, by writing to Shelly L. Humeston, Secretary, Salisbury Bank and Trust Company, 5 Bissell Street, P.O. Box 1868, Lakeville, Connecticut 06039.

**Item 11. EXECUTIVE  
COMPENSATION**

The information required by this item appears in Salisbury's Proxy Statement for the 2016 Annual Meeting of Shareholders, under the captions: "Elements of Compensation" and "Executive Compensation" and "Board of Directors Compensation." Such information is incorporated herein by reference and made a part hereof.

**Item 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND  
RELATED SHAREHOLDER MATTERS**

The information required by this item appears in Salisbury's Proxy Statement for the 2016 Annual Meeting of Shareholders, under the captions "Security Ownership of Certain Beneficial Owners ("Principal Shareholders")" "Directors and Nominees for Election for a Three Year Term and Director Independence" and "Executive Compensation." Such information is incorporated herein by reference and made a part hereof.

**Item 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS AND DIRECTOR  
INDEPENDENCE**

The information required by this item appears in Salisbury's Proxy Statement for the 2016 Annual Meeting of Shareholders, under the captions "Directors and Nominees for Election for a Three Year Term and Director Independence" and "Transactions with Management and Others." Such information is incorporated herein by reference and made a part hereof.

**Item 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES**

The information required by this item appears in Salisbury's Proxy Statement for the 2016 Annual Meeting of Shareholders, under the caption "Relationship with Independent Public Accountants" and "Audit Committee Pre-Approval of Audit and Permissible Non-Audit Services of Independent Auditors." Such information is incorporated herein by reference and made a part hereof.

**PART IV**

**Item 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES**

(a)(1) Financial Statements. The Consolidated Financial Statements of Registrant and its subsidiary are included within Item 7 of Part II of this report.

(a)(2) Financial Statement schedules. All schedules for which provision is made in the applicable accounting regulations of the Securities and Exchange Commission have been omitted because they are either not applicable or the required information is included in the Consolidated Financial Statements or Notes thereto included within Item 8 of this Form 10-K.

(b) Exhibits. The following exhibits are included as part of this Form 10-K.

**Exhibit  
No. Description**

2.1 Agreement and Plan of Merger by and among Salisbury Bancorp, Inc., Salisbury Bank and Trust Company and Riverside Bank dated March 18, 2014 (incorporated by reference to Exhibit 2.1 of Form 8-K filed on March 19, 2014).

Edgar Filing: SALISBURY BANCORP INC - Form 10-K

- 3.1 Certificate of Incorporation of Salisbury Bancorp, Inc. (incorporated by reference to Exhibit 3.1 of Registrant's 1998 Registration Statement on Form S-4 filed April 23, 1998, File No.: 33-50857).
- 3.1.1 Amendment to Article Third of Certificate of Incorporation of Registrant (incorporated by reference to Exhibit 3.1 of Registrant's Form 8-K filed March 11, 2009).
- 3.1.2 Certificate of Amendment to Certificate of Incorporation of Registrant (incorporated by reference to Exhibit 3.1 of Registrant's Form 8-K filed March 19, 2009).
- 3.1.3 Certificate of Amendment to Certificate of Incorporation for the Series B Preferred Stock (incorporated by reference to Registrant's Form 8-K filed on August 25, 2011).
- 3.1.4 Certificate of Amendment to Certificate of Incorporation of Registrant (incorporated by reference to Exhibit 3.1 of Registrant's Form 8-K filed October 30, 2014).

97



- 3.2 Amended and Restated Bylaws (incorporated by reference to Exhibit 3.1 of Form 8-K filed November 25, 2014).
- 4.1 Warrant to purchase Common Stock dated March 13, 2009. (incorporated by reference to Exhibit 4.1 of Registrant's 2010 Annual Report on Form 10-K filed March 31, 2011). (Such Warrant was repurchased by Salisbury on November 2, 2011 and simultaneously cancelled. See Exhibit 10.8 below).
- 4.2 Form of Subordinated Note, dated as of December 10, 2015, issued by Salisbury Bancorp, Inc. (incorporated by reference to Exhibit 4.1 of Registrant's Form 8-K filed December 10, 2015).
- 10.1 Consulting and Non-Compete Agreement dated June 1, 2009 by and between Salisbury and John F. Perotti. (incorporated by reference to Exhibit 10.2 of Registrant's 2010 Annual Report on Form 10-K filed March 31, 2011).
- 10.2 2001 Director's Stock Retainer Plan (incorporated by reference to Exhibit 10.1 of Registrant's 2001 Annual Report on Form 10-KSB/A filed May 8, 2002). (Such Plan expired in 2011 and was replaced by the 2011 Long Term Incentive Plan. See Exhibit 10.9 below).
- 10.3 Securities Purchase Agreement dated August 25, 2011 with the U.S. Treasury Department relating to the Small Business Lending Fund (incorporated by reference to Exhibit 10.1 of Registrant's Form 8-K filed on August 25, 2011).
- 10.4 2011 Long Term Incentive Plan adopted by the Board on March 25, 2011 and approved by the shareholders at Salisbury's 2011 Annual Meeting of Shareholders (incorporated by reference to Exhibit 10.9 of Registrant's Annual Report on Form 10-K filed March 19, 2012).
- 10.5 Amendment Number One to 2011 Long Term Incentive Plan dated as of January 18, 2013 (incorporated by reference to Exhibit 10.10 of Registrant's Annual Report on Form 10-K filed March 7, 2013).
- 10.6 Severance Agreement between Salisbury Bank and Trust and Mr. Richard J. Cantele, Jr. effective as of January 1, 2013 (incorporated by reference to Exhibit 10.1 of Registrant's Form 8-K filed February 15, 2013).
- 10.7 Non-qualified Deferred Compensation Plan effective as of January 1, 2013 (incorporated by reference to Exhibit 10.2 of Registrant's Form 8-K filed February 15, 2013).
- 10.8 Change in Control Agreement with Donald E. White dated April 1, 2013 (incorporated by reference to Exhibit 10.3 of Form 10-Q filed May 14, 2013).
- 10.9 Employee Stock Ownership Plan (incorporated by reference to Exhibit 10.14 of Form 10-K filed March 28, 2014).
- 10.10 Salisbury Bancorp, Inc. 2015 Phantom Stock Appreciation Unit and Long-Term Incentive Plan (incorporated by reference to Exhibit 10.1 of Form 8-K filed January 2, 2015).
- 10.11 Amendment Number One to Salisbury Bancorp, Inc. 2015 Phantom Stock Appreciation Unit and Long-Term Incentive Plan (incorporated by reference to Exhibit 10.1 of Form 8-K filed January 30, 2015).
- 10.12 Amendment Number Two to 2011 Long Term Incentive Plan dated as of January 29, 2016.
- 10.13 Form of Split-dollar Life Insurance Agreements with Senior Executive Officers.
- 10.14 Employment Agreement with John M. Davies.
- 10.15 Form of Subordinated Note Purchase Agreement, dated as of December 10, 2015, between Salisbury Bancorp, Inc. and the Purchasers identified therein. (incorporated by reference to Exhibit 10.1 of Registrant's Form 8-K filed December 10, 2015).
- 21.1 Subsidiaries of the Registrant.
- 23.1 Consent of Baker Newman & Noyes, LLC.
- 23.2 Consent of Shatswell, MacLeod & Company, P.C.
- 31.1 Chief Executive Officer Certification Pursuant to 17 CFR 240.13a-14, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Chief Financial Officer Certification Pursuant to 17 CF 240.13a-14, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Chief Executive Officer and Chief Financial Officer Certification Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

(c) Financial Statement Schedules

No financial statement schedules are required to be filed as Exhibits pursuant to Item 15(c).

**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

SALISBURY BANCORP, INC.

/s/ Richard J. Cantele, Jr.  
Richard J. Cantele, Jr.  
President and Chief Executive Officer  
March 30, 2016

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

*/s/ Louis E. Allyn, II*  
Louis E. Allyn, II  
Director  
March 30, 2016

*/s/ Michael D. Gordon*  
Michael D. Gordon  
Director  
March 30, 2016

*/s/ Charles M. Andola*  
Charles M. Andola  
Director  
March 30, 2016

*/s/ Polly Diane Hoe*  
Polly Diane Hoe  
Director  
March 30, 2016

*/s/ George E. Banta*  
George E. Banta  
Director  
March 30, 2016

*/s/ Nancy F. Humphreys*  
Nancy F. Humphreys  
Director  
March 30, 2016

*/s/ Arthur J. Bassin*  
Arthur J. Bassin  
Director  
March 30, 2016

*/s/ Holly J. Nelson*  
Holly J. Nelson  
Director  
March 30, 2016

*/s/ Louise F. Brown*  
Louise F. Brown  
Director  
March 30, 2016

*/s/ John F. Perotti*  
John F. Perotti  
Director  
March 30, 2016

*/s/ Richard J. Cantele, Jr.*  
Richard J. Cantele, Jr.  
Director, President and Chief Executive Officer  
March 30, 2016

*/s/ Rudolph P. Russo*  
Rudolph P. Russo  
Director  
March 30, 2016

/s/ Robert S. Drucker  
Robert S. Drucker  
Director  
March 30, 2016

/s/ Michael A. Varet  
Michael A. Varet  
Director, Chairman of the Board  
March 30, 2016

/s/ David B. Farrell  
David B. Farrell  
Director  
March 30, 2016

/s/ Donald E. White  
Donald E. White  
Chief Financial Officer  
and Chief Accounting Officer  
March 30, 2016