Community Partners Bancorp
Form 10-K
March 29, 2013

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-K

(Mark One)
x ANNUAL REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2012

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

For the transition period from ________ to _______

Commission file number: 000-51889

COMMUNITY PARTNERS BANCORP
(Exact Name of Registrant as Specified in Its Charter)

New Jersey (State or Other Jurisdiction of Incorporation or Organization)	20-3700861 (I.R.S. Employer Identification Number)

766 Shrewsbury Avenue, Tinton Falls, New Jersey 07724
(Address of Principal Executive Offices, including Zip Code)

(732) 389-8722
(Registrant's telephone number, including area code)

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

Title of each class	Name of each exchange on which registered
Common Stock, no par value	The NASDAQ Stock Market LLC

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

Preferred Stock Purchase Rights
(Title of Class)

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

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

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

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 x No o

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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 amendment to this Form 10-K. x

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

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

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

The aggregate market value of the registrant's voting and non-voting common equity held by non-affiliates of the registrant, computed by reference to the price at which the common stock was last sold, or the average bid and asked price of such common equity, as of the last business day of the registrant's most recently completed second fiscal quarter, is $40,220,716.

As of March 15, 2013, 8,017,175 shares of the registrant's common stock were outstanding.

Documents incorporated by reference

Portions of the registrant's definitive Proxy Statement for its 2013 Annual Meeting of Shareholders are incorporated by reference into Part III of this report and will be filed within 120 days of December 31, 2012.

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PART I

Forward-Looking Statements

When used in this and in future filings by us with the Securities and Exchange Commission (the "SEC"), in our press releases and in oral statements made with the approval of one of our authorized executive officers, the words or phrases "will," "will likely result," "could," "anticipates," "believes," "continues," "expects," "plans," "will continue," "is "estimated," "project" or "outlook" or similar expressions (including confirmations by one of our authorized executive officers of any such expressions made by a third party with respect to us) are intended to identify statements constituting "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934 and that are intended to come within the safe harbor protection provided by these sections. We wish to caution readers not to place undue reliance on any such forward-looking statements, each of which speaks only as of the date made, even if subsequently made available on our website or otherwise. Such statements are subject to certain risks and uncertainties, many of which are beyond our control, that could cause actual results to differ materially from historical earnings and those presently anticipated or projected. The forward-looking statements are and will be based on management's then-current views and assumptions regarding future events and operating performance, and are applicable only as of the dates of such statements.

Factors that may cause actual results to differ from those results expressed or implied, include, but are not limited to, those listed in this report under the heading "Risk Factors"; the ability of customers to repay their obligations; the adequacy of the allowance for loan losses; developments in the financial services industry and U.S. and global credit markets; changes in the direction of the economy nationally or in New Jersey; changes in interest rates; competition; loss of management and key personnel; government regulation; environmental liability; failure to implement new technologies in our operations; changes in our liquidity; changes in our funding sources; failure of our controls and procedures; disruptions of our operational systems and relationships with vendors; and our success in managing risks involved in the foregoing. Although management has taken certain steps to mitigate any negative effect of the aforementioned items, significant unfavorable changes could severely impact the assumptions used and have an adverse effect on profitability. Such risks and other aspects of our business and operations are described in Item 1. "Business", Item 1A. "Risk Factors" and Item 7. "Management's Discussion and Analysis of Financial Condition and Results of Operations" of this report. We have no obligation to publicly release the result of any revisions which may be made to any forward-looking statements to reflect anticipated or unanticipated events or circumstances occurring after the date of such statements.

Item 1. Business.

The disclosures set forth in this item are qualified by Item 1A. "Risk Factors", Item 7. "Management's Discussion and Analysis of Financial Condition and Results of Operations" and other statements set forth in this report.

Community Partners Bancorp

Community Partners Bancorp, which we refer to herein as "Community Partners," the "Company," "we," "us" and "our," i business corporation organized under the laws of the State of New Jersey in August 2005. The principal place of business of Community Partners is located at 766 Shrewsbury Avenue, Tinton Falls, New Jersey 07724 and its telephone number is (732) 389-8722.

Effective December 31, 2008, Community Partners consolidated its two wholly owned bank subsidiaries, The Town Bank ("Town Bank"), based in Westfield, New Jersey, and Two River Community Bank ("Two River" or the "Bank"), based in Middletown, New Jersey. The two banks had been under common ownership since Community Partners was organized to acquire them, in a transaction that took place in April 2006. The consolidation of Town Bank into Two

River streamlined operations and created administrative efficiencies and reductions in overhead costs. As a result, there is now only one New Jersey state-chartered commercial bank, Two River. The Town Bank branches had used the Town Bank name and had operated as a division of Two River Community Bank up until May 2009, when the Town Bank branches began operation under the Two River Community Bank title. The entire branch network comprises 16 branches in Monmouth and Union counties, New Jersey.

In early October 2012, the Company relocated and consolidated its executive offices and all bank-related departments into a new corporate headquarters located in Tinton Falls, New Jersey.

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Other than its investment in the Bank, Community Partners currently conducts no other significant business activities. Community Partners may determine to operate its own business or acquire other commercial banks, thrift institutions or bank holding companies, or engage in or acquire such other activities or businesses as may be permitted by applicable law, although it has no present plans or intentions to do so. When we refer to the business conducted by Community Partners in this document, including any lending or other banking activities, we are referring to the business that Community Partners conducts through the Bank.

As of December 31, 2012, the Company had consolidated assets of $733.9 million, total deposits of $606.8 million and shareholders' equity of $92.0 million.

Employees

As of December 31, 2012, the Company and its subsidiaries had 137 full-time equivalent employees, of whom 134 were full-time and 7 were part-time. None of the Company's employees are represented by a union or covered by a collective bargaining agreement. Management of the Company and the Bank believe that, in general, their employee relations are good.

Two River Community Bank

Two River Community Bank was organized in January 2000 as a New Jersey state-chartered commercial bank to engage in the business of commercial and retail banking. As a community bank, the Bank offers a wide range of banking services including demand, savings and time deposits and commercial and consumer/installment loans to small and medium-sized businesses, not-for-profit organizations, professionals and individuals primarily in Monmouth, Middlesex and Union counties, New Jersey. The Bank also offers its customers numerous banking products such as safe deposit boxes, night depository, wire transfers, money orders, travelers checks, automated teller machines, direct deposit, telephone and internet banking and corporate business services. The Bank currently operates 16 banking offices in Monmouth and Union counties, New Jersey and a corporate headquarters building. The Bank's corporate headquarters is located at 766 Shrewsbury Avenue, Tinton Falls, New Jersey, while its principal banking office is located at 1250 Highway 35 South, Middletown, New Jersey. Other banking offices are located in Allaire, Atlantic Highlands, Cliffwood, Manasquan, Navesink, Port Monmouth, Red Bank (2), Tinton Falls (2), West Long Branch, Westfield (2), Cranford and Fanwood, New Jersey. The Bank also operates two regional lending offices in New Brunswick and Summit, New Jersey, for the purpose of expanding our presence in these communities.

We believe that the Bank's customers still want to do business and have a relationship with their banker. To accomplish this objective, we emphasize to our employees the importance of delivering exemplary customer service and seeking out opportunities to build further relationships with the Bank's customers. The Bank's deposits are insured by the Federal Deposit Insurance Corporation ("FDIC") up to the statutory limits.

Competition

The Bank faces substantial competition for deposits and creditworthy borrowers. It competes with New Jersey and regionally based commercial banks, savings banks and savings and loan associations, as well as national financial institutions, most of which have assets, capital and lending limits greater in amount than that of the Bank. Other competitors include money market mutual funds, mortgage bankers, insurance companies, stock brokerage firms, regulated small loan companies, credit unions and issuers of commercial paper and other securities.

Products and Services

The Bank offers a full range of banking services to our customers. These services include a wide variety of business and consumer lending products as well as corporate services for businesses and professionals. We offer a range of deposit products including checking, savings and money market accounts plus certificates of deposit ("CD"). The Bank also participates in the Certificate of Deposit Account Registry Service ("CDARS"), a service that enables us to provide our customers with additional FDIC insurance on CD products. Other products and services include remote deposit capture, safe deposit boxes, ACH services, debit and ATM cards, gift cards, traveler's checks, money orders, direct deposit and coin counting. We also offer customers the convenience of a full complement of telephone and internet banking services that allows them to check account balances, receive email alerts, transfer funds, initiate stop payment requests, re-order checks and pay bills. The Bank invested in several additional technology solutions for our customers in 2011, including an enhanced internet banking system that allows transfers between accounts outside of the Bank and a mobile banking solution that permits customers to view accounts, set up alerts and transfer funds within their accounts. In 2012, we have installed "smart" ATM's that accept deposits without envelopes, and added the ability to open deposit accounts online. We will continue to look for solutions and enhancements that will provide additional convenience for our customers.

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Lending Activities

The Bank engages in a variety of lending activities, which are primarily categorized as either commercial, real estate or consumer lending. The strategy is to focus our lending activities on small and medium-sized business customers and retain customers by offering them a wide range of products and personalized service. Commercial and real estate mortgage lending (consisting of commercial real estate, commercial business, construction and other commercial lending, including medical lending and private banking) are currently our main lending focus. Loans are funded primarily from deposits, although we do occasionally borrow to fund loan growth or meet deposit outflows.

The Bank presently generates virtually all of our loans from borrowers located in the State of New Jersey, with a significant portion in Union and Monmouth counties. Loans are generated through marketing efforts, the Bank's present base of customers, walk-in customers, referrals, the directors and members of the Bank's advisory boards. The Bank strives to maintain a high overall credit quality through the establishment of and adherence to prudent lending policies and practices. The Bank has an established written loan policy that has been adopted by the Board of Directors, which is reviewed at least annually. Any loans to members of the Board of Directors or their affiliates must be reviewed and approved by the Bank's Board of Directors in accordance with the loan policy as well as applicable state and federal banking laws. In accordance with our loan policy, approvals of affiliated transactions are made only by independent board members.

In managing the growth and quality of the Bank's loan portfolio, we have focused on: (i) the application of prudent underwriting criteria; (ii) the active involvement by senior management and the Bank's Board of Directors in the loan approval process; (iii) the active monitoring of loans to ensure timely repayment and early detection of potential problems; and (iv) a loan review process by an independent loan review firm, which conducts in-depth reviews of portions of the loan portfolio on a quarterly basis.

Our principal earning assets are loans originated or participated in by the Bank. The risk that certain borrowers will not be able to repay their loans under the existing terms of the loan agreement is inherent in the lending function. Risk elements in a loan portfolio include non-accrual loans (as defined below), past due and restructured loans, potential problem loans, loan concentrations (by industry or geographically) and other real estate owned acquired through foreclosure or a deed in lieu of foreclosure. Because the vast majority of the loans are made to borrowers located in Union and Monmouth counties, New Jersey, each loan or group of loans presents a geographical and credit risk based upon the condition of the local economy. The local economy is influenced by conditions such as housing prices, employment conditions and changes in interest rates.

Construction Loans

We originate fixed-rate and adjustable-rate loans to individuals and builders to finance the construction of residential dwellings. We also originate construction loans for commercial development projects, including multifamily buildings, restaurants, shopping centers and owner-occupied properties used for businesses. Within these project types, the Bank also offers land development loans. Our construction loans generally provide for the payment of interest only during the construction phase which is usually twelve months for residential owner occupied properties and twelve to eighteen months for commercial properties and upwards to 36 months for land development projects, depending on the size and scope of the project. At the end of the commercial or residential construction phase, the loan can either convert to a permanent loan or is paid in full. Before making a commitment to fund a construction loan, we require an appraisal of the property by a bank approved independent licensed appraiser, appropriate environmental due diligence, a construction cost review, an inspection of the property before disbursement of funds during the stages of the construction process, and pre-qualification from an identified source for the permanent takeout.

Construction financing is generally considered to involve a higher degree of risk of loss than long-term financing on improved, occupied real estate. Risk of loss on a construction loan depends largely upon the accuracy of the initial estimate of the property's value at completion of construction and the estimated cost (including interest) of construction. During the construction phase, a number of factors could result in delays and cost overruns. If the estimate of construction costs proves to be inaccurate, we may be required to advance funds beyond the amount originally committed to permit completion of the building. If the estimate of value proves to be inaccurate, we may be confronted, at or before the maturity of the loan, with a building having a value which is insufficient to assure full repayment. If we are forced to foreclose on a building before or at completion due to a default, there can be no assurance that we will be able to recover all of the unpaid balance of, and accrued interest on, the loan as well as related foreclosure and holding costs.

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Commercial and Industrial and Commercial Real Estate Loans

The Bank originates commercial and industrial loans for business purposes to sole proprietorships, partnerships, corporations and small businesses in our lending market areas. We extend commercial business loans on a secured and unsecured basis. Secured commercial loans are generally collateralized by residential and nonresidential real estate, marketable securities, accounts receivable, inventory, industrial/commercial machinery and equipment, and furniture and fixtures. To further enhance our security position, we typically require personal guarantees of the principal owners of the entities to which we extend credit. These loans are made on both lines of credit and fixed-term basis ranging from one to five years in duration. When making commercial business loans, we consider the financial statements and/or tax returns of the borrower, the borrower's payment history along with the principal owners' payment history, the debt service capabilities of the borrower, the projected cash flows of the business, the value of the collateral and the financial strength of the guarantor.

Commercial real estate loans are made to local commercial, retail and professional firms and individuals for the acquisition of new property or the refinancing of existing property. These loans are typically related to commercial businesses and secured by the underlying real estate used in these businesses or real property of the principals. These loans are generally offered on a fixed or variable rate basis, subject to rate re-adjustments every five years and amortization schedules ranging from 5 to 25 years.

Our established written underwriting guidelines for commercial loans are periodically reviewed and enhanced as needed. Pursuant to these guidelines, in granting commercial loans, we look primarily to the borrower's cash flow as the principal source of loan repayment. To monitor cash flows on income properties, we require borrowers and loan guarantors of loan relationships to provide annual financial statements, rent rolls and/or tax returns. Collateral and personal guarantees of the principals of the entities to which we lend are consistent with the requirements of our loan policy.

Commercial loans are often larger and may involve greater risks than other types of lending. Because payments of such loans are often dependent on the successful operation of the business involved, repayment of such loans may be more sensitive than other types of loans and are subject to adverse conditions in the real estate market, or the general economy. We are also involved with off-balance sheet financial instruments, which include collateralized commercial and standby letters of credit. We seek to minimize these risks through our underwriting guidelines and prudent risk management techniques. Any collateral securing such loans may depreciate over time, may be difficult to appraise and may fluctuate in value. Environmental surveys and inspections are obtained when circumstances suggest the possible presence of hazardous materials. There can be no assurances, however, of success in the efforts to minimize these risks.

Unlike residential mortgage loans, which generally are made on the basis of the borrower's ability to make repayment from his or her employment or other income and which are secured by real property the value of which tends to be more easily ascertainable, commercial loans are of higher risk and typically are made on the basis of the borrower's ability to make repayment from the cash flow of the borrower's business operation. As a result, the availability of funds for the repayment of commercial loans may depend substantially on the success of the business itself as the primary source of repayment. Further, any collateral securing such loans may depreciate over time, may be difficult to appraise and may fluctuate in value.

Residential Real Estate Loans

We offer a full range of residential real estate loans. We do not originate subprime or negative amortization loans. Each residential mortgage loan is evidenced by a promissory note secured by a mortgage or deed of trust creating a first lien on one-to-four family residential property. Residential real estate properties underlying residential mortgage loans consist of single-family detached units, individual condominium units, two-to-four family dwelling units and townhouses.

Consumer Loans

The Bank offers consumer loans that are extended to individuals for personal or household purposes. These loans consist of home equity lines of credit, home equity loans, personal loans, automobile loans and overdraft protection.

Our home equity revolving lines of credit come with a floating interest rate tied to the prime rate. Lines of credit are available to qualified applicants in amounts up to $350,000 for up to 15 years. We also offer fixed rate home equity loans in amounts up to $350,000 for a term of up to 15 years. Credit is based on the income and cash flow of the individual borrowers, properly margined real estate collateral supporting the mortgage debt and past credit history.

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Consumer loans may entail greater risk than do residential mortgage loans, particularly in the case of consumer loans that are unsecured or secured by assets that depreciate rapidly. In such cases, repossessed collateral for a defaulted consumer loan may not provide an adequate source of repayment for the outstanding loan and the remaining deficiency often does not warrant further substantial collection efforts against the borrower. In addition, consumer loan collections depend on the borrower's continuing financial stability, and therefore are more likely to be adversely affected by job loss, divorce, illness or personal bankruptcy. Furthermore, the application of various federal and state laws, including bankruptcy and insolvency laws, may limit the amount that can be recovered on such loans.

Participation Loans

The Bank underwrites all loan participations in accordance with our underwriting standards. We will not participate in a loan transaction unless each participant has a substantial interest in the loan relationship. In addition, we also consider the financial strength and reputation of the lead lender. To monitor cash flows on loan participations, we look for the lead lender to provide at a minimum, tax returns and annual financial statements for the borrower. Generally, we also conduct an annual internal loan review for participations.

Small Business Administration ("SBA") Loans

In June 2010, the Bank announced the formation of the SBA Lending Division, which is consistent with the Bank's mandate of community lending in Monmouth, Middlesex and Union counties, New Jersey. During the fourth quarter of 2011, the Bank achieved Preferred Lending status, which allows us to have delegated authority to approve and close SBA loans up to $5.0 million. Our risk philosophy in SBA lending is an extension of our existing credit culture and focused on the cash flow of the businesses while maintaining our commitment to providing small and mid-sized companies access to the credit they need to expand and hire. The Bank participates in SBA's 7(a), including 7(a) sub-program such as SBA Express, and 504 loan programs. The 7(a) program typically provides guarantees ranging from 50% to 85%. The 504 program provides fixed rate financing with a first lien position for a conventional loan followed by a SBA debenture loan in a subordinated position. The 504 program is administered through SBA's Certified Development Companies ("CDCs"). A typical 504 structure transaction is broken down by a 10% equity injection by the borrower, a 40% SBA debenture and a 50% conventional mortgage.

Asset Quality

We believe that strong asset quality is a key to long-term financial success. We have sought to grow and diversify the loan portfolio, while maintaining a high level of asset quality and moderate credit risk, using underwriting standards that we believe are conservative and diligent monitoring and collection efforts. As we continue to grow and leverage our capital, we envision that loans will continue to be our principal earning assets. An inherent risk in lending is the borrower's ability to repay the loan under its existing terms. Risk elements in a loan portfolio include non-accrual loans (as defined below), past due and restructured loans, potential problem loans, loan concentrations (by industry or geographically) and other real estate owned acquired through foreclosure or a deed in lieu of foreclosure.

Non-performing assets include loans that are not accruing interest (non-accrual loans) as a result of principal or interest being in default for a period of 90 days or more, loans past due 90 days or more and still accruing and other real estate owned, which consists of real estate acquired as the result of a defaulted loan. When a loan is classified as non-accrual, interest accruals cease and all past due interest is reversed and charged against current income. Until the loan becomes current as to principal or interest, as applicable, any payments received from the borrower are applied to outstanding principal and fees and costs to the Bank, unless we determine that the financial condition of the borrower and other factors merit recognition of such payments as interest. During 2011, the Bank adopted Financial Accounting Standards Board ("FASB") guidance on determination of whether a restructuring is a troubled debt restructuring ("TDR"). The guidance was applicable to restructurings on or after January 1, 2011. A TDR is a loan in which the contractual terms have been modified resulting in the Bank granting a concession to a borrower who is experiencing financial difficulties in order for the Bank to have a greater opportunity of collecting the indebtedness from the borrower. Non-accruing TDR’s are included in non-performing loans. Non-performing assets are further discussed within the “Asset Quality” section under Item 7 of this report.

We utilize a risk system, as described below under the section titled “Allowance for Loan Losses”, as an analytical tool to assess risk and set appropriate reserves. In addition, the FDIC has a classification system for problem loans and other lower quality assets, classifying them as “substandard,” “doubtful” or “loss.” A loan is classified as “substandard” when it is inadequately protected by the current value and paying capacity of the obligor or the collateral pledged, if any. Loans with this classification have a well-defined weakness or a weakness that jeopardizes the liquidation of the debt. They are characterized by the distinct possibility that some loss may occur if the deficiencies are not corrected. A loan is classified “doubtful” when it has all the weaknesses inherent in a loan classified as substandard with the added characteristics that the weaknesses make collection or liquidation in full, on the basis of currently existing factors, conditions, and values, highly questionable and improbable. A loan is classified as “loss” when it is considered uncollectible and such little value that the loan’s continuance as an asset on the balance sheet is not warranted.

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In addition to categories for non-accrual loans and loans past due 90 days or more that are still accruing interest, we maintain a "watch list" of performing loans where management has identified conditions which potentially could cause such loans to be downgraded into higher risk categories in future periods. Loans on this list are subject to heightened scrutiny and more frequent review by management. See Note 1-H in the Notes to Consolidated Financial Statements for more information.

Allowance for Loan Losses

We maintain an allowance for loan losses at a level that we believe is adequate to provide for probable losses inherent in the loan portfolio. Loan losses are charged directly to the allowance when they occur and any recovery is credited to the allowance when realized. Risks from the loan portfolio are analyzed on a continuous basis by the Bank's senior management, outside independent loan review auditors, the directors' loan committee, and the Board of Directors.

The level of the allowance is determined by assigning specific reserves to impaired loans and general reserves on all other loans. The portion of the allowance that is allocated to impaired loans is determined by estimating the inherent loss on each credit after giving consideration to the value of the underlying collateral. A risk system, consisting of multiple grading categories, is utilized as an analytical tool to assess risk and set appropriate general reserves. Along with the risk system, senior management evaluates risk characteristics of the loan portfolio under current and anticipated economic conditions and considers such factors as the financial condition of the borrower, past and expected loss experience, and other factors management feels deserve recognition in establishing an appropriate reserve. These estimates are reviewed at least quarterly, and as adjustments become necessary, they are realized in the periods in which they become known. Additions to the allowance are made by provisions charged to expense and the allowance is reduced by net charge-offs (i.e., loans judged to be uncollectible and charged against the reserve, less any recoveries on such loans).

Although management attempts to maintain the allowance at a level deemed adequate to cover any losses, future additions to the allowance may be necessary based upon any changes in market conditions, either generally or specific to our area, or changes in the circumstances of particular borrowers. In addition, various regulatory agencies periodically review our allowance for loan losses, and may require us to take additional provisions based on their judgments about information available to them at the time of their examination. See Note 1-I in the Notes to Consolidated Financial Statements for more information.

Risk Management

Managing risk is an essential part of a successful financial institution. Our most prominent risk exposures are credit risk, interest rate risk and market risk. Credit risk is the risk of not collecting the interest and/or the principal balance of a loan or investment when it is due. Interest rate risk is the potential reduction of net interest income as a result of changes in interest rates. Market risk arises from fluctuations in interest rates that may result in changes in the values of financial instruments, such as available for sale securities that are accounted for on a fair value basis. Other risks that we face are operational risks, liquidity risks and reputation risk. Operational risks include risks related to fraud, regulatory compliance, processing errors, and technology and disaster recovery. Liquidity risk is the possible inability to fund obligations to depositors or borrowers. Reputation risk is the risk that negative publicity or press, whether true or not, could cause a decline in our customer base or revenue.

The management of and authority to assume interest rate risk is the responsibility of the Asset/Liability Committee ("ALCO"), which is comprised of senior management and board members. The primary objective of Asset/Liability management is to establish prudent risk management guidelines and to coordinate balance sheet composition with interest rate risk management to sustain a reasonable and stable net interest income throughout various interest rate cycles. We have policies and practices for measuring and reporting interest rate risk exposure, through analysis of the net interest margin, gap position, simulation testing, liquidity ratios and the Economic Value of Portfolio Equity. In addition, we annually review our interest rate risk policy, which includes limits on the impact to earnings from shifts in interest rates.

Credit Risk Management

Our strategy for credit risk management focuses on having well-defined credit policies and uniform underwriting criteria and providing prompt attention to potential problem loans. The Bank internally conducts semi-annual commercial real estate stress testing. To further enhance our credit risk management strategy, we engage a third party loan review firm to provide additional portfolio surveillance. When a borrower fails to make a required loan payment, we take a number of steps to attempt to have the borrower cure the delinquency and restore the loan to current status. When the loan becomes 15 days past due, a late charge notice is generated and sent to the borrower and a representative of the Bank attempts to communicate by phone with the borrower to discuss the late payment. If payment is not then received by the 30th day of delinquency, a further notification is sent to the borrower. If no resolution can be achieved, after a loan becomes 90 days delinquent, we may commence foreclosure or other legal proceedings. If a foreclosure action is instituted and the loan is not brought current, paid in full, or refinanced before the foreclosure sale, the real property securing the loan generally is sold at foreclosure. We may consider loan workout arrangements with certain borrowers under certain circumstances.

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Management reports to the Board of Directors monthly regarding the amount of loans delinquent more than 30 days, all loans in foreclosure and all foreclosed and repossessed property that we own.

Investment Portfolio

Our investment portfolio consists primarily of obligations of U.S. Government sponsored agencies as well as municipal and government authority bonds, with high grade corporate bonds accounting for less than 10% of the portfolio. Government regulations limit the type and quality of instruments in which the Company may invest its funds.

We conduct our asset/liability management through consultation with members of our Board of Directors, senior management and an outside financial advisor. The asset/liability investment committee, commonly known as an ALCO committee, is comprised of the president, senior officers and certain members of our Board of Directors. The ALCO committee, in consultation with our Board of Directors, is responsible for the review of interest rate risk and evaluates future liquidity needs over various time periods.

We have established a written investment policy which is reviewed annually by the ALCO committee and our Board of Directors that applies to Community Partners and the Bank. The investment policy identifies investment criteria and states specific objectives in terms of risk, interest rate sensitivity and liquidity and emphasizes the quality, term and marketability of the securities acquired for our investment portfolio.

The ALCO committee is responsible for monitoring the investment portfolio and ensuring that investments comply with the investment policy. The ALCO committee may from time to time consult with investment advisors. The Bank's president and its chief financial officer working with the financial advisor may purchase or sell securities in accordance with the guidelines of the ALCO committee. The Board of Directors reviews the components, including new transactions of the investment portfolio on a monthly basis.

Deposit Products

We emphasize relationships with commercial and individual customers and seek to obtain transaction accounts, which are frequently non-interest bearing deposits or lower cost interest bearing checking, savings and money market deposit accounts.

Deposits are the primary source of funds used in lending and other general business purposes. In addition to deposits, we may derive additional funds from principal repayments on loans, the sale of investment securities and borrowings from other financial institutions. Loan amortization payments have historically been a relatively predictable source of funds. The level of deposit liabilities can vary significantly and is influenced by prevailing interest rates, money market conditions, general economic conditions and competition.

The Bank's deposits consist of checking accounts, savings accounts, money market accounts and certificates of deposit. During the first half of 2012, we began to offer a suite of online only deposit products that we believe will be attractive to customers who prefer doing their banking online. All deposits, including the online accounts, are obtained from individuals, partnerships, corporations and unincorporated businesses in our market area. The Bank participates in CDARS, a service that enables us to provide our customers with additional FDIC insurance on CD products. We attempt to control the flow of deposits primarily by pricing our accounts to remain generally competitive with other financial institutions in our market area.

Business Growth Strategy

Our current plan for growth includes expanding our deposit product line and looking for opportunities to expand and optimize our branch network. We will focus on establishing a market presence in the communities between Union and Monmouth counties, New Jersey by adding strategically located new office(s) and considering selective acquisitions that would be accretive to earnings within the first full year of combined operations. During 2011, the Bank opened two regional lending offices in New Brunswick and Summit, New Jersey, for the purpose of expanding our presence in these communities. We believe that this strategy continues to build shareholder value and increase revenues and earnings per share by creating a larger base of lending and deposit relationships and achieving economics of scale and other efficiencies. Our efforts include looking for potential new retail banking offices in Middlesex county, New Jersey and other attractive markets where we have established lending relationships, as well as exploring opportunities to grow and add other profitable banking-related businesses. In November 2012, we opened a new and larger full service branch office in Red Bank, New Jersey. We believe that by establishing banking offices and making selective acquisitions in attractive growth markets while providing exemplary customer service, our core deposits will naturally increase. In addition, we launched online account opening capabilities in the first half of 2012 on our website to attract a wider consumer base with the convenience of being able to open deposit accounts 24 hours a day. Our current strategy continues to permit account openings in existing and contiguous markets.

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In March 2013, the Company filed the requisite applications to close its existing smaller branch in Red Bank as well as its Cliffwood branch. Management believes that the closure of both offices is in line with the strategic plans of optimizing the profitability of its branch network. The Company expects a minimal loss of customer relationships due to these closures and anticipates annual pre-tax expense savings of approximately $290,000. Both branches are expected to close in June 2013.

Supervision and Regulation

Overview

Community Partners operates within a system of banking laws and regulations intended to protect bank customers and depositors, and these laws and regulations govern the permissible operations and management, activities, reserves, loans and investments of the Company.

Community Partners is a bank holding company under the Federal Bank Holding Company Act of 1956 ("BHCA"), as amended by the Financial Modernization Act of 1999, known as the Gramm-Leach-Bliley Act, and is subject to the supervision of the Board of Governors of the Federal Reserve System (the "Federal Reserve"). In general, the BHCA limits the business of bank holding companies to banking, managing or controlling banks, and performing certain servicing activities for subsidiaries and, as a result of the Gramm-Leach-Bliley Act amendments, permits bank holding companies that are also financial holding companies to engage in any activity, or acquire and retain the shares of any company engaged in any activity, that is either (1) financial in nature or incidental to such financial activity or (2) complementary to a financial activity and does not pose a substantial risk to the safety and soundness of depository institutions or the financial system generally. In order for a bank holding company to engage in the broader range of activities that are permitted by the BHCA for bank holding companies that are also financial holding companies, upon satisfaction of certain regulatory criteria, the bank holding company must file a declaration with the Federal Reserve Board that it elects to be a "financial holding company." Community Partners does not presently intend to seek a "financial holding company" designation at this time, and does not believe that the current decision not to seek a financial holding company designation will adversely affect its ability to compete in its chosen markets. We believe that seeking such a designation for Community Partners would not position it to compete more effectively in the offering of products and services currently offered by the Bank. Community Partners is also subject to other federal laws and regulations as well as the corporate laws and regulations of New Jersey, the state of its incorporation.

The BHCA prohibits the Company, with certain exceptions, from acquiring direct or indirect ownership or control of more than five percent of the voting shares of any company which is not a bank and from engaging in any business other than that of banking, managing and controlling banks or furnishing services to subsidiary banks. The BHCA requires prior approval by the Federal Reserve Board of the acquisition by the Company of more than five percent of the voting stock of any other bank. Satisfactory capital ratios, Federal Community Reinvestment Act ratings and anti-money laundering policies are generally prerequisites to obtaining federal regulatory approval to make acquisitions.

The Bank is a commercial bank chartered under the laws of the State of New Jersey and is subject to the New Jersey Banking Act of 1948 (the "Banking Act"). As such, it is subject to regulation, supervision and examination by the New Jersey Department of Banking and Insurance and by the FDIC. Each of these agencies regulates aspects of activities conducted by the Bank and Community Partners, as discussed below. The Bank is not a member of the Federal Reserve Bank of New York.

The following descriptions summarize the key laws and regulations to which the Bank is subject, and to which Community Partners is subject as a registered bank holding company. These descriptions are not intended to be complete and are qualified in their entirety by reference to the full text of the statutes and regulations. Future changes in these laws and regulations, or in the interpretation and application thereof by their administering agencies, cannot be predicted, but could have a material effect on the business and results of Community Partners and the Bank.

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Small Business Lending Fund

On August 11, 2011, the Company received $12 million under the Small Business Lending Fund ("SBLF"). The SBLF was created in the fall of 2010 as part of the Small Business Jobs Act. The SBLF provides Tier 1 capital to community banks with assets of $10 billion or less, and provides incentives for making small business loans, defined as certain loans of up to $10 million to businesses with up to $50 million in annual revenues. In exchange for the $12 million, the Company issued to the U.S. Department of the Treasury ("Treasury") 12,000 shares of its Non-Cumulative Perpetual Preferred Stock, Series C, having a $1,000 liquidation preference per share (the "SBLF Preferred Shares"). The SBLF Preferred Shares qualify as Tier 1 capital.

Unlike the Troubled Asset Relief Program Capital Purchase Plan ("TARP CPP"), under the SBLF program, Treasury did not receive any warrants in connection with SBLF funding. Dividend rates on the SBLF Preferred Shares will be determined by the bank's lending practices with small business loans. The Company used a portion of the proceeds of the SBLF funds to redeem the full $9.0 million of its outstanding shares of Senior Preferred Stock, Series A (the "TARP Preferred Shares"), previously issued to the Treasury under TARP CPP. The TARP Preferred Shares, issued under TARP CPP qualified as Tier 1 capital and paid cumulative dividends at a rate of 5% per annum for the first five years. Dividends on the TARP Preferred Shares were payable on February 15, May 15, August 15 and November 15 of each year. As a result of the redemption of the TARP Preferred Shares, the Company is no longer subject to the executive compensation requirements in connection with the TARP CPP.

The noncumulative dividend rate on the SBLF Preferred Shares will be adjusted to reflect the amount of a change in the Company's qualified small business lending from its baseline, determined based upon the Company's qualified small business lending for each of the four full quarters ending June 30, 2010. Accordingly, the dividend rate will change as follows:

	Dividend Rate Following Investment Date		
Increase in Qualified Small Business Lending from the Baseline	First 9 Quarters*	Quarter 10 to Year 4.5	After Year 4.5
0% or less	5%	7%	9%
More than 0%, but less than 2.5%	5%	5%	9%
2.5% or more, but less than 5%	4%	4%	9%
5% or more, but less than 7.5%	3%	3%	9%
7.5% or more, but less than 10%	2%	2%	9%
10% or more	1%	1%	9%

* For the first nine quarters, the dividend rate will be adjusted quarterly.

After 10 years, if the SBLF Preferred Shares are not redeemed, the dividend rate will increase to the highest possible dividend rate as permitted by the Company's regulators. Dividends are payable quarterly on January 1, April 1, July 1 and October 1 of each year.

On August 1, 2011, the Company distributed a dividend of one right (a "Right") for each outstanding share of the Company's common stock, to shareholders of record at the close of business on August 1, 2011 (the "Record Date"). Each Right entitles the registered holder to purchase from the Company one one-thousandth of a share of Series B Junior Participating Preferred Stock, at a purchase price of $25.00, subject to adjustment, (as so adjusted, the "Exercise Price"). The Rights are designed to protect shareholders from abusive takeover tactics and attempts to acquire control of the Company at an inadequate price. The Rights are not exercisable or transferable unless certain specified events occur.

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Incentive Compensation

In June 2010, the Federal Reserve, the Office of the Currency Comptroller and FDIC issued comprehensive final guidance on incentive compensation policies intended to ensure that the incentive compensation policies of banking organizations do not undermine the safety and soundness of such organizations by encouraging excessive risk-taking. The guidance, which covers all employees that have the ability to materially affect the risk profile of an organization, either individually or as part of a group, is based upon the key principles that a banking organization's incentive compensation arrangements should (i) provide incentives that do not encourage risk-taking beyond the organization's ability to effectively identify and manage risks, (ii) be compatible with effective internal controls and risk management, and (iii) be supported by strong corporate governance, including active and effective oversight by the organization's board of directors. Also, in April 2011, the FDIC published a proposed interagency rule to implement certain incentive compensation requirements of the Dodd-Frank Act. Under the proposed rule, financial institutions must prohibit incentive-based compensation arrangements that encourage inappropriate risk taking that are deemed excessive or that may lead to material losses.

The Federal Reserve will review, as part of the regular, risk-focused examination process, the incentive compensation arrangements of banking organizations, such as us, that are not "large, complex banking organizations." These reviews will be tailored to each organization based on the scope and complexity of the organization's activities and the prevalence of incentive compensation arrangements. The findings of the supervisory initiatives will be included in reports of examination. Deficiencies will be incorporated into the organization's supervisory ratings, which can affect the organization's ability to make acquisitions and take other actions. Enforcement actions may be taken against a banking organization if its incentive compensation arrangements, or related risk-management control or governance processes, pose a risk to the organization's safety and soundness and the organization is not taking prompt and effective measures to correct the deficiencies.

The scope and content of the U.S. banking regulators' policies on executive compensation are continuing to develop and are likely to continue evolving in the near future. It cannot be determined at this time whether compliance with such policies will adversely affect the ability of the Company and the Bank to hire, retain and motivate their key employees.

Dividend Restrictions

The primary source of cash to pay dividends, if any, to the Company's shareholders and to meet the Company's obligations is dividends paid to the Company by the Bank. Dividend payments by the Bank to the Company are subject to the laws of the State of New Jersey, the Banking Act, the Federal Deposit Insurance Act ("FDIA") and the regulation of the New Jersey State Department of Banking and Insurance and of the Federal Reserve. Under the Banking Act and the FDIA, a bank may not pay any dividends if, after paying such dividends, it would be undercapitalized under applicable capital requirements. In addition to these explicit limitations, the federal regulatory agencies are authorized to prohibit a banking subsidiary or bank holding company from engaging in unsafe or unsound banking practices. Depending upon the circumstances, the agencies could take the position that paying a dividend would constitute an unsafe or unsound banking practice.

It is the policy of the Federal Reserve Board that bank holding companies should pay cash dividends on common stock only out of income available from the immediately preceding year and only if prospective earnings retention is consistent with the organization's expected future needs and financial condition. The policy provides that bank holding companies should not maintain a level of cash dividend that undermines the bank holding company's ability to serve as a source of strength to its banking subsidiary. A bank holding company may not pay dividends when it is insolvent.

The terms of the SBLF Preferred Shares impose limits on the ability of the Company to pay dividends and repurchase shares of common stock. Under the terms of the SBLF Preferred Shares, no repurchases may be effected, and no dividends may be declared or paid on preferred shares ranking pari passu with the SBLF Preferred Shares, junior preferred shares, or other junior securities (including the common stock) during the current quarter and for the next three quarters following the failure to declare and pay dividends on the SBLF Preferred Shares, except that, in any such quarter in which the dividend is paid, dividend payments on shares ranking pari passu may be paid to the extent necessary to avoid any resulting material covenant breach.

Under the terms of the SBLF Preferred Shares, the Company may only declare and pay a dividend on the common stock or other stock junior to the SBLF Preferred Shares, or repurchase shares of any such class or series of stock, if, after payment of such dividend, the dollar amount of the Company's Tier 1 Capital would be at least 90% of the Signing Date Tier 1 Capital, which is approximately $54.4 million, excluding any subsequent net charge-offs and any redemption of the SBLF Preferred Shares (the "Tier 1 Dividend Threshold"). Beginning on the first day of the eleventh dividend period, the amount of the Tier 1 Dividend Threshold will be reduced by 10% for each one percent increase in qualified small business lending from the baseline level through the ninth dividend period.

Community Partners did not pay any cash dividends to common shareholders in 2012.

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Transactions with Affiliates

Banking laws and regulations impose certain restrictions on the ability of bank holding companies to borrow from and engage in other transactions with their subsidiary banks. Generally, these restrictions require that any extensions of credit must be secured by designated amounts of specified collateral and be limited to (i) 10% of the bank's capital stock and surplus per non-bank affiliated borrower, and (ii) 20% of the bank's capital stock and surplus aggregated as to all non-bank affiliated borrowers. In addition, certain transactions with affiliates must be on terms and conditions, including credit standards, at least as favorable to the institution as those prevailing for arms-length transactions.

FIRREA

Under the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 ("FIRREA"), a depository institution insured by the FDIC can be held liable for any loss incurred by, or reasonably expected to be incurred by, the FDIC in connection with (i) the default of a commonly controlled FDIC-insured depository institution or (ii) any assistance provided by the FDIC to a commonly controlled FDIC-insured depository institution in danger of default. These provisions have commonly been referred to as FIRREA's "cross guarantee" provisions. Further, under FIRREA, the failure to meet capital guidelines could subject a bank to a variety of enforcement remedies available to federal regulatory authorities.

FIRREA also imposes certain independent appraisal requirements upon a bank's real estate lending activities and further imposes certain loan-to-value restrictions on a bank's real estate lending activities. The bank regulators have promulgated regulations in these areas.

Deposit Insurance

All U.S. banks are required to have their deposits insured by the FDIC. On July 21, 2010, the President signed into law the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"). As a result of changes made by the Dodd-Frank Act, the maximum amount of deposit insurance per depositor is $250,000, an increase from the old limit of $100,000. In addition, all non-interest bearing transaction account balances (basically, business checking accounts) are insured to an unlimited amount through 2012. The FDIC charges premiums or "assessments" to pay for the deposit insurance provided. These assessments are based on the average total assets of a bank minus the bank's average tangible equity.

Deposit insurance assessments have been "risk based," in that the riskier a bank's perceived business activities, the higher deposit insurance rate it has to pay. All banks are assigned to one of four "risk categories" by the FDIC, pursuant to their capital levels and examination results. The assignment to a particular risk category is made by the FDIC each quarter based on the most recent information available. Then, the FDIC applies certain adjustments to each bank based on its specific asset attributes to determine a final assessment ratio. As discussed above, these assessments are based on assets, not deposits, and the assessment rates will range from 2.5 basis points to 45 basis points. (The actual dollar amount paid by each small bank is expected to be very close to the amounts paid when the assessment base was composed of deposits.) In addition, the assessment rate for large banks (those over $10 billion in assets) is derived from a formula that that further takes into account specific activities and asset quality of a particular bank. Our bank is well below the $10 billion threshold for this additional assessment calculation.

The Dodd-Frank Act requires the deposit insurance fund to reach a reserve level of 1.35% of all insured deposits by September 2020, and authorizes the FDIC to implement changes in assessment rates in order to achieve such level. The Dodd-Frank Act authorizes the FDIC to establish a "designated reserve ratio" (which the FDIC has now set at 2.0%), and to reduce or eliminate assessments if the designated reserve ratio is met. If the deposit fund reserve ratio is 2.5% or more, the FDIC is authorized, but not required, to return assessments to banks. Given that most experts believe that the deposit fund will continue to incur losses over the short term for bank failures that have occurred and will occur from the financial crisis, it is expected that all banks will have to pay significant amounts of deposit insurance assessments for the foreseeable future, with little likelihood of reductions in deposit insurance assessments (or return of assessments paid) unless there is a material improvement in the economy and the health of the financial industry.

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Capital Adequacy

The Federal Reserve has adopted risk-based capital guidelines for banks and bank holding companies. The minimum guideline for the ratio of total capital to risk-weighted assets is 8%. At least half of the total capital is to be comprised of common stock, retained earnings, minority interests in the equity accounts of consolidated subsidiaries, noncumulative perpetual preferred stock and a limited amount of qualifying cumulative perpetual preferred stock, less goodwill and certain other intangibles ("Tier 1 Capital"). The remainder may consist of other preferred stock, certain other instruments and a portion of the loan loss allowance ("Tier II Capital"). "Total Capital" is the sum of Tier I Capital and Tier II Capital.

In addition, the Federal Reserve has established minimum leverage ratio guidelines for banks and bank holding companies. These guidelines provide for a minimum ratio of Tier 1 Capital to average total assets of 3% for banks that meet certain specified criteria, including having the highest regulatory rating. All other banks and bank holding companies generally are required to maintain a leverage ratio of at least 3% plus an additional cushion of 100 to 200 basis points. At December 31, 2012, Community Partners' leverage ratio was 10.36%.

The Company's and the Bank's capital ratios at December 31, 2012 and 2011 are set forth in "Management's Discussion and Analysis of Financial Condition and Results of Operations – Capital Resource". Both the Company and the Bank were "well-capitalized" at December 31, 2012.

The Basel Committee on Banking Supervision (the "Basel Committee") released a comprehensive list of proposals for changes to capital, leverage, and liquidity requirements for banks in December 2009 (commonly referred to as "Basel III"). In July 2010, the Basel Committee announced the design for its capital and liquidity reform proposals.

In September 2010, the oversight body of the Basel Committee announced minimum capital ratios and transition periods providing: (i) the minimum requirement for the Tier 1 common equity ratio will be increased from the current 2.0% level to 4.5% (to be phased in by January 1, 2015); (ii) the minimum requirement for the Tier 1 capital ratio will be increased from the current 4.0% to 6.0% (to be phased in by January 1, 2015); (iii) an additional 2.5% of Tier 1 common equity to total risk-weighted assets (to be phased in between January 1, 2016 and January 1, 2019; and (iv) a minimum leverage ratio of 3.0% (to be tested starting January 1, 2013). The revised capital requirements also narrow the definition of capital, excluding instruments that no longer qualify as Tier 1 common equity as of January 1, 2013, and phasing out other instruments over several years.

The liquidity proposals under Basel III include: (i) a liquidity coverage ratio (to become effective January 1, 2015); (ii) a net stable funding ratio (to become effective January 1, 2018); and (iii) a set of monitoring tools for banks to report minimum types of information to their regulatory supervisors.

In November 2012, the federal banking regulators delayed the January 2013 effective date of Basel III's proposed bank capital buffer rules, and did not provide a substitute date for effectiveness. In their announcement, they did indicate that they will take into account operational and other considerations when determining appropriate implementation dates and associated transition periods. This U.S. Regulator approved proposal would substantially amend the regulatory risk-based capital rules applicable to the Corporation and the Bank. The proposed rules implement the "Basel III" regulatory capital reforms and changes required by the Dodd-Frank Act.

Many of the details of the new framework related to minimum capital levels and minimum liquidity requirements in the Basel Committee's proposals will remain uncertain until the final release is issued later this year. Implementation of the final provisions of Basel III will require implementing regulations and guidelines by U.S. banking regulators. Implementation of these new capital and liquidity requirements has created significant uncertainty with respect to the future liquidity and capital requirements for financial institutions. Therefore, we are not able to predict at this time the content of liquidity and capital guidelines or regulations that may be adopted by regulatory agencies or the impact that any changes in regulation may have on the Company and the Bank.

Prompt Corrective Action

The Federal Deposit Insurance Act (FDIA) requires federal banking regulators to take prompt corrective action with respect to depository institutions that do not meet minimum capital requirements. Failure to meet minimum requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have an adverse material effect on Community Partners' financial condition. Under the FDIA's Prompt Corrective Action Regulations, the Bank must meet specific capital guidelines that involve quantitative measures of its assets, liabilities and certain off-balance sheet items as calculated under regulatory accounting practices.

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The Prompt Corrective Action Regulations define specific capital categories based on an institution's capital ratios. The capital categories, in declining order, are "well capitalized," "adequately capitalized," "undercapitalized," "significantly undercapitalized," and "critically undercapitalized." The FDIA imposes progressively more restrictive constraints on operations, management and capital distributions, depending on the capital category by which the institution is classified. Institutions categorized as "undercapitalized" or worse may be subject to requirements to file a capital plan with their primary federal regulator, prohibitions on the payment of dividends and management fees, restrictions on asset growth and executive compensation, and increased supervisory monitoring, among other things. Other restrictions may be imposed on the institution by the regulatory agencies, including requirements to raise additional capital, sell assets or sell the entire institution. Once an institution becomes "critically undercapitalized," it generally must be placed in receivership or conservatorship within 90 days.

The Prompt Corrective Action Regulations provide that an institution is "well capitalized" if the institution has a total risk-based capital ratio of 10.0% or greater, a Tier I risk-based capital ratio of 6.0% or greater, and a leverage ratio of 5.0% or greater. The institution also may not be subject to an order, written agreement, and capital directive or prompt corrective action directive to meet and maintain a specific level for any capital measure. An institution is "adequately capitalized" if it has a total risk-based capital ratio of 8.0% or greater, a Tier I risk-based capital ratio of 4.0% or greater, and a leverage ratio of 4.0% or greater (or a leverage ratio of 3.0% or greater if the institution is rated composite 1 in its most recent report of examination, subject to appropriate federal banking agency guidelines), and the institution does not meet the definition of a well-capitalized institution. An institution is deemed "undercapitalized" if it has a total risk-based capital ratio that is less than 8.0%, a Tier I risk-based capital ratio of less than 4.0%, or a leverage ratio of less than 4.0% (or a leverage ratio of 3.0% or greater if the institution is rated composite 1 in its most recent report of examination, subject to appropriate federal banking agency guidelines), and the institution does not meet the definition of a significantly undercapitalized or critically undercapitalized institution. An institution is "significantly undercapitalized" if the institution has a total risk-based capital ratio that is less than 6.0%, a Tier I risk-based capital ratio of less than 3.0%, or a leverage ratio less than 3.0% and the institution does not meet the definition of a critically undercapitalized institution, and is "critically undercapitalized" if the institution has a ratio of tangible equity to total assets that is equal to or less than 2.0%.

The appropriate federal banking agency may, under certain circumstances, reclassify a well-capitalized insured depository institution as adequately capitalized. The appropriate agency is also permitted to require an adequately capitalized or undercapitalized institution to comply with the supervisory provisions as if the institution were in the next lower category (but not to treat a significantly undercapitalized institution as critically undercapitalized) based on supervisory information other than an institution's capital levels.

Unsafe and Unsound Practices

Notwithstanding its Prompt Corrective Action Regulations category dictated by risk-based capital ratios, the FDIA permits the appropriate bank regulatory agency to reclassify an institution if it determines, after notice and a hearing, that the condition of the institution is unsafe or unsound, or if it deems the institution to be engaging in an unsafe or unsound practice. Also, if a federal regulatory agency with jurisdiction over a depository institution believes that the depository institution will engage, is engaging, or has engaged in an unsafe or unsound practice, the regulator may require that the bank cease and desist from such practice, following notice and a hearing on the matter.

The USA PATRIOT Act

On October 26, 2001, the President of the United States signed into law certain comprehensive anti-terrorism legislation known as the USA PATRIOT Act of 2001. Title III of the USA PATRIOT Act substantially broadened the scope of the U.S. anti-money-laundering laws and regulations by imposing significant new compliance and due diligence obligations on financial institutions, creating new crimes and penalties and expanding the extra-territorial jurisdiction of the United States. The Treasury has issued a number of implementing regulations which apply various requirements of the USA PATRIOT Act to financial institutions such as the Bank. Those regulations impose new obligations on financial institutions to maintain appropriate policies, procedures and controls to detect, prevent and report money laundering and terrorist financing.

Failure of a financial institution to comply with the USA PATRIOT Act's requirements could have serious legal consequences for the institution and adversely affect its reputation. Community Partners and the Bank adopted appropriate policies, procedures and controls to address compliance with the requirements of the USA PATRIOT Act under the existing regulations and will continue to revise and update its policies, procedures and controls to reflect changes required by the USA PATRIOT Act and by Treasury regulations.

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Community Reinvestment Act

The Federal Community Reinvestment Act ("CRA") requires banks to respond to the full range of credit and banking needs within their communities, including the needs of low and moderate-income individuals and areas. A bank's failure to address the credit and banking needs of all socio-economic levels within its markets may result in restrictions on growth and expansion opportunities for the bank, including restrictions on new branch openings, relocation, formation of subsidiaries, mergers and acquisitions. Upon completion of a CRA examination, an overall CRA rating is assigned using a four-tiered rating system. These ratings are: Outstanding, Satisfactory, Needs to Improve, and Substantial Noncompliance.

In the latest CRA performance evaluation examination report with respect to the Bank, dated July 2, 2012, the Bank received a rating of Satisfactory.

Consumer Privacy

In addition to fostering the development of "financial holding companies," the Gramm-Leach-Bliley Act modified laws relating to financial privacy. Its financial privacy provisions generally prohibit financial institutions, including Community Partners and the Bank, from disclosing or sharing nonpublic personal financial information to third parties for marketing or other purposes not related to transactions, unless customers have an opportunity to "opt out" of authorizing such disclosure, and have not elected to do so. It has never been the policy of Community Partners or the Bank, to release such information except as may be required by law.

Loans to One Borrower

Federal banking laws limit the amount a bank may lend to a single borrower to 15% of the bank's capital base, unless the entire amount of the loan is secured by adequate amounts of readily marketable collateral. However, no loan to one borrower may exceed 25% of a bank's statutory capital, notwithstanding collateral pledged to secure it.

New Jersey banking law limits the total loans and extensions of credit by a bank to one borrower at one time to 15% of the capital funds of the bank when the loan is fully secured by collateral having a market value at least equal to the amount of the loans and extensions of credit. Such loans and extensions of credit are limited to 10% of the capital funds of the bank when the total loans and extensions of credit by a bank to one borrower at one time are fully secured by readily available marketable collateral having a market value (as determined by reliable and continuously available price quotations) at least equal to the amount of funds outstanding. This 10% limitation is separate from and in addition to the 15% limitation noted in the beginning of this paragraph. If a bank's lending limit is less than $500,000, the bank may nevertheless have total loans and extensions of credit outstanding to one borrower at one time not to exceed $500,000. At December 31, 2012, the Bank's lending limit to one borrower was $12.2 million.

Sarbanes-Oxley Act of 2002

The Sarbanes-Oxley Act of 2002 (the "Sarbanes-Oxley Act"), which became law on July 30, 2002, created new legal requirements affecting corporate governance, accounting and corporate reporting for companies with publicly traded securities.

The Sarbanes-Oxley Act provides for, among other things:

- a prohibition on personal loans made or arranged by the issuer to its directors and executive officers (except for loans made by a bank subject to Regulation O);

- independence requirements for audit committee members;
- disclosure of whether at least one member of the audit committee is a “financial expert” (as such term is defined by the SEC) and if not, why not;
- independence requirements for outside auditors;
- certification of financial statements and reports on Forms 10-K and 10-Q by the chief executive officer and the 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 due to corporate misconduct;

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- disclosure of a code of ethics for financial officers and filing a Form 8-K for a change or waiver of such code; and
- various increased criminal penalties for violations of securities laws.

Additionally, Section 404 of the Sarbanes-Oxley Act requires that a public company subject to the reporting requirements of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), include in its annual report (i) a management's report on internal control over financial reporting assessing the company's internal controls, and (ii) for larger publicly traded companies, an auditor's attestation report, completed by the independent registered public accounting firm that prepares or issues an accountant's report that is included in the company's annual report, attesting to the effectiveness of management's internal controls over financial reporting. Because we are neither a "large accelerated filer" nor an "accelerated filer", compliance with the auditor's attestation report requirement is not required.

All of the national stock exchanges, including the Nasdaq Capital Market where our common stock is listed, have implemented corporate governance rules, including rules strengthening director independence requirements for boards, and the adoption of charters for the nominating, corporate governance, and audit committees. The rule changes are intended to, among other things, make the Board of Directors independent of management and allow shareholders to more easily and efficiently monitor the performance of companies and directors. These increased burdens have increased our legal and accounting fees and the amount of time that our Board of Directors and management must devote to corporate governance issues.

Dodd-Frank Act

The Dodd-Frank Act, which was enacted in July 2010, significantly restructured financial regulation in the United States, including through the creation of a new resolution authority, mandating higher capital and liquidity requirements, and requiring banks to pay increased fees to regulatory agencies.

The implications of the Dodd-Frank Act for the Company's businesses will depend to a large extent on the manner in which rules adopted pursuant to the Dodd-Frank Act are implemented by the primary U.S. financial regulatory agencies, as well as potential changes in market practices and structures in response to the requirements of the Dodd-Frank Act and financial reforms in other jurisdictions. Among other things:

- The Dodd-Frank Act repealed the federal prohibitions on the payment of interest on demand deposits, thereby permitting depository institutions to pay interest on business transaction and other accounts. Depending on competitive responses, this significant change to existing law could have an adverse impact on the Company's interest expense.

- The Dodd-Frank Act also broadens the base for FDIC insurance assessments. Assessments will now be based on the average consolidated total assets less tangible equity capital of a financial institution.

- The Dodd-Frank Act also permanently increases the maximum amount of deposit insurance for banks, savings institutions and credit unions to $250,000 per depositor, retroactive to January 1, 2008, and non-interest bearing transaction accounts have unlimited deposit insurance through December 31, 2012.

- Bank and thrift holding companies with assets of less than $15 billion as of December 31, 2009, such as the Company, will be permitted to include trust preferred securities that were issued before May 19, 2010, as Tier 1 capital; however, trust preferred securities issued by a bank or thrift holding company (other than those with assets of less than $500 million) after May 19, 2010, will no longer count as Tier 1 capital. Trust preferred securities still will be entitled to be treated as Tier 2 capital.

- The Dodd-Frank Act centralized responsibility for consumer financial protection by creating a new agency, the Consumer Financial Protection Bureau (“CFPB”), and giving it responsibility for implementing, examining and enforcing compliance with federal consumer protection laws.

- The “Durbin Amendment” provisions of the Dodd-Frank Act provided that debit card interchange fees must be reasonable and proportional to the cost incurred by the issuer with respect to the transaction. In June 2011, the Federal Reserve adopted regulations setting the maximum permissible interchange fee as the sum of 21 cents per transaction and 5 basis points multiplied by the value of the transaction, with an additional adjustment of up to one cent per transaction, with an additional adjustment of up to one cent per transaction if the issuer implements certain fraud-prevention standards.

- The Dodd-Frank Act created a new systemic risk oversight body, the Financial Stability Oversight Council (“FSOC”), to oversee and coordinate the efforts of the primary U.S. financial regulatory agencies in establishing regulations to address financial stability concerns.

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- The Dodd-Frank Act directs the FSOC to make recommendations to the Federal Reserve as to enhanced supervision and prudential standards applicable to large, interconnected financial institutions, including bank holding companies with total consolidated assets of $50 billion or more, and authorizes the Federal Reserve to establish such standards either on its own or upon the recommendations of the FSOC.

- The Dodd-Frank Act includes provisions permitting national and insured state banks to engage in de novo interstate branching if, under the laws of the state where the new branch is to be established, as state bank chartered in that state would be permitted to establish a branch.

- The Dodd-Frank Act requires various U.S. financial regulatory agencies to implement comprehensive rules governing the supervision, structure, trading and regulation of swap and over the-counter derivative markets and participants. The Dodd-Frank Act requires a large number of rules in this area, many of which are not yet final.

- The Dodd-Frank Act requires the federal financial regulatory agencies to adopt rules that prohibit banks and their affiliates from engaging in proprietary trading and investing in and sponsoring certain unregistered investment companies (defined as hedge funds and private equity funds), with implementation starting as early as July 2012. The statutory provision is commonly referred to as the “Volcker Rule”. In October 2011, federal regulators proposed rules to implement the Volcker Rule. We do not currently anticipate that the Volcker Rule will have a material effect on our operations. However, until a final rule is adopted, the precise financial impact of the rule cannot be determined.

- In October 2011, the Federal Reserve issued a final rule implementing resolution planning requirements in the Dodd-Frank Act. The final rule requires bank holding companies with assets of $50 billion or more and nonbank financial firms designated by FSOC for supervision by the Federal Reserve to annually submit resolution plans to the FDIC and Federal Reserve. Each plan shall describe the company’s strategy for rapid and orderly resolution in bankruptcy during times of financial distress. Under the final rule, companies will submit their initial resolution plans on a staggered basis.

Executive Compensation.

The Dodd-Frank Act provides for a say on pay for shareholders of all public companies. Under the Dodd-Frank Act, each company must give its shareholders the opportunity to vote on the compensation of its executives at least once every three years. The Dodd-Frank Act also adds disclosure and voting requirements for golden parachute compensation that is payable to named executive officers in connection with sale transactions.

The SEC is required under the Dodd-Frank Act to issue rules obligating companies to disclose in proxy materials for annual meetings of shareholders information that shows the relationship between executive compensation actually paid to their named executive officers and their financial performance, taking into account any change in the value of the shares of a company’s stock and dividends or distributions.

The Dodd-Frank Act provides that the SEC must issue rules directing the stock exchanges to prohibit listing any security of a company unless the company develops and implements a policy providing for disclosure of the policy of the company on incentive-based compensation that is based on financial information required to be reported under the securities laws and that, in the event the company is required to prepare an accounting restatement due to the material noncompliance of the company with any financial reporting requirement under the securities laws, the company will recover from any current or former executive officer of the company who received incentive-based compensation during the three-year period preceding the date on which the company is required to prepare the restatement based on the erroneous data, any exceptional compensation above what would have been paid under the restatement.

Corporate Governance.

The Dodd-Frank Act requires the SEC, by rule, to require that each company disclose in the proxy materials for its annual meetings whether an employee or board member is permitted to purchase financial instruments designed to hedge or offset decreases in the market value of equity securities granted as compensation or otherwise held by the employee or board member.

The Dodd-Frank Act clarifies that the SEC may, but is not required to, promulgate rules that would require that a company's proxy materials include a nominee for the board of directors submitted by a shareholder. Although the SEC promulgated rules to accomplish this, these rules were invalidated by a federal appeals court decision. The SEC has said that they will not challenge the ruling, but has not ruled out the possibility that new rules could be proposed.

The Dodd-Frank Act requires stock exchanges to have rules prohibiting their members from voting securities that they do not beneficially own (unless they have received voting instructions from the beneficial owner) with respect to the election of a member of the board of directors (other than an uncontested election of directors of an investment company registered under the Investment Company Act of 1940), executive compensation or any other significant matter, as determined by the SEC by rule.

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FDIC Matters and Resolution Planning.

The Dodd-Frank Act created an orderly liquidation process that the FDIC can employ for failing financial companies that are not insured depository institutions. The Dodd-Frank Act gives the FDIC new authority to create a widely available emergency financial stabilization program to guarantee the obligations of solvent depository institutions and their holding companies and affiliates during times of severe economic stress. Additionally, Dodd-Frank also codifies many of the temporary changes that had already been implemented, such as permanently increasing the amount of deposit insurance to $250,000.

New laws or regulations or changes to existing laws and regulations (including changes in interpretation or enforcement) could materially adversely affect our financial condition or results of operations. Many aspects of the Dodd-Frank Act are subject to further rulemaking and interpretation, and will take effect over several years. The overall financial impact on the Company and its subsidiaries or the financial services industry generally cannot be anticipated at this time.

Overall Impact of New Legislation and Regulations

Various legislative initiatives are from time to time introduced in Congress and in the New Jersey State Legislature. It cannot be predicted whether or to what extent the business and condition of Community Partners or the Bank will be affected by new legislation or regulations, and legislation or regulations as yet to be proposed or enacted. Given that the financial industry remains under stress and severe scrutiny, and given that the U.S. economy has not yet fully recovered to pre-crisis levels of activity, we fully suspect that there will be significant legislation and regulatory actions that will materially affect the banking industry generally and our bank specifically for the foreseeable future.

Available Information

The Company maintains a website at www.tworiverbank.com. The Company makes available on its website free of charge its annual reports on Form 10-K, quarterly reports on Form 10-Q, Extensible Business Reporting Language (“XBRL”), a standards-based way to communicate and exchange business information between business systems, and current reports on Form 8-K, and amendments to those reports which are filed with or furnished to the SEC pursuant to Section 13(a) of the Securities Exchange Act of 1934. These documents are made available on the Company’s website as soon as reasonably practicable after they are electronically filed with or furnished to the SEC. Also available on the website are our Code of Conduct, our Shareholder Communications Policy and the charters of our Nominating and Corporate Governance Committee, Audit Committee, and Compensation Committee.

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Item 1A. Risk Factors.

The following are some important factors that could cause the Company's actual results to differ materially from those referred to or implied in any forward-looking statement. These are in addition to the risks and uncertainties discussed elsewhere in this Annual Report on Form 10-K and the Company's other filings with the SEC.

Our dependence on loans secured by real estate subjects us to risks relating to fluctuations in the real estate market and related interest rates and legislation that could result in significant additional costs and capital requirements that could adversely affect our financial condition and results of operations.

Approximately 88.5% of our loan portfolio as of December 31, 2012 was comprised of loans collateralized by real estate, with 100% of the real estate located in New Jersey. The real estate collateral in each case provides an alternate source of repayment in the event of default by the borrower and may deteriorate in value during the time the credit is extended. The real estate markets in New Jersey deteriorated in the last several years. A continued weakening of the real estate market in our primary market areas could have an adverse effect on the demand for new loans, the ability of borrowers to repay outstanding loans, the value of real estate and other collateral securing the loans and the value of real estate owned by us. As real estate values decline, it is also more likely that we would be required to make provisions for additional loan losses, which could adversely affect our financial condition and results of operations.

Current market conditions include an over-supply of land, lots and finished homes in many markets, including those where we do business. As of December 31, 2012, we had $83.8 million, or 14.6%, of our total loans in real estate construction loans. Of this amount, $85,000 was land loans and $29.6 million were made to finance residential construction with an identified purchaser. Substantially all of these loans are located in Monmouth and Union counties, New Jersey. Further, $54.1 million of real estate construction loans were made to finance commercial construction. Construction loans are subject to risks during the construction phase that are not present in standard residential real estate and commercial real estate loans. These risks include:

- the viability of the contractor;
- the value of the project being subject to successful completion;
- the contractor's ability to complete the project, to meet deadlines and time schedules and to stay within cost estimates; and
- concentrations of such loans with a single contractor and its affiliates.

Real estate construction loans also present risks of default in the event of declines in property values or volatility in the real estate market during the construction phase. If we are forced to foreclose on a project prior to completion, we may not be able to recover the entire unpaid portion of the loan, may be required to fund additional amounts to complete a project and may have to hold the property for an indeterminate amount of time. If any of these risks were to occur, it could adversely affect our financial condition, results of operations and cash flows.

The federal banking agencies have issued guidance regarding high concentrations of commercial real estate loans within bank loan portfolios. The guidance requires financial institutions that exceed certain levels of commercial real estate lending compared with their total capital to maintain heightened risk management practices that address the following key elements: including board and management oversight and strategic planning, portfolio management, development of underwriting standards, risk assessment and monitoring through market analysis and stress testing, and maintenance of increased capital levels as needed to support the level of commercial real estate lending. If there is any deterioration in our commercial real estate or real estate construction portfolios or if our regulators conclude that we have not implemented appropriate risk management practices, it could adversely affect our business and result in a requirement of increased capital levels, and such capital may not be available at that time.

Our commercial real estate and commercial loans expose us to increased credit risks, and these risks will increase if we succeed in increasing these types of loans.

We focus our lending efforts on commercial-related loans and intend to grow commercial real estate and commercial loans further as a proportion of our portfolio. As of December 31, 2012, commercial real estate loans and commercial and industrial loans totaled $426.5 million. In general, commercial real estate loans and commercial and industrial loans yield higher returns and often generate a deposit relationship, but also pose greater credit risks than do owner-occupied residential real estate loans. As our various commercial-related loan portfolios increase, the corresponding risks and potential for losses from these loans will also increase.

We make both secured and some unsecured commercial and industrial loans. Unsecured loans generally involve a higher degree of risk of loss than do secured loans because, without collateral, repayment is wholly dependent upon the success of the borrowers' businesses. Secured commercial and industrial loans are generally collateralized by accounts receivable, inventory, equipment or other assets owned by the borrower and include a personal guaranty of the business owner. Compared to real estate, that type of collateral is more difficult to monitor, its value is harder to ascertain, it may depreciate more rapidly and it may not be as readily saleable if repossessed. Further, commercial and industrial loans generally will be serviced primarily from the operation of the business, which may not be successful, and commercial real estate loans generally will be serviced from income on the properties securing the loans.

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Our financial condition and results of operations would be adversely affected if our allowance for loan losses is not sufficient to absorb actual losses or if we are required to increase our allowance.

Despite our underwriting criteria, we may experience loan delinquencies and losses. In order to absorb losses associated with non-performing loans, we maintain an allowance for loan losses based on, among other things, historical experience, an evaluation of economic conditions, and regular reviews of delinquencies and loan portfolio quality. Determination of the allowance inherently involves a high degree of subjectivity and requires us to make significant estimates of current credit risks and future trends, all of which may undergo material changes. At any time there are likely to be loans in our portfolio that will result in losses but that have not been identified as non-performing or potential problem credits. We cannot be sure that we will be able to identify deteriorating credits before they become non-performing assets or that we will be able to limit losses on those loans that are identified.

We may be required to increase our allowance for loan losses for any of several reasons. State and federal regulators, in reviewing our loan portfolio as part of a regulatory examination, may request that we increase our allowance for loan losses. Changes in economic conditions affecting borrowers, new information regarding existing loans, identification of additional problem loans and other factors, both within and outside of our control, may require an increase in our allowance. In addition, if charge-offs in future periods exceed our allowance for loan losses, we will need additional increases in our allowance for loan losses. Any increases in our allowance for loan losses will result in a decrease in our net income and, possibly, our capital, and may materially affect our results of operations in the period in which the allowance is increased.

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

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

Difficult market conditions and economic trends in the real estate market have adversely affected our industry and our business.

We are particularly affected by downturns in the U. S. real estate market. Dramatic declines in the real estate market over the past two years, with decreasing property values and increasing delinquencies and foreclosures, may have a negative impact on the credit performance of commercial and construction, mortgage, and consumer loan portfolios resulting in significant write-downs of assets by many financial institutions. In addition, the values of real estate collateral supporting many loans have declined and may continue to decline. General downward economic trends, reduced availability of commercial credit and increased unemployment levels may negatively impact the credit performance of commercial and consumer credit, resulting in additional write-downs. Concerns over the stability of the financial markets and the economy have resulted in decreased lending by financial institutions to their customers. This market turmoil and tightening of credit has led to increased commercial and consumer deficiencies, lack of customer confidence, increased market volatility and widespread reduction in general business activity. The resulting economic pressure on consumers and businesses and the lack of confidence in the financial markets may adversely affect our business, financial condition, results of operations and stock price. A worsening of these economic conditions would likely exacerbate the adverse effects of these difficult market conditions on us and others in the industry. Our ability to properly assess the creditworthiness of customers and to estimate the losses inherent in our credit exposure is made more complex by these difficult market and economic conditions. Accordingly, if these market conditions and trends continue, we may experience increases in foreclosures, delinquencies and customer bankruptcies, as well as more restricted access to funds.

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The effects of Superstorm Sandy or similar natural disaster may negatively impact collateral values or loan originations in the areas in which we do business.

On October 29, 2012, Superstorm Sandy made landfall in New Jersey, causing widespread property damage throughout the northeastern United States, including our primary market area in New Jersey. Although Superstorm Sandy did not have a material adverse effect on our operations, financial condition or results of operations, we continue to monitor and assess the extent to which collateral values associated with loans and leases may have been reduced and repair costs have risen, both of which could necessitate additional provisions to the allowance for loan and lease losses. In addition, the disruption in utilities, transportation, and communications systems in the affected areas may reduce our volume of loan and lease originations or other operational functions.

A similar or worse natural disaster than Superstorm Sandy could have a material adverse effect. Natural disasters can disrupt our operations, result in damage to our properties, reduce or destroy the value of the collateral for our loans and negatively affect the local economies in which we operate, which could have a material adverse effect on our results of operations and financial condition. The occurrence of a natural disaster could result in one or more of the following: (i) an increase in loan delinquencies; (ii) an increase in problem assets and foreclosures; (iii) a decrease in the demand for our products and services; or (iv) a decrease in the value of the collateral for loans, especially real estate, in turn reducing customers' borrowing power, the value of assets associated with problem loans and collateral coverage.

The Company's profitability depends significantly on local economic conditions.

The Company's success depends primarily on the general economic conditions of the primary markets in New Jersey in which it operates and where its loans are concentrated. Unlike nationwide banks that are more geographically diversified, the Company provides banking and financial services to customers primarily in Monmouth and Union counties, New Jersey. The local economic conditions in these areas have a significant impact on the Company's commercial and industrial, real estate and construction loans, the ability of its borrowers to repay their loans and the value of the collateral securing these loans. In addition, if the population or income growth in the Company's market areas is slower than projected, income levels, deposits and housing starts could be adversely affected and could result in a reduction of the Company's expansion, growth and profitability. Although economic conditions in Monmouth and Union counties, New Jersey have not deteriorated to the same extent as in other areas of the country, such conditions could decline further. If the Company's market areas experience a downturn or a recession for a prolonged period of time, the Company could experience significant increases in nonperforming loans, which could lead to operating losses, impaired liquidity and eroding capital. A significant decline in general economic conditions, caused by inflation, recession, acts of terrorism, outbreaks of hostilities or other international or domestic calamities, unemployment, monetary and fiscal policies of the federal government or other factors could impact these local economic conditions and could negatively affect the Company's financial condition, results of operations and cash flows.

The small to medium-sized businesses that the Company lends to may have fewer resources to weather a downturn in the economy, which may impair a borrower's ability to repay a loan to the Company that could materially harm the Company's operating results.

The Company targets its business development and marketing strategy primarily to serve the banking and financial services needs of small to medium-sized businesses. These small to medium-sized businesses frequently have smaller market share than their competition, may be more vulnerable to economic downturns, often need substantial additional capital to expand or compete and may experience significant volatility in operating results. Any one or more of these factors may impair the borrower's ability to repay a loan. In addition, the success of a small to medium-sized business often depends on the management talents and efforts of one or two persons or a small group of persons, and the death, disability or resignation of one or more of these persons could have a material adverse impact on the business and its ability to repay a loan. Economic downturns and other events that negatively impact the Company's market areas could cause the Company to incur substantial credit losses that could negatively affect the Company's results of operations and financial condition.

We currently do not intend to pay dividends on our common stock. In addition, our future ability to pay dividends is subject to restrictions.

We have not paid any dividends to our holders of common stock in the past. In the event that we decide to pay dividends, there are a number of restrictions on our ability to pay dividends. It is the policy of the Federal Reserve that bank holding companies should pay cash dividends on common stock only out of income available over the past year and only if prospective earnings retention is consistent with the organization's expected future needs and financial condition. The policy provides that bank holding companies should not maintain a level of cash dividends that undermines the bank holding company's ability to serve as a source of strength to its banking subsidiaries. If we fail to pay dividends on our SBLF Preferred Shares, we will be prohibited from paying dividends on our common stock.

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Our principal source of funds to pay dividends on our common stock will be cash dividends that we receive from the Bank. The payment of dividends by the Bank to us is subject to certain restrictions imposed by federal and state banking laws, regulations and authorities. The federal banking statutes prohibit federally insured banks from making any capital distributions (including a dividend payment) if, after making the distribution, the institution would be "under capitalized" as defined by statute. In addition, the relevant federal regulatory agencies have authority to prohibit an insured bank from engaging in an unsafe or unsound practice, as determined by the agency, in conducting an activity. The payment of dividends could be deemed to constitute such an unsafe or unsound practice, depending on the financial condition of the Bank. Regulatory authorities could impose administratively stricter limitations on the ability of the Bank to pay dividends to us if such limits were deemed appropriate to preserve certain capital adequacy requirements.

The dividend rate on the SBLF Preferred Shares we issued in connection with the SBLF will fluctuate initially from 1% to 5% based on our level of "Qualified Small Business Lending," or "QSBL," as compared to our "baseline" level. The cost of the capital we received from the SBLF Preferred Shares will increase if the level of our "QSBL" as of June 30, 2013 does not represent an increase from our "baseline" level. This cost also will increase if we have not redeemed the SBLF Preferred Shares within 4.5 years of the closing of the SBLF transaction.

The per annum dividend rate on the SBLF Preferred Shares can fluctuate on a quarterly basis during the first ten quarters during which the SBLF Preferred Shares is outstanding, based upon changes in the amount of qualified small business lending (QSBL), as defined in the Supplemental Reports related to the SBLF transaction, from a "baseline" level (QSBL Baseline). During the three months ended December 31, 2012, the dividend rate was 4.323% and will be 3.511% and 2.000% for the first and second quarter of 2013, respectively. For the dividend periods ending with the tenth dividend period, the annual dividend rate may be adjusted to between 1% and 5%, to reflect the amount of percentage change in the Bank's level of QSBL from the QSBL Baseline to the level as of the end of the second quarter preceding the dividend period in question. For the eleventh dividend period through 4.5 years after the closing of the SBLF transaction, the annual dividend rate will be fixed at between 1% and 5%, based upon the percentage increase in QSBL from the QSBL Baseline to the level as of the end of the ninth dividend period (i.e., as of September 30, 2013); however, if there is no increase in QSBL from the QSBL Baseline to the level as of the end of the ninth dividend period (or if QSBL has decreased during that time period), the dividend rate will be fixed at 7%. Further, the potential dividend rate reduction in any period is limited, such that the reduction will not apply to any Series B Preferred Stock proceeds that exceed the dollar amount of the increase in QSBL for that period as compared to the QSBL Baseline.

In addition, if our QSBL is not above the QSBL Baseline at the end of March 31, 2013, because of our participation in TARP CPP, we must also pay a lending incentive fee of 2% per annum (payable quarterly), calculated based on the liquidation value of the outstanding SBLF Preferred Shares as of the end of that quarter, beginning with dividend payment dates on or after April 1, 2014 and ending on April 1, 2016. After 4.5 years from the closing of the SBLF transaction, the annual dividend rate will be fixed at 9%, regardless of the level of QSBL. Depending on our financial condition at the time, any such increases in the dividend rate could have a material negative effect on our liquidity.

Future dividend payments and common stock repurchases are subject to certain restrictions by the terms of the Secretary of the Treasury's equity investment in us.

Under the terms of the SBLF, for so long as any preferred stock issued under the SBLF remains outstanding, we are prohibited from making a dividend payment or share repurchase if, after the payment or repurchase, our Tier 1 capital would not be at least 90% of the amount existing at the time immediately after September 27, 2011, excluding any subsequent net charge-offs and partial repayments of the SBLF funding. This 90% limitation will decrease by a dollar amount equal to 10% of the SBLF funding for every 1% increase in QSBL that we have achieved over the QSBL Baseline. These restrictions will no longer apply to us after we have repaid the SBLF funding in full.

Failure to pay dividends on our SBLF Preferred Shares may have negative consequences, including external involvement in the Company’s board of directors.

If dividends on the SBLF Preferred Shares are not paid in full for six quarterly dividend periods, whether or not consecutive, and if the aggregate liquidation preference amount of the then-outstanding shares of SBLF Preferred Shares is at least $25.0 million, the total number of positions on our board of directors will automatically increase by two and the holders of the SBLF Preferred Shares, acting as a single class, will have the right to elect two individuals to serve in the new director positions. This right and the terms of such directors will end when we have paid full dividends for at least four consecutive quarterly dividend periods. If full dividends have not been paid on the SBLF Preferred Shares for five or more quarterly dividend periods, whether or not consecutive, we must invite a representative selected by the holders of a majority of the outstanding shares of SBLF Preferred Shares, voting as a single class, to attend all meetings of our board of directors in a nonvoting observer capacity. Any such representative would not be obligated to attend any board meeting to which he or she is invited, and this right will end when we have paid full dividends for at least four consecutive dividend periods.

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Our preferred shares impact net income available to our common stockholders and our earnings per share.

The dividends declared on the SBLF Preferred Shares reduce net income available to common shareholders and our earnings per common share. The SBLF Preferred Shares will also receive preferential treatment in the event of liquidation, dissolution or winding up of the Company.

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

Our income and cash flows and the value of our assets depend to a great extent on the difference between the interest rates we earn on interest-earning assets, such as loans and investment securities, and the interest rates we pay on interest-bearing liabilities such as deposits and borrowings. These rates are highly sensitive to many factors which are beyond our control, including general economic conditions and policies of various governmental and regulatory agencies and, in particular, the Federal Reserve. Changes in monetary policy, including changes in interest rates, will influence not only the interest we receive on our loans and investment securities and the amount of interest we pay on deposits and borrowings but will also affect our ability to originate loans and obtain deposits and the value of our investment portfolio. If the rate of interest we pay on our deposits and other borrowings increases more than the rate of interest we earn on our loans and other investments, our net interest income, and therefore our earnings, could be adversely affected. Our earnings also could be adversely affected if the rates on our loans and other investments fall more quickly than those on our deposits and other borrowings.

Competition may decrease our growth or profits.

We face substantial competition in all phases of our operations from a variety of different competitors, including commercial banks, savings and loan associations, mutual savings banks, credit unions, consumer finance companies, factoring companies, leasing companies, insurance companies and money market mutual funds. There is very strong competition among financial services providers in our principal service area. Our competitors may have greater resources, higher lending limits or larger branch systems than we do. Accordingly, they may be able to offer a broader range of products and services as well as better pricing for those products and services than we can.

In addition, some of the financial services organizations with which we compete are not subject to the same degree of regulation as is imposed on federally insured financial institutions such as the Bank. As a result, those non-bank competitors may be able to access funding and provide various services more easily or at less cost than we can, adversely affecting our ability to compete effectively.

We rely on our management and other key personnel, and the loss of any of them may adversely affect our operations.

We are and will continue to be dependent upon the services of our executive management team. The Company's performance is largely dependent on the talents and efforts of highly skilled individuals. There is intense competition in the financial services industry for qualified employees. In addition, the Company faces increasing competition with businesses outside the financial services industry for the most highly skilled individuals. The unexpected loss of services of any key management personnel or commercial loan officers could have an adverse effect on our business and financial condition because of their skills, knowledge of our market, years of industry experience and the difficulty of promptly finding qualified replacement personnel. The Company's business operations could be adversely affected if it were unable to attract new employees and retain and motivate its existing employees.

We may be adversely affected by government regulation.

The banking industry is heavily regulated. Banking regulations are primarily intended to protect the federal deposit insurance funds and depositors, not shareholders. Changes in the laws, regulations, and regulatory practices affecting the banking industry may increase our costs of doing business or otherwise adversely affect us and create competitive advantages for others. Regulations affecting banks and financial services companies undergo continuous change, and we cannot predict the ultimate effect of these changes, which could have a material adverse effect on our profitability or financial condition.

The anti-money laundering or AML, and bank secrecy, or BSA, laws have imposed far-reaching and substantial requirements on financial institutions. The enforcement policy with respect to AML/BSA compliance has been vigorously applied throughout the industry, with regulatory action taking various forms. We believe that our policies and procedures with respect to combating money laundering are effective and that our AML/BSA policies and procedures are reasonably designed to comply with current applicable standards. We cannot provide assurance that in the future we will not face a regulatory action, adversely affecting our ability to acquire banks or open new branches.

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Additionally, the federal government has passed a variety of other reforms related to banking and the financial industry including, without limitation, the Dodd-Frank Act. The Dodd-Frank Act imposes significant regulatory and compliance changes. The key effects of the Dodd-Frank Act on our business are:

- changes to regulatory capital requirements;

- exclusion of hybrid securities, including trust preferred securities, issued on or after May 19, 2010 from tier 1 capital;

- creation of new government regulatory agencies (such as the Financial Stability Oversight Council, which will oversee systemic risk, and the Consumer Financial Protection Bureau, which will develop and enforce rules for bank and non-bank providers of consumer financial products);

- potential limitations on federal preemption;

- changes to deposit insurance assessments;

- regulation of debit interchange fees we earn;

- changes in retail banking regulations, including potential limitations on certain fees we may charge; and

- changes in regulation of consumer mortgage loan origination and risk retention.

Some provisions of the Dodd-Frank Act became effective immediately upon its enactment. Many provisions, however, will require regulations to be promulgated by various federal agencies in order to be implemented, some of which have been proposed by the applicable federal agencies. The provisions of the Dodd-Frank Act may have unintended effects, which will not be clear until implementation. The changes resulting from the Dodd-Frank Act could limit our business activities, require changes to certain of our business practices, impose upon us more stringent capital, liquidity and leverage requirements or otherwise materially and adversely affect us. These changes may also require us to invest significant management attention and resources to evaluate and make any changes necessary to comply with new statutory and regulatory requirements. Failure to comply with the new requirements could also materially and adversely affect us.

Environmental liability associated with lending activities could result in losses.

In the course of our business, we may foreclose on and take title to properties securing our loans. If hazardous substances were discovered on any of these properties, we could be liable to governmental entities or third parties for the costs of remediation of the hazard, as well as for personal injury and property damage. Many environmental laws can impose liability regardless of whether we knew of, or were responsible for, the contamination. In addition, if we arrange for the disposal of hazardous or toxic substances at another site, we may be liable for the costs of cleaning up and removing those substances from the site even if we neither own nor operate the disposal site. Environmental laws may require us to incur substantial expenses and may materially limit use of properties we acquire through foreclosure, reduce their value or limit our ability to sell them in the event of a default on the loans they secure. In addition, future laws or more stringent interpretations or enforcement policies with respect to existing laws may increase our exposure to environmental liability.

Failure to implement new technologies in our operations may adversely affect our growth or profits.

The market for financial services, including banking services and consumer finance services is increasingly affected by advances in technology, including developments in telecommunications, data processing, computers, automation, Internet-based banking and telebanking. Our ability to compete successfully in our markets may depend on the extent to which we are able to exploit such technological changes. However, we can provide no assurance that we will be able to properly or timely anticipate or implement such technologies or properly train our staff to use such technologies. Any failure to adapt to new technologies could adversely affect our business, financial condition or operating results.

A limited market exists for our common stock.

Our common stock commenced trading on the NASDAQ Capital Market on April 4, 2006 and trading volumes since that time have been modest. The limited trading market for our common stock may cause fluctuations in the market value of our common stock to be exaggerated, leading to price volatility in excess of that which would occur in a more active trading market. Accordingly, you may have difficulty selling our common stock at prices which you find acceptable or which accurately reflect the value of the Company.

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We are subject to liquidity risk.

Liquidity risk is the potential that we will be unable to meet our obligations as they become due, capitalize on growth opportunities as they arise, or pay regular cash dividends because of an inability to liquidate assets or obtain adequate funding in a timely basis, at a reasonable cost and within acceptable risk tolerances.

Liquidity is required to fund various obligations, including credit commitments to borrowers, mortgage and other loan originations, withdrawals by depositors, repayment of borrowings, dividends to shareholders, operating expenses and capital expenditures. Liquidity is derived primarily from retail deposit growth and retention; principal and interest payments on loans; principal and interest payments on and the sale, maturity and prepayment of investment securities; net cash provided from operations and access to other funding sources.

Our access to funding sources in amounts adequate to finance our activities could be impaired by factors that affect us specifically or the financial services industry in general. Factors that could detrimentally impact our access to liquidity sources include a decrease in the level of our business activity due to a market downturn or adverse regulatory action against us. Our ability to borrow could also be impaired by factors that are not specific to us, such as a severe disruption of the financial markets or negative views and expectations about the prospects for the financial services industry as a whole as evidenced by turmoil faced by banking organizations in 2008 in the domestic and worldwide credit markets.

Future offerings of debt or other securities may adversely affect the market price of our stock.

In the future, we may attempt to increase our capital resources or, if our or the Bank's capital ratios fall below the required minimums, we or the Bank could be forced to raise additional capital by making additional offerings of debt or preferred equity securities, including medium-term notes, trust preferred securities, senior or subordinated notes and preferred stock. Upon liquidation, holders of our debt securities and shares of preferred stock and lenders with respect to other borrowings will receive distributions of our available assets prior to the holders of our common stock. Additional equity offerings may dilute the holdings of our existing shareholders or reduce the market price of our common stock, or both. Holders of our common stock are not entitled to preemptive rights or other protections against dilution.

The Company may lose lower-cost funding sources.

Checking, savings, and money market deposit account balances and other forms of customer deposits can decrease when customers perceive alternative investments, such as the stock market, as providing a better risk/return tradeoff. If customers move money out of bank deposits and into other investments, the Company could lose a relatively low-cost source of funds, increasing its funding costs and reducing the Company's net interest income and net income.

The Company is subject to operational risk.

The Company faces the risk that the design of its controls and procedures, including those to mitigate the risk of fraud by employees or outsiders, may prove to be inadequate or are circumvented, thereby causing delays in detection of errors or inaccuracies in data and information. Management regularly reviews and updates the Company'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 Company's controls and procedures or failure to comply with regulations related to controls and procedures could have a material adverse effect on the Company's business, results of operations and financial condition.

The Company may also be subject to disruptions of its systems arising from events that are wholly or partially beyond its control (including, for example, computer viruses or electrical or telecommunications outages), which may give rise to losses in service to customers and to financial loss or liability. The Company is further exposed to the risk that its external vendors may be unable to fulfill their contractual obligations (or will be subject to the same risk of fraud or operational errors by their respective employees as is the Company) and to the risk that the Company's (or its vendors') business continuity and data security systems prove to be inadequate.

Item 1B. Unresolved Staff Comments.

Not applicable.

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Item 2. Properties.

The following table provides certain information with respect to properties used by the Company or the Bank in their operations:

Office Location	Address	Description	Opened	
Corporate Headquarters	766 Shrewsbury Avenue Tinton Falls, NJ	17,626 sq. ft. building (leased)	10/12	
The Bank's Main Office:	1250 Highway 35 South Middletown, NJ	5,300 sq. ft. first-floor stand- alone building (leased)	02/00	
Allaire:	Monmouth Executive Airport 229 Airport Road, Bldg. 13 Farmingdale, NJ	3,800 sq. ft. building (leased)	02/04	
Atlantic Highlands:	84 First Avenue Atlantic Highlands, NJ	700 sq. ft. store front (leased)	03/02	
Cliffwood:	Angel Street & Route 35 Aberdeen, NJ	2,500 sq. ft. building (leased)	11/04	(1)
Cranford Office:	104 Walnut Avenue Cranford, NJ	800 sq. ft. storefront (leased)	11/07	
Fanwood:	328 South Avenue Fanwood, NJ	2,966 sq. ft. stand-alone building (leased)	03/08	
Manasquan:	240 Route 71 Manasquan, NJ	4,300 sq. ft. stand-alone building (leased)	06/08	
Navesink:	East Pointe Shopping Center 2345 Route 36 Atlantic Highlands, NJ	2,080 sq. ft. in strip shopping center (leased)	09/05	
Port Monmouth:	357 Highway 36 Port Monmouth, NJ	2,180 sq. ft. stand-alone building (leased)	06/01	
Red Bank:	City Centre Plaza 100 Water Street Red Bank, NJ	512 sq. ft. in strip shopping center (leased)	09/02	(1)
Red Bank:	140 Broad Street Red Bank, NJ	2,350 sq. ft. store front (leased)	11/12	
Tinton Falls:	4050 Asbury Avenue	3,400 sq. ft. stand-alone building (leased)	10/06	

	Tinton Falls, NJ		
Tinton Falls:	656 Shrewsbury Avenue Tinton Falls, NJ	3,650 sq. ft. stand-alone building (leased)	08/00
West Long Branch:	359 Monmouth Road West Long Branch, NJ	3,100 sq. ft. in strip shopping center (leased)	01/04
Westfield:	520 South Avenue Westfield, NJ	3,000 sq. ft. stand-alone building (leased)	10/98
Westfield:	44 Elm Street Westfield, NJ	3,000 sq. ft. downtown building (owned)	04/01

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The Company owns property located at 245-249 North Avenue in Cranford, New Jersey, which is classified as assets held for sale in other assets. The Company plans to construct a full service branch at this location and has submitted the plans to various contractors for bids. After bids are received, the Board of Directors will determine if the Company will move forward with this project. Construction would be anticipated to begin in the third quarter of 2013 and be completed by the first quarter of 2014. We will reclassify this property from an asset held for sale in other assets to premises and equipment when the determination is made by the Board of Directors. The current carrying value of this property is $1.0 million.

(1) The Company has filed applications with its banking regulators to close these locations. For more information see "Item 9B. Other Information."

Item 3. Legal Proceedings.

The Company may, in the ordinary course of business, become a party to litigation involving collection matters, contract claims and other legal proceedings relating to the conduct of its business. The Company may also have various commitments and contingent liabilities which are not reflected in the accompanying consolidated balance sheet. At December 31, 2012, we were not involved in any material legal proceedings.

Item 4. Mine Safety Disclosures.

Not applicable

PART II

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

The common stock of the Company trades on the Nasdaq Capital Market under the trading symbol "CPBC". The following are the high and low sales prices per share.

	2012		2011	
	High	Low	High	Low
First Quarter	$ 6.10	$ 4.55	$ 5.19	$ 4.34
Second Quarter	6.20	5.50	5.06	4.32
Third Quarter	5.98	5.45	5.10	4.38
Fourth Quarter	6.05	5.27	4.75	4.47

As of March 15, 2013, there were approximately 543 record holders of the Company's common stock.

On January 24, 2013, the Company announced that the Board of Directors approved and authorized a share repurchase program (the "2013 Program"). The 2013 Program authorizes the repurchase of up to 5% of the outstanding shares of the Company's common stock, or approximately 399,200 shares based on the 7,983,778 shares outstanding as of December 31, 2012, provided that the aggregate amount that the Company may spend on such repurchases is limited to $2.2 million. The program will continue until the earlier of the completion of the repurchase or January 24, 2014.

Item 6. Selected Financial Data.

Not required.

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Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.

The following management's discussion and analysis of financial condition and results of operations is intended to provide a better understanding of the significant changes and trends relating to the financial condition, results of operations, capital resources, liquidity and interest rate sensitivity of Community Partners Bancorp as of December 31, 2012 and 2011 and for the years then ended. The following information should be read in conjunction with the audited consolidated financial statements as of and for the years ended December 31, 2012 and 2011, including the related notes thereto.

Critical Accounting Policies and Estimates

The following discussion is based upon our financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP"). The preparation of these financial statements requires the Company to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses.

Note 1 to our audited consolidated financial statements contains a summary of the Company's significant accounting policies. Management believes the following critical accounting policies encompass the more significant judgments and estimates used in the preparation of our consolidated financial statements.

Allowance for Loan Losses. Management believes our policy with respect to the methodology for the determination of the allowance for loan losses ("ALLL") involves a high degree of complexity and requires management to make difficult and subjective judgments which often require assumptions or estimates about highly uncertain matters. Changes in these judgments, assumptions or estimates could materially impact the results of operations. This critical policy and its application are reviewed quarterly with our audit committee and Board of Directors.

Management is responsible for preparing and evaluating the ALLL on a quarterly basis in accordance with Bank policy, and the Interagency Policy Statement on the ALLL released by the Board of Governors of the Federal Reserve System on December 13, 2006 as well as GAAP. We believe that our allowance for loan losses is adequate to cover specifically identifiable loan losses, as well as estimated losses inherent in our portfolio for which certain losses are probable but not specifically identifiable. The allowance for loan losses is based upon management's evaluation of the adequacy of the allowance account, including an assessment of known and inherent risks in the portfolio, giving consideration to the size and composition of the loan portfolio, actual loan loss experience, level of delinquencies, detailed analysis of individual loans for which full collectability may not be assured, the existence and estimated net realizable value of any underlying collateral and guarantees securing the loans, and current economic and market conditions. Although management utilizes the best information available, the level of the allowance for loan losses remains an estimate that is subject to significant judgment and short term change. Various regulatory agencies may require us and our banking subsidiaries to make additional provisions for loan losses based upon information available to them at the time of their examination. Furthermore, the majority of our loans are secured by real estate in New Jersey, primarily in Monmouth and Union counties. Accordingly, the collectability of a substantial portion of the carrying value of our loan portfolio is susceptible to changes in local market conditions and may be adversely affected should real estate values decline or the New Jersey and/or our local market areas experience economic shock.

Stock Based Compensation. Stock based compensation cost has been measured using the fair value of an award on the grant date and is recognized over the service period, which is usually the vesting period. The fair value of each option is amortized into compensation expense on a straight-line basis between the grant date for the option and each vesting date. The Company estimates the fair value of stock options on the date of grant using the Black-Scholes option pricing model. The model requires the use of numerous assumptions, many of which are highly subjective in nature.

Goodwill Impairment. Although goodwill is not subject to amortization, the Company must test the carrying value for impairment at least annually or more frequently if events or changes in circumstances indicate that the asset might be impaired. Impairment testing requires that the fair value of our reporting unit be compared to the carrying amount of its net assets, including goodwill. Our reporting unit was identified as our community bank operations. If the fair value of the reporting unit exceeds the book value, no write-down of recorded goodwill is necessary. If the fair value of a reporting unit is less than book value, an expense may be required on the Company's books to write-down the related goodwill to the proper carrying value. Impairment testing during 2012 and 2011 for goodwill and intangibles was completed and the Company did not require any impairment charge during the years ended December 31, 2012 and 2011.

Investment Securities Impairment Valuation. Securities are evaluated on at least a quarterly basis, and more frequently when market conditions warrant such an evaluation, to determine whether a decline in their value is other-than-temporary. The analysis of other-than-temporary impairment requires the use of various assumptions including, but not limited to, the length of time the investment's book value has been greater than fair value, the severity of the investment's decline and the credit deterioration of the issuer. For debt securities, management assesses whether (a) it has the intent to sell the security and (b) it is more likely than not that it will be required to sell the security prior to its anticipated recovery. These steps are done before assessing whether the entity will recover the cost basis of the investment.

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In instances when a determination is made that an other-than-temporary impairment exists but the investor does not intend to sell the debt security and it is not more likely than not that it will be required to sell the debt security prior to its anticipated recovery, the other-than-temporary impairment is separated into (a) the amount of the total other-than-temporary impairment related to a decrease in cash flows expected to be collected from the debt security (the credit loss) and (b) the amount of the total other-than-temporary impairment related to all other factors. The amount of the total other-than-temporary impairment related to the credit loss is recognized in earnings. The amount of the total other-than-temporary impairment related to all other factors is recognized in other comprehensive income.

Other Real Estate Owned ("OREO"). OREO includes real estate acquired through foreclosure. Real estate owned is carried at the lower of cost or fair value, less estimated costs to sell. When a property is acquired, the excess of the loan balance over fair value is charged to the allowance for loan losses. Operating results from real estate owned including rental income, operating expenses, and gains and losses realized from the sales of real estate owned are recorded as incurred. OREO is periodically reviewed to ensure that the fair value of the property supports the carrying value.

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

Executive Summary

The Company reported net income to common shareholders of $4.4 million for the year ended December 31, 2012, compared to a net income to common shareholders of $3.5 million in 2011, an increase of $873,000, or 25.0%. Basic and diluted earnings per common share after preferred stock dividends and accretion were $0.55 and $0.54, respectively, for the year ended December 31, 2012 compared to basic and diluted earnings of $0.44 per common share for the same period in 2011. In 2011, net income to common shareholders was adversely impacted by the $301,000 remaining discount accretion resulting from the redemption of the preferred stock issued under the U.S. Treasury's TARP Capital Purchase Plan. Excluding the effect of this item (non-GAAP), net income to common shareholders for the year ended December 31, 2012 would have increased $572,000, or 15.1%. For the year ended December 31, 2012, net interest income increased by $412,000, or 1.6%, to $26.2 million from $25.8 million recorded for the year ended December 31, 2011. Our results for 2012 were primarily affected by increased net interest income and non-interest income due primarily to the strong loan and core deposit growth, a decrease in the provision for loan losses and an increase in non-interest income due primarily to other loan fees and gains on the sale of SBA loans. These increases were partially offset by an increase in non-interest expense primarily due to higher salary and benefit costs resulting in part to the expansion of our lending division, as well as an increase in net OREO expenses and loan workout expenses.

Total assets increased by $59.3 million, or 8.8%, to $733.9 million at December 31, 2012 from $674.6 million at December 31, 2011. The increase in total assets was primarily the result of the strong deposit growth which helped fund the strong loan and investment securities growth during the year.

Total loans amounted to $571.4 million at December 31, 2012, which was an increase of $41.3 million, or 7.8%, compared to the December 31, 2011 amount of $530.1 million. During 2012, $525,000 of net loans were transferred to other real estate owned. The Company continues to provide commercial and consumer lending to our market customers in addition to maintaining our high credit standards in a challenging market. The allowance for loan losses totaled $8.0 million, or 1.40% of total loans, at December 31, 2012, compared to $7.3 million or 1.38% of total loans, at December 31, 2011. The increase in the allowance for loan losses is primarily the result of growth in the loan portfolio.

Deposits increased to $606.8 million at December 31, 2012 from $553.9 million at December 31, 2011, an increase of $52.9 million, or 9.6%. The increase in deposits is primarily attributable to the growth in our core checking deposits resulting primarily from increased business and consumer activity.

Shareholders' equity amounted to $92.0 million at December 31, 2012 from $87.1 million at December 31, 2011, an increase of $4.9 million, or 5.6%. At year-end 2012, tangible book (non-GAAP) value per common share increased to $7.71 compared to $7.13 at December 31, 2011.

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Results of Operations

Our principal source of revenue is net interest income, the difference between interest income on interest earning assets and interest expense on deposits and borrowings. Interest earning assets consist primarily of loans, investment securities and federal funds sold. Sources to fund interest earning assets consist primarily of deposits and borrowed funds. Our net income is also affected by our provision for loan losses, non-interest income and non-interest expenses. Non-interest income consists primarily of service charges, commissions and fees, while non-interest expenses are comprised of salaries and employee benefits, occupancy costs and other operating expenses.

The following table provides certain performance ratios for the dates and periods indicated.

	2012	2011	2010
Return on average assets	0.69%	0.65%	0.56%
Return on average tangible assets (1)	0.71%	0.67%	0.57%
Return on average equity	5.36%	5.16%	4.60%
Return on average tangible equity (1)	6.75%	6.64%	6.05%
Net interest margin	4.08%	4.21%	4.15%
Average equity to average assets	12.84%	12.54%	12.08%
Average tangible equity to average tangible assets (1)	10.47%	10.02%	9.45%

(1) The following table provided the reconciliation of Non-GAAP Financial Measures for the dates indicated:

	2012	2011	2010
Net income available to common shareholders	$ 4,367	$ 3,494	$ 3,039
Effect of accelerated portion of discount accretion	-	301	-
Net income available to common shareholders excluding accelerated discount accretion	$ 4,367	$ 3,795	$ 3,039
Diluted earnings per common share	$ 0.54	$ 0.44	$ 0.39
Effect of accelerated portion of discount accretion	-	.04	-
Diluted earnings per common share excluding excluding accelerated discount accretion	$ 0.54	$ 0.48	$ 0.39
Book value per common share	$ 10.02	$ 9.46	$ 9.12
Effect of intangible assets	(2.31)	(2.33)	(2.39)
Tangible book value per common share	$ 7.71	$ 7.13	$ 6.73
Return on average assets	0.69%	0.65%	0.56%
Effect of intangible assets	0.02%	0.02%	0.01%
Return on average tangible assets	0.71%	0.67%	0.57%
Return on average equity	5.36%	5.16%	4.60%
Effect of average intangible assets	1.39%	1.48%	1.45%
Return on average tangible equity	6.75%	6.64%	6.05%
Average equity to average assets	12.84%	12.54%	12.08%

Effect of intangible assets	(2.37%)	(2.52%)	(2.63%)
Average tangible equity to average tangible assets	10.47%	10.02%	9.45%

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This Report contains certain financial information determined by methods other than in accordance with generally accepted accounting policies in the United States (GAAP). These non-GAAP financial measures are “net income available to common shareholders excluding U.S. Treasury preferred stock refund and accelerated discount accretion,” ‘diluted earnings per common share excluding U.S. Treasury preferred stock refund and accelerated discount accretion,” “tangible book value per common share,” “return on average tangible assets,” “return on average tangible equity” and “average tangible equity to average tangible assets.” This non-GAAP disclosure has limitations as an analytical tool and should not be considered in isolation or as a substitute for analysis of the Company’s results as reported under GAAP, nor is it necessarily comparable to non-GAAP performance measures that may be presented by other companies. Our management uses these non-GAAP measures in its analysis of our performance because it believes these measures are material and will be used as a measure of our performance by investors.

We anticipate that our performance ratios will remain challenged as we expect income from continuing operations in 2013 to continue to be impacted the prolonged low interest rate environment, by poor economic conditions in the New Jersey real estate market, high unemployment and low consumer confidence. In addition, should a further general decline in economic conditions in New Jersey continue throughout 2013 and beyond, the Company may suffer higher default rates on its loans, decreased value of assets it holds as collateral, and reduced loan originations as we continue to pursue only quality loans based on our guidelines.

Year Ended December 31, 2012 Compared to Year Ended December 31, 2011

Net Income

The Company reported net income to common shareholders of $4.4 million for the year ended December 31, 2012, compared to a net income to common shareholders of $3.5 million in 2011, an increase of $873,000, or 25.0%. Basic and diluted earnings per common share after preferred stock dividends and accretion were $0.55 and $0.54, respectively, for the year ended December 31, 2012 compared to basic and diluted earnings of $0.44 per common share for the same period in 2011. In 2011, net income to common shareholders was adversely impacted by the $301,000 remaining discount accretion resulting from the redemption of the preferred stock issued under the U.S. Treasury’s TARP Capital Purchase Plan. Excluding the effect of this item (non-GAAP), net income to common shareholders for the year ended December 31, 2012 would have increased $572,000, or 15.1%. The primary reasons for the increase in net income was due to an improvement in our net interest income resulting primarily from loan and core deposit growth, a decrease in the provision for loan losses and an increase in non-interest income due primarily to other loan fees and gains on sale of SBA loans. These increases were partially offset by an increase in non-interest expense primarily due to higher salary and benefit costs resulting in part to the expansion of our lending division, as well as an increase in net OREO expenses and loan workout expenses.

Net Interest Income

For the year ended December 31, 2012, net interest income amounted to $26.2 million, as compared to $25.8 million for the year ended December 31, 2011. This increase of $412,000, or 1.6%, was primarily the result of a higher level of average interest earning assets, lower deposit rates and a higher level of core checking deposits. As general economic conditions continued to remain weak, the Federal Reserve kept short term interest rates at 0.25% throughout 2012. Our average earning assets increased by $30.2 million, or 4.9%, to $643.4 million for the year ended December 31, 2012 from $613.2 million for the year ended December 31, 2011, while our net interest spread decreased by 11 basis points to 3.88% for the year ended December 31, 2012 as compared to 3.99% for the same period in 2011. The net interest margin decreased by 13 basis points to 4.08% for year ended December 31, 2012 as compared to 4.21% for the same period in 2011, primarily as a result of the prolonged low interest rate environment, which has exerted pressure on asset yields.

For the year ended December 31, 2012, total interest income decreased to $30.8 million from $31.0 million for the year ended December 31, 2011. This slight decrease of $208,000, or 0.7%, was primarily due to interest rate-related decreases in interest income of $2.0 million, partially offset by volume-related increases in interest income of $1.8 million for the year ended December 31, 2012 as compared to the prior year. The average yield on our interest earning assets decreased by 27 basis points to 4.79% for the year ended December 31, 2012 from 5.06% for the prior year.

Interest and fees on loans decreased by $217,000, or 0.7%, to $29.2 million for the year ended December 31, 2012 compared to $29.4 million for the same period in 2011. Of the $217,000 decrease in interest and fees on loans, $1.7 million was attributable to rate-related decreases partially offset by $1.5 million of volume-related increases. During 2012, there was $167,000 of interest and late fee reversals on loans transferred to non-accrual status, as compared to $48,000 in 2011. The average balance of the loan portfolio for the year ended December 31, 2012 increased by $26.6 million, or 5.1%, to $546.0 million from $519.4 million for the same period in 2011. The average annualized yield on the loan portfolio decreased to 5.35% for the year ended December 31, 2012, from 5.66% for the same period in 2011. The average balance of non-accrual loans was $5.1 million and $5.8 million for the years ended December 31, 2012 and 2011, respectively. The average balance in OREO amounted to $4.7 million and $7.8 million for the years ended December 31, 2012 and 2011, respectively, which impacted the Company’s loan yield for both periods presented.

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Interest income on Federal funds sold and interest bearing deposits was $81,000 for the year ended December 31, 2012, representing a decrease of $22,000, or 21.4%, from $103,000 for the same period in 2011. For the year ended December 31, 2012, Federal funds sold had no average balance as compared to $3.1 million with an average annualized yield of 0.22%, for the same period in 2011. During the second quarter of 2011, in order to maximize earnings on excess liquidity and increased safety of our funds, the Bank transferred its entire Federal funds sold balance to the Federal Reserve Bank of New York, which paid a higher return than our correspondent banks. Accordingly, for the year ended December 31, 2012, interest bearing deposits had an average balance of $31.7 million and an average annualized yield of 0.26% as compared to $37.8 million and an average annualized yield of 0.25% in 2011.

Interest income on investment securities totaled $1.6 million for the year ended December 31, 2012, compared to $1.5 million for year ended December 31, 2011. The $31,000 increase in interest income on investment securities was primarily attributable to an increase in volume related activity offset in part by a decrease in rate related activity. New purchases made in 2012 were made at lower rates resulting from the lower rate environment. For the year ended December 31, 2012, investment securities had an average balance of $65.6 million with an average annualized yield of 2.38%, compared to an average balance of $52.9 million with an average yield of 2.90%, for the year ended December 31, 2011.

Total interest expense amounted to $4.6 million for the year ended December 31, 2012, compared to $5.2 million for the corresponding period in 2011, a decrease of $620,000, or 11.8%. Of this decrease in interest expense, $618,000 was due to rate-related decreases on interest-bearing liabilities primarily resulting from lower deposit costs and a $2,000 decrease for volume-related decreases on interest-bearing liabilities.

The average balance of interest-bearing liabilities increased to $507.9 million for the year ended December 31, 2012, from $491.5 million for the same period last year, an increase of $16.4 million, or 3.3%. The average balance in NOW deposits during 2012 increased $11.7 million from $57.4 million with an average annualized yield of 0.45% for the year ended December 31, 2011, to $69.1 million with an average annualized yield of 0.43% for the same period in 2012. Additionally, the average balance on savings deposit accounts increased from $199.6 million with an average annualized yield of 0.86% for the year ended December 31, 2011, to $217.9 million with an average annualized yield of 0.74% for the year ended December 31, 2012. During 2012, average demand deposits reached $97.0 million, an increase of $10.3 million, or 11.9%, over the same period last year. These average balance increases were partially offset by decreases in certificates of deposit by $10.3 million, or 8.9%, to $106.0 million with an average annualized yield of 1.75% for the year ended December 31, 2012, from $116.3 million with an average annualized yield of 1.89% for the same period in 2011. Average money market deposits decreased by $5.0 million, or 5.7%, to $83.1 million with an average annualized yield of 0.38% for the year ended December 31, 2012, from $88.1 million with an average annualized yield of 0.58% for the same period in 2011. For the year ended December 31, 2012, the average yield on our interest-bearing liabilities was 0.91%, compared to 1.07% for the year ended December 31, 2011.

Our strategies for increasing and retaining core relationship deposits, managing loan originations within our acceptable credit criteria and loan category concentrations, and our planned branch network growth have combined to meet our liquidity needs. The Company also offers agreements to repurchase securities, commonly known as repurchase agreements, to its customers as an alternative to other insured deposits. Average balances of repurchase agreements for the year ended December 31, 2012 increased to $18.3 million, with an average interest rate of 0.59%, compared to $16.6 million, with an average interest rate of 0.71%, for the same prior year period.

The Company also utilizes FHLB term borrowings as an additional funding source. Average FHLB term borrowings amounted to $13.5 million for the years ended December 31, 2012 and 2011, respectively, with an average yield of 3.21% for both periods.

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The following table reflects, for the periods presented, the components of our net interest income, setting forth: (1) average assets, liabilities, and shareholders' equity, (2) interest income earned on interest-earning assets and interest expense paid on interest-bearing liabilities, (3) average yields earned on interest-earning assets and average rates paid on interest-bearing liabilities, (4) our net interest spread (i.e., the average yield on interest-earning assets less the average rate on interest-bearing liabilities), and (5) our yield on interest-earning assets. There have been no tax equivalent adjustments made to yields.

	Years ended December 31,							
	2012			2011			201	
	Average balance	Interest income/ expense	Average rates earned/ paid	Average balance	Interest income/ expense	Average rates earned/ paid	Average balance	Inte inco exp
	(in thousands, except for percentages)							
ASSETS								
Interest-Earning Assets:								
Interest bearing deposits in banks	$ 31,748	$ 81	0.26%	$ 37,801	$ 96	0.25%	$ 30,808	$
Federal funds sold	-	-	-	3,145	7	0.22%	12,704	
Investment securities	65,624	1,565	2.38%	52,932	1,534	2.90%	45,885	1
Loans, net of unearned fees (1) (2)	545,986	29,192	5.35%	519,364	29,409	5.66%	514,553	29
Total Interest-Earning Assets	643,358	30,838	4.79%	613,242	31,046	5.06%	603,950	31
Non-Interest-Earning Assets:								
Allowance for loan loss	(7,351)			(6,682)			(6,869)	
Other assets	63,303			59,723			54,173	
Total Assets	$ 699,310			$ 666,283			$ 651,254	
LIABILITIES & SHAREHOLDERS' EQUITY								
Interest-Bearing Liabilities:								
NOW deposits	$ 69,063	296	0.43%	$ 57,378	257	0.45%	$ 48,638	
Savings deposits	217,879	1,605	0.74%	199,641	1,720	0.86%	199,380	2
Money market deposits	83,140	320	0.38%	88,095	508	0.58%	99,659	
Time deposits	106,012	1,856	1.75%	116,331	2,202	1.89%	117,946	2
Securities sold under agreements to repurchase	18,266	107	0.59%	16,593	118	0.71%	15,367	
Long-term debt	13,500	434	3.21%	13,500	433	3.21%	9,719	
Total Interest-Bearing Liabilities	507,860	4,618	0.91%	491,538	5,238	1.07%	490,709	6
Non-Interest-Bearing Liabilities:								
Demand deposits	96,967			86,687			78,052	
Other liabilities	4,726			4,525			3,854	
Total Non-Interest-Bearing Liabilities	101,693			91,212			81,906	
Shareholders' Equity	89,757			83,533			78,639	
Total Liabilities and Shareholders' Equity	$ 699,310			$ 666,283			$ 651,254	

NET INTEREST INCOME	$ 26,220	$ 25,808	$ 25
NET INTEREST SPREAD (3)	3.88%	3.99%	
NET INTEREST MARGIN (4)	4.08%	4.21%	

(1) Included in interest income on loans are loan fees.
(2) Includes non-performing loans.
(3) The interest rate spread is the difference between the weighted average yield on average interest-earning assets and the weighted average cost of average interest-bearing liabilities.
(4) The interest rate margin is calculated by dividing net interest income by average interest-earning assets.

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Analysis of Changes in Net Interest Income

The following table sets forth for the periods indicated the amounts of the total change in net interest income that can be attributed to changes in the volume of interest-earning assets and interest-bearing liabilities and the amount of the change that can be attributed to changes in interest rates.

	Years ended December 31,					
	2012 vs. 2011			2011 vs. 2010		
	Increase (decrease) due to change in					
	Average volume	Average rate	Net	Average volume	Average rate	Net
	(in thousands)					
Interest Earned On:						
Interest bearing deposits in banks	$ (15)	$ -	$ (15)	$ 18	$ -	$ 18
Federal funds sold	(7)	-	(7)	(20)	-	(20)
Investment securities	276	(245)	31	184	(246)	(62)
Loans, net of unearned fees	1,512	(1,729)	(217)	277	(446)	(169)
Total Interest Income	1,766	(1,974)	(208)	459	(692)	(233)
Interest Paid On:						
NOW deposits	52	(13)	39	53	(93)	(40)
Savings deposits	158	(273)	(115)	3	(495)	(492)
Money market deposits	(29)	(159)	(188)	(102)	(272)	(374)
Time deposits	(196)	(150)	(346)	(31)	(55)	(86)
Securities sold under agreements to repurchase	12	(23)	(11)	13	(60)	(47)
Long-term debt	1	-	1	136	(53)	83
Total Interest Expense	(2)	(618)	(620)	72	(1,028)	(956)
Net Interest Income	$ 1,768	$ (1,356)	$ 412	$ 387	$ 336	$ 723

The change in interest due to both volume and rate has been allocated proportionally to both, based on their relative absolute values.

Provision for Loan Losses

Our provision for loan losses for the year ended December 31, 2012 was $1.4 million, as compared to $2.2 million for the year ended December 31, 2011. The decrease in our provision was primarily due to lesser allowance requirements for certain identified impaired loans partially offset by loan growth. The $1.4 million provision for 2012 was driven by a number of factors, including, our assessment of the current state of the economy, prolonged high levels of unemployment in our market, and allowances related to impaired loans and loan activity. The provision for the comparable 2011 period was driven by similar factors. The provision for loan losses is determined by an allocation process whereby an estimated allowance is allocated to the specific allowance for impaired loans and the general allowance for pools of loans. The allocation reflects management's assessment of economic conditions, credit quality and other risk factors inherent in the loan portfolio. The allowance for loan losses totaled $8.0 million, or 1.40% of total loans at December 31, 2012, compared to $7.3 million or 1.38% of total loans, at December 31, 2011. The increase of $674,000 in the allowance for loan losses is primarily due to the additional provision of $1.4 million recorded during 2012 and $190,000 in loan recoveries, partially offset by loan charge-offs and partial write-downs of $896,000.

In management's opinion, the allowance for loan losses, totaling $8.0 million at December 31, 2012, is adequate to cover losses inherent in the portfolio. In the current interest rate and credit quality environment, our prudent risk management philosophy has been to stay within our established credit culture. Management will continue to review the need for additions to our allowance for loan losses based upon its ongoing review of the loan portfolio and credit quality trends, the level of delinquencies as well as general market and economic conditions.

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Non-Interest Income

Non-interest income amounted to $2.6 million for the year ended December 31, 2012, compared to $2.3 million for the year ended December 31, 2011. This increase of $283,000, or 12.1%, was primarily due to an increase of $271,000 in fees generated by our residential mortgage department and an $86,000 increase in the gain on sale of SBA loans. Other increases included $62,000 in service fees on deposit accounts, higher bank-owned life insurance income of $87,000, resulting from increased purchases of such investments during the fourth quarter of 2011 and an increase of $45,000 in debit card fees. These increases were partially offset by a decrease of $206,000 in securities gains as well as an $80,000 credit loss on a pooled trust preferred security recorded in 2012 as compared to none in 2011. Management evaluates securities for other-than-temporary impairments at least on a quarterly basis, and more frequently when the economic and market concerns warrant such evaluations.

Non-Interest Expenses

The following table provides a summary of non-interest expenses by category for the years ended December 31, 2012 and 2011.

(dollars in thousands)	Years ended December 31, 2012	Years ended December 31, 2011	Increase (Decrease)	% Increase (Decrease)
Salaries and employee benefits	$ 10,915	$ 10,539	$ 376	3.6%
Occupancy and equipment	3,200	3,205	(5)	(0.2%)
Professional fees	754	851	(97)	(11.4%)
Advertising and marketing	270	225	45	20.0%
Data processing	748	641	107	16.7%
Insurance	345	390	(45)	(11.5%)
FDIC insurance and assessments	553	673	(120)	(17.8%)
Outside service fees	508	422	86	20.4%
Amortization of identifiable intangibles	163	201	(38)	(18.9%)
OREO expenses, OREO impairment and sales, net	699	270	429	158.9%
Loan workout expenses	240	166	74	44.6%
Other operating	1,452	1,510	(58)	(3.8%)
Total Non-Interest Expenses	$ 19,847	$ 19,093	$ 754	3.9%

Non-interest expenses for year ended December 31, 2012 increased $754,000, or 3.9%, compared to the year ended December 31, 2011. Salaries and employee benefits increased $376,000, or 3.6%, primarily due to higher residential mortgage commissions along with the hiring of additional key personnel as the Company continues to expand its lending division. Data processing increased $107,000, or 16.7%, primarily to due to costs resulting from our new headquarters facility and new Red Bank branch. Outside service fees increased $86,000, or 20.4% primarily due to increases in network processing charges and appraisal costs. OREO expenses, OREO impairment and sales, net, increased $429,000, or 158.9%, primarily due to a net loss of $197,000 from the sale of ten OREO properties in 2012 as compared to a net gain of $381,000 from the same period in 2011 resulting from the sale of six OREO properties. Additionally, $360,000 in impairment write-downs were recorded relating to two existing OREO properties in 2012 compared to $275,000 in 2011. OREO carrying expenses decreased $234,000 primarily due to decrease of OREO properties resulting from the sales in 2012. Loan workout expenses increased $74,000, or 44.6%, primarily due to the recapture of previously paid expenses during 2011. These increases were partially offset by a decrease in occupancy and equipment expense of $5,000, or 0.2%, primarily due to lower depreciation expense resulting from fully depreciated fixed assets partially offset by new branch and corporate headquarter expenses. Professional fees declined

$97,000, or 11.4%, for the year ended December 31, 2012, as compared to the same prior year period, primarily due to lower legal costs and auditing fees. Federal Deposit Insurance Corporation (“FDIC”) insurance and assessments decreased $120,000, or 17.8%, primarily due to the change in assessment calculation from a deposit based calculation to an asset based less Tier 1 capital calculation. Amortization of intangible assets, which was the result of The Town Bank acquisition in 2006, amounted to $163,000 during 2012 as compared to $201,000 in 2011. Other operating expense decreased $58,000, or 3.8%, primarily due to a $100,000 write-down on a property held for sale recorded in 2011.

Income Tax Expense

For the year ended December 31, 2012, the Company recorded $2.8 million in income tax expense, compared to $2.5 million for the year ended December 31, 2011. The effective tax rate for the year ended December 31, 2012 and 2011 was 36.8% and 37.1%, respectively.

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Financial Condition
December 31, 2012 Compared to December 31, 2011

Assets

At December 31, 2012, total assets were $733.9 million, an increase of $59.3 million, or 8.8% compared to total assets of $674.6 million at December 31, 2011. At December 31, 2012, total loans were $571.4 million, an increase of $41.3 million, or 7.8%, from the $530.1 million reported at December 31, 2011. Investment securities, including restricted stock, were $75.4 million at December 31, 2012 as compared to $62.8 million at December 31, 2011, an increase of $12.6 million, or 20.1%. At December 31, 2012, cash and cash equivalents totaled $48.5 million compared to $38.0 million at December 31, 2011, an increase of $10.5 million, or 27.6%, as our liquidity position continues to remain strong at December 31, 2012. Goodwill totaled $18.1 million at both December 31, 2012 and 2011.

Liabilities

Total deposits increased $52.9 million, or 9.6%, to $606.8 million at December 31, 2012, from $553.9 million at December 31, 2011. Deposits are the Company's primary source of funds. The deposit increase during 2012 was primarily attributable to the Company's strategic initiative to continue to grow market share through core deposit relationships. The Company anticipates continued loan demand increases during 2013 and beyond, and will depend on the expansion and maturation of the branch network as its primary funding source. As a secondary funding source, the Company intends to utilize borrowed funds, including brokered CD's, at opportune times during changing rate cycles. The Company continues to experience change in the mix of the deposit products through its branch sales efforts, which are targeted to gain market penetration. In order to fund future quality loan demand, the Company intends to raise the most cost-effective funding available within the market area.

Securities Portfolio

Investment securities, including restricted investments, totaled $75.4 million at December 31, 2012 compared to $62.8 million at December 31, 2011, an increase of $12.6 million, or 20.1%. Investment securities purchases amounted to $30.8 million, while repayments, calls and maturities amounted to $15.2 million. In 2012, there were six sales of securities available-for-sale totaling $2.9 million resulting in a gain on sale of $118,000 as compared to nine sales of securities available-for-sale totaling $4.0 million resulting in a gain on sale of $324,000 during 2011.

The Company maintains an investment portfolio to fund increased loans and liquidity needs (resulting from decreased deposits or otherwise) and to provide an additional source of interest income. The portfolio is composed of obligations of the U.S. Government agencies and U.S. Government-sponsored entities, municipal securities, corporate debt securities and a Community Reinvestment Act ("CRA") mutual fund. All of our mortgage-backed investment securities are collateralized by pools of mortgage obligations that are guaranteed by privately managed, U.S. Government-sponsored enterprises ("GSE"), such as Fannie Mae, Freddie Mac and Government National Mortgage Association. Due to these GSE guarantees, these investment securities are susceptible to less risk of non-performance and default than other corporate securities which are collateralized by private pools of mortgages. At December 31, 2012, the Company maintained $20.4 million of GSE residential mortgage-backed securities in the investment portfolio and $23.0 million of collateralized residential mortgage obligations, all of which are current as to payment of principal and interest and are performing to the terms set forth in their respective prospectuses.

Included within the Company's investment portfolio are trust preferred securities, which consists of four single issue securities and one pooled issue security. These securities have an amortized cost value of $3.0 million and a fair value of $2.3 million at December 31, 2012. The unrealized loss on these securities is related to general market conditions, the widening of interest rate spreads and downgrades in credit ratings. The single issue securities are from large money center banks. The pooled instrument consists of securities issued by financial institutions and insurance companies, and we hold the mezzanine tranche of such security. Senior tranches generally are protected from defaults by over-collateralization and cash flow default protection provided by subordinated tranches, with senior tranches having the greatest protection and mezzanine tranches subordinated to the senior tranches. For the pooled trust preferred security, management reviewed expected cash flows and credit support and determined it was not probable that all principal and interest would be repaid. In this pooled trust preferred security, there are 28 of 39 banks and insurance companies that are performing at December 31, 2012. The deferrals and defaults as a percentage of original collateral at December 31, 2012 was 29.2%. As the Company does not intend to sell this security and it is more likely than not that the Company will not be required to sell this security, the total other-than-temporary impairment on this security was $472,000 at December 31, 2012, of which $308,000 was determined to be a credit loss and charged to operations and $164,000 was determined to be non-credit related and included in the other comprehensive income component. There was an $80,000 other-than-temporary impairment charge to earnings during 2012, as compared to none for the same period in 2011. At December 31, 2012, the fair value of this pooled security was $28,000 and the amortized cost was $192,000.

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Management evaluates all securities for other-than-temporary impairment at least on a quarterly basis, and more frequently when economic and market concerns warrant such evaluations. As of December 31, 2012, all of these securities are current with their scheduled interest payments, with the exception of the one pooled trust preferred security with an amortized cost basis of $192,000 at December 31, 2012, which has been remitting reduced amounts of interest as some individual participants of the pool have deferred interest payments. Future deterioration in the cash flow of these instruments or the credit quality of the financial institution issuers could result in additional impairment charges in the future.

The Company accounts for its investment securities as available for sale or held to maturity. Management determines the appropriate classification at the time of purchase. Based on an evaluation of the probability of the occurrence of future events, we determine if we have the ability and intent to hold the investment securities to maturity, in which case we classify them as held to maturity. All other investments are classified as available for sale.

Securities classified as available for sale must be reported at fair value, with unrealized gains and losses excluded from earnings and reported as a separate component of shareholders' equity, net of taxes. Gains or losses on the sales of securities available for sale are recognized upon realization utilizing the specific identification method. The net effect of unrealized gains or losses, caused by marking our available for sale portfolio to fair value, could cause fluctuations in the level of shareholders' equity and equity-related financial ratios as changes in market interest rates cause the fair value of fixed-rate securities to fluctuate.

Securities classified as held to maturity are carried at cost, adjusted for amortization of premium and accretion of discount over the terms of the maturity in a manner that approximates the interest method.

The following table sets forth the carrying value of the securities portfolio as of December 31, 2012, 2011 and 2010 (in thousands).

	December 31,		
	2012	2011	2010
Investment securities available for sale at fair value:			
U.S. Government agency securities	$ -	$ 2,258	$ 5,786
Municipal securities	1,310	1,307	2,016
U.S. Government-sponsored enterprises ("GSE") - Residential mortgage-backed securities	20,374	21,878	16,251
Collateralized residential mortgage obligations	22,996	17,163	5,745
Corporate debt securities, primarily financial institutions	3,655	2,528	3,087
Community Reinvestment Act ("CRA") mutual fund	2,421	2,321	2,194
	$ 50,756	$ 47,455	$ 35,079
Investment securities held to maturity at amortized cost:			
Municipal securities	$ 17,799	$ 11,296	$ 8,522
GSE – Residential mortgage-backed securities	1,083	-	-
Collateralized residential mortgage obligations	892	-	-
Corporate debt securities, primarily financial institutions	1,812	1,809	2,307
	$ 21,586	$ 13,105	$ 10,829

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The contractual maturity distribution and weighted average yields, calculated on the basis of the stated yields to maturity, taking into account applicable premiums or discounts, of the securities portfolio at December 31, 2012 is set forth in the following table (excluding restricted stock and mutual fund). Securities available for sale are carried at amortized cost in the table for purposes of calculating the weighted average yield. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. There have been no tax equivalent adjustments made to the yields on tax-exempt securities.

December 31, 2012 (dollars in thousands)	Due within 1 year		Due 1 – 5 years		Due 5 – 10 years		Due after 10 years		Total
	Amortized cost	Wtd Avg Yield	Amortized cost	Wtd Avg Yield	Amortized cost	Wtd Avg Yield	Amortized cost	Wtd Avg Yield	Amortized cost
Investment securities available for sale:									
Municipal securities	$ -	-	$ -	-	$ 424	4.40%	$ 831	4.52%	$ 1,255
GSE - Residential mortgage-backed securities	-	-	74	6.48%	4,627	2.84%	15,180	2.94%	19,881
Collateralized residential mortgage obligations	-	-	-	-	1,470	2.25%	21,185	2.23%	22,655
Corporate debt securities, primarily financial institutions	-	-	1,791	2.65%	1,040	2.02%	1,186	1.38%	4,017
	$ -	-	$ 1,865	2.80%	$ 7,561	2.70%	$ 38,382	2.53%	$ 47,808
Investment securities held to maturity:									
Municipal securities	$ 9,032	0.81%	$ 1,922	3.78%	$ 4,967	3.85%	$ 1,878	4.68%	$ 17,799
GSE - Residential mortgage-backed securities	-	-	-	-	-	-	1,083	3.50%	1,083
Collateralized residential mortgage obligations	-	-	-	-	-	-	892	2.00%	892
Corporate debt securities primarily financial institutions	-	-	-	-	-	-	1,812	0.85%	1,812
	$ 9,032	0.81%	$ 1,922	3.78%	$ 4,967	3.85%	$ 5,665	2.81%	$ 21,586

Loan Portfolio

The following table summarizes total loans outstanding by loan category and amount on the dates indicated.

	December 31,					
	2012		2011		2010	
	Amount	Percent	Amount	Percent	Amount	Percent
	(in thousands, except for percentages)					
Commercial and industrial	$ 138,438	24.2%	$ 136,869	25.8%	$ 134,266	26.1%
Real estate - construction	83,755	14.6%	51,180	9.6%	33,909	6.6%

Real estate - commercial		288,060		50.4%		270,688		51.0%		262,996		51.2%
Real estate - residential		20,875		3.6%		19,201		3.6%		21,473		4.2%
Consumer		40,975		7.2%		52,853		10.0%		60,879		11.9%
Unearned fees		(656	)	0.0%		(661	)	0.0%		(529	)	0.0%
Total loans	$	571,447		100.0%	$	530,130		100.0%	$	512,994		100.0%

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	December 31,			
	2009		2008	
	Amount	Percent	Amount	Percent
	(in thousands, except for percentages)			
Commercial and industrial	$ 126,794	24.7%	$ 114,758	25.6%
Real estate - construction	74,133	14.4%	81,774	18.2%
Real estate - commercial	228,818	44.5%	177,650	39.6%
Real estate - residential	19,381	3.8%	19,860	4.4%
Consumer	64,723	12.6%	55,009	12.2%
Unearned fees	(450)	0.0%	(271)	0.0%
Total loans	$ 513,399	100.0%	$ 448,780	100.0%

Total loans, net of unearned fees, increased by $41.3 million, or 7.8%, to a new high of $571.4 million at December 31, 2012 compared to $530.1 million at December 31, 2011. While the overall economy has been restrictive and somewhat constrained by the fragile economic environment, our local economy seems to reflect some strengthening in certain sectors. However, we anticipate continued increased loan volume to be a major challenge for 2013, as we continue to target credit worthy customers. Adverse credit conditions have created a difficult environment for both borrowers and lenders. The low rate environment has created a higher than anticipated level of prepayments and payoffs by borrowers looking to deleverage portions of their business and personal debts. The mix of our loan composition at December 31, 2012 when compared to December 31, 2011 reflects our desire to emphasize commercial and industrial, real estate-commercial and real estate-construction. Within the loan portfolio, commercial real estate loans remained the largest component, constituting 50.4% of our total loans outstanding at December 31, 2012, down from 51.0% from the prior year. These loans increased by $17.4 million, or 6.4%, to $288.1 million at December 31, 2012, compared to $270.7 million at December 31, 2011. Commercial and industrial loans increased $1.5 million to $138.4 million at year-end 2012 compared to $136.9 million at year-end 2011, an increase of 1.1%, and comprised 24.2% of our portfolio, down from 25.8% for the prior year. Real estate construction loans increased by $32.6 million, or 63.6%, to $83.8 million at December 31, 2012, and comprised 14.6% of our total loans outstanding, up from 9.6% for the prior year. This increase is primarily due to increased draws on existing commercial real estate construction loans as well as new construction loans which required initial draws on projects. Residential real estate loans increase $1.7 million and comprised 3.6% of our total loan portfolio at both December 31, 2012 and 2011. Consumer loans decreased by $11.9 million or 22.5%, to $41.0 million at December 31, 2012 compared to $52.9 million at December 31, 2011, and comprised 7.2% of our 2012 loan portfolio compared to 10.0% for 2011.

The following table sets forth the aggregate maturities of commercial related loans, net of unearned discounts and deferred loan fees, in specified categories and the amount of such loans, which have fixed and variable rates as of December 31, 2012.

As of December 31, 2012	Due within 1 year	Due 1–5 years	Due after 5 years	Total
		(in thousands)		

Commercial and industrial	$	59,082	$	44,100	$	35,256	$	138,438
Real estate - construction		32,508		9,704		41,543		83,755
Real estate - commercial		17,291		32,671		238,098		288,060
Total	$	108,881	$	86,475	$	314,897	$	510,253
Fixed rate loans	$	27,328	$	61,644	$	42,704	$	131,676
Variable rate loans		81,553		24,831		272,193		378,577
Total	$	108,881	$	86,475	$	314,897	$	510,253

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Asset Quality

One of our key operating objectives has been, and continues to be, to maintain a high level of credit quality. We continually analyze our asset quality through a variety of strategies, we have been proactive in addressing problem and non-performing assets and management believes our allowance for loan losses are adequate to cover known and potential losses. These strategies, as well as our prudent maintenance of sound credit standards for new loan originations, have resulted in relatively low levels of non-performing loans. Our loan portfolio composition generally consists of loans secured by commercial real estate, development and construction of real estate projects in the Union and Monmouth counties, New Jersey. The Company has established a loan production office ("LPO") in the Union and Middlesex counties and has generated loans from these locations. We continue to have lending success and growth in the medical markets through our Private Banking Department. Since the latter part of 2008, the financial and capital markets have been faced with significant disruptions and volatility. The weakened economy has contributed to an overall challenge in building loan volume and we continue to be faced with declines in real estate values, which tend to reduce the collateral coverage of our existing loans. Efficient and effective asset-management strategies reflect the type and quality of assets being originated.

The Company's continues to be proactive in identifying troubled credits early, record charge-offs promptly based on current collateral values, and to maintain an adequate allowance for loan losses at all times. Our lending markets continue to be impacted by the continued weakness in the real estate and housing markets as well as the prolonged high unemployment rate. We closely monitor local and regional real estate markets and other factors related to risks inherent in our loan portfolio.

The Bank does not originate or purchase loans with payment options, negative amortization loans or sub-prime loans. We evaluate the classification of all our loans and the financial results of some of those loans may be adversely affected by changes in the prevailing economic conditions, either nationally or in our local Union, Middlesex and Monmouth County areas, including decreases in real estate values, adverse employment conditions, the monetary and fiscal policies of the federal and state government and other significant external events. For loans involved in a workout situation, a new or updated appraisal or evaluation, as appropriate, is ordered to address current project plans and market conditions that were considered in the development of the workout plan. The consideration include whether there has been material deterioration in the following factors: the performance of the project; conditions for the geographic market and property type; variances between actual conditions and original appraisal assumptions; changes in project specifications (e.g., changing a planned condominium project to an apartment building); loss of a significant lease or a take-out commitment; or increases in pre-sales fallout. A new appraisal may not be necessary in instances where an internal evaluation is used and appropriately updates the original appraisal assumptions to reflect current market conditions and provides an estimate of the collateral's fair value for impairment analysis.

Non-Performing Assets

Non-performing assets include loans that are not accruing interest (non-accrual loans) as a result of principal or interest being in default for a period of 90 days or more, loans past due 90 days or more and still accruing and other real estate owned, which consists of real estate acquired as the result of a defaulted loan. A loan is placed on non-accrual status when collection of all principal or interest is considered unlikely or when principal or interest is past due for 90 days or more, unless the loan is well-secured and the repayment of the debt or restoration to a current status will occur in the near term, in which case, the loan will continue to accrue interest. Any unpaid interest previously accrued on those loans is reversed from income. Interest income on other non-accrual loans is recognized only to the extent of interest payments received. During 2011, the Bank adopted Financial Accounting Standards Board ("FASB") – Receivables (Topic 310) guidance on determination of whether a restructuring is a troubled debt restructuring ("TDR"). The guidance was applicable to restructurings on or after January 1, 2011. A TDR is a loan in which the contractual terms have been modified resulting in the Bank granting a concession to a borrower who is experiencing financial difficulties in order for the Bank to have a greater opportunity of collecting the indebtedness from the borrower. Non-accruing TDRs are included in non-performing loans.

At December 31, 2012 and 2011, the Company had $7.5 million and $5.2 in non-accrual loans, respectively. All of the non-performing loans are secured by real estate. There was one loan totaling $1,800 past due 90 days or more and still accruing interest at December 31, 2012 as compared to no loans at December 31, 2011.

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The following table summarizes our non-performing assets for each of the five years in the period ended December 31, 2012. Total TDR's are broken out at the bottom portion of the table.

	Years ended December 31,				
(dollars in thousands)	2012	2011	2010	2009	2008
Non-Performing Assets:					
Non-Performing Loans:					
Commercial and industrial	$ 1,681	$ 2,349	$ 792	$ 4,719	$ 5,334
Real estate – construction	-	292	523	7,121	5,147
Real estate – commercial	3,542	145	605	-	-
Real estate – residential	263	263	-	-	-
Consumer	1,986	2,191	3,729	2,311	2,477
Total Non-Performing Loans	7,472	5,240	5,649	14,151	12,958
Loans Past Due 90 days or More and Still Accruing	2	-	-	-	-
Other Real Estate Owned	1,752	7,765	8,098	-	-
Total Non-Performing Assets	$ 9,226	$ 13,005	$ 13,747	$ 14,151	$ 12,958
Ratios:					
Non-Performing loans to total loans	1.31%	0.99%	1.10%	2.76%	2.89%
Non-Performing assets to total assets	1.26%	1.93%	2.16%	2.21%	2.27%
Troubled Debt Restructured Loans	$ 9,551	$ 7,579	$ 5,435	$ 4,717	$ -

Total non-performing loans increased by $2.2 million from December 31, 2011 to December 31, 2012. Eighteen loans comprise the $7.5 million of non-performing loans at December 31, 2012 compared to twelve loans which comprised the $5.2 million at December 31, 2011. At December 31, 2012, the Company believes it has a manageable level of non-performing loans, many of which are in the late stages of resolution.

Non-performing commercial and industrial loans decreased by $668,000 at December 31, 2012 due primarily to the settlement payoff of one loan totaling $517,000, wherein the Company received full principal including fees. Additionally, there was a full charge-off of one loan totaling $113,000 and a partial charge-off on one loan totaling $280,000, both of which were previously reserved for, the transfer of one loan to OREO totaling $335,000 which was subsequently sold during the second quarter 2012, in which the Company recorded a gain of $7,000 and a $60,000 principal pay-down on one loan. These decreases were partially offset by the addition of three loans totaling $637,000.

At December 31, 2012, non-performing real estate-construction loans decreased by $292,000 from December 31, 2011. The loan reported as of December 31, 2011 was taken into OREO via Deed-in-Lieu of foreclosure during the second quarter of 2012.

At December 31, 2012, non-performing real estate-commercial loans increased by $3.4 million from December 31, 2011. This increase is primarily due to two loans totaling $2.1 million, which are being actively pursued for collection, as well as two loans totaling $1.3 million, which the Company expects full resolution by year-end 2013.

At December 31, 2012, non-performing real estate-residential loans was unchanged at $263,000, from December 31, 2011.

Non-performing consumer loans decreased by $205,000 from December 31, due to the partial charge-off of $158,000 on one loan, which was previously reserved for and the pay-off including fees of two loans totaling $253,000.These decreases were partially offset by the addition of four loans totaling $208,000.

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At December 31, 2012, OREO balance decreased to $1.8 million as compared to $7.8 million at December 31, 2011. The decrease of $6.0 million is primarily due to the sale of ten OREO properties with a carrying value of $5.8 million, for which the Company recorded a net loss of $197,000 during 2012. Additionally, the Company recorded $360,000 in impairments on two existing OREO properties, primarily due to a decrease in collateral values which was supported by current appraisals. These decreases were partially offset by the addition of two OREO properties totaling $525,000 as well as $66,000 of capitalized construction costs. Our OREO balance at December 31, 2012 consists of three properties, with the largest OREO property totaling $800,000, which is a 23 acre parcel of land located in Middlesex County. The remaining $1.0 million is comprised principally of real estate construction and commercial properties.

Loans whose terms are modified are classified as troubled debt restructurings if the Company grants such borrowers concessions and it is deemed that those borrowers are experiencing financial difficulty. Concessions granted under a troubled debt restructuring generally involve a temporary reduction in interest rate or a modification of a loan's amortization schedule. Non-accrual troubled debt restructurings are restored to accrual status if principal and interest payments, under the modified terms, are current for six consecutive months after the modification is in place. Loans classified as troubled debt restructurings are designated as impaired. Modifications involving troubled borrowers may include a modification of a loan's amortization schedule, reduction in the stated interest rate and rescheduling of future cash flows.

The Company's troubled debt restructured modifications are typically made on short terms (12 month terms) in order to aggressively monitor and track performance. The short-term modifications performances are monitored for continued payment performance for an additional period of time after the expiration of the concession. Balance reductions and annualized loss rates are also important metrics that are monitored. The main objective of the modification programs is to reduce the payment burden for the borrower and improve the net present value of the Company's expected cash flows.

As of December 31, 2012, loans modified in a troubled debt restructuring totaled $9.6 million, including $5.9 million that are current, $3.0 million that are 30-59 days past due and $221,000 that are 60-89 days past due and one non-accrual loan totaling $476,000. All loans modified in a troubled debt restructuring as of December 31, 2012 were current at the inception of the modifications.

Potential Problem Loans

Overall credit quality in the portfolio remains strong even though the economic weakness has impacted several potential problem loans. Potential problem loans consist of special mention and substandard loans that continue to accrue interest. At December 31, 2012, the Company had $48.1 million in loans that were risk rated as special mention or substandard. This is an increase of approximately $12.0 million from year ended December 31, 2011, which totaled $36.1 million. The change in risk rated loans was attributable to certain loans which were downgraded due to a variety of changing conditions, including general economic conditions and/or conditions applicable to the specific borrower. All loans which were downgraded during 2012, are currently performing. It is believed that the remediation of a majority of these loans represented in the increase may warrant a risk rating upgrade at a point in the near future.

At December 31, 2012, other than the loans set forth above, the Company is not aware of any loans which present serious doubts as to the ability of its borrowers to comply with present loan repayment terms and which are expected to fall into one of the risk categories set forth in the description herein.

Allowance for Loan Losses

Analysis and Determination of the Allowance for Loan Losses

The allowance for loan losses is a valuation allowance for probable credit losses in the loan portfolio. We evaluate the need to establish allowances against losses on loans on a monthly basis and such allowances are reported to the Board of Directors on a quarterly basis. Through our prudent risk management practices, we continuously monitor the credit quality of our loan portfolio and maintain an allowance sufficient to absorb current probable and estimable losses inherent in our loan portfolio. We are committed to the timely recognition of problem loans and maintaining an appropriate and adequate allowance.

Our methodology for assessing the appropriateness of the allowance for loan losses consists of: (1) a specific allowance on impaired loans and (2) a general valuation allowance on the remainder of the loan portfolio. Although we determine the amount of each element of the allowance separately, the entire allowance for loan losses is available for the entire portfolio.

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As part of the allowance computation at December 31, 2012, the Company undertook a comprehensive review and inspection of all loans with collateral identified as being located within certain impact zones of Superstorm Sandy that impacted the region in October 2012. In the analysis, the Company reviewed a total of $26.1 million in loans, comprised of $20.4 million of commercial real estate and commercial and industrial loans, which represented 4.0% of this segment of the loan portfolio, $4.9 million of consumer loans, consisting primarily of home equity products, which represented 12.0% of this segment of the portfolio, and $800,000 of residential mortgage loans, which represented 4.0% of this segment of our portfolio. In total, the $26.1 million of identified loans represented 4.6% of the total loan portfolio. The Company evaluated the impact of the storm relative to the adequacy of the allowance for loan losses. Based on that evaluation, there were no loan charge-offs or specific losses identified at this time. Although the ultimate amount of loan losses relating to the storm is uncertain and difficult to predict, as information continues to be gathered, the Company recorded an additional provision for loan losses of $204,000 for the quarter and year ended December 31, 2012, solely related to the impact of the storm. Management continues to meet with clients, working with them in an effort to repair damages to their residences and businesses.

Specific Allowance Required for Impaired Loans

The first element of the allowance for loan loss analysis involves the estimation of allowance specific to individually evaluated impaired loans including restructured commercial and industrial, commercial and residential real estate, and consumer loans. In this process, a specific allowance may be established for impaired loans based on an analysis of the most probable sources of repayment, including discounted cash flows, liquidation of collateral, or the market value of the loan itself. Restructured consumer loans are also evaluated in this element of the estimate.

General Valuation Allowance on the Remainder of the Loan Portfolio

We establish a general allowance for non-impaired loans to recognize the inherent losses associated with lending activities. This general valuation allowance is determined by segregating the loans by loan category and assigning percentages to each category. The percentages are adjusted for significant factors that, in management’s judgment, affect the collectability of the portfolio as of the evaluation date. These significant factors include changes in existing general economic and business conditions affecting our primary lending areas and the national economy, staff lending experience, recent historical loss experience in particular segments of the portfolio, specific reserve and classified asset trends, delinquency trends and risk rating trends. These loss factors are subject to ongoing evaluation to ensure their relevance in the current economic environment.

Future adjustments to the allowance for loan losses account may be necessary due to economic, operating, regulatory and other conditions beyond our control. Our primary lending emphasis is the origination of loans secured by commercial and residential real estate in the greater central New Jersey area. The downturn and instability in the economy has affected our local markets, resulting in a slowdown in residential and commercial real estate sales. We are diligently working to address any asset quality concerns, including working with borrowers and increasing our allowance for loan losses when appropriate to ensure that we are well positioned for any losses that we may incur.

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The following table summarizes our allowance for loan losses for each of the five years in the period ended December 31.

	Years ended December 31,				
	2012	2011	2010	2009	2008
	(in thousands, except for percentages)				
Balance at beginning of year	$ 7,310	$ 6,246	$ 6,184	$ 6,815	$ 4,675
Provision charged to expense	1,380	2,205	3,100	2,205	2,301
Recoveries of loans charged off:					
Commercial and industrial	18	1	78	4	-
Real estate – construction	169	58	15	-	-
Consumer	3	52	-	-	-
Loans charged-off:					
Commercial and industrial	(552)	(482)	(1,061)	(526)	-
Real estate – construction	(59)	(82)	(1,420)	(2,012)	(158)
Real estate – residential	-	-	(150)	-	-
Consumer	(285)	(688)	(500)	(302)	(3)
Charge-offs, net	(706)	(1,141)	(3,038)	(2,836)	(161)
Balance of allowance at end of year	$ 7,984	$ 7,310	$ 6, 246	$ 6,184	$ 6,815
Ratio of net charge-offs to average loans outstanding	0.13%	0.22%	0.59%	0.59%	0.04
Balance of allowance at period-end as a percent of loans at year end	1.40%	1.38%	1.22%	1.20%	1.52%
Ratio of allowance at period-end to non-performing loans	106.85%	139.50%	110.57%	43.70%	52.59%

Allocation of the Allowance for Loan Losses

The following table sets forth the allocation of the allowance for loan losses by category of loans and the percentage of loans in each category to total loans for each of the five years in the period ended December 31, 2012.

	December 31,								
	2012			2011			2010		
		Percent of			Percent of			Percent of	
(dollars in thousands)	Amount	Allowance to total allowance	Loans to total loans	Amount	Allowance to total allowance	Loans to total loans	Amount	Allowance to total allowance	Loans to total loans
Balance applicable to :									
Commercial and industrial	$ 1,837	23.0%	24.2%	$ 2,448	33.5%	25.8%	$ 2,081	33.3%	26.1%

Real estate - construction	1,646	20.6%	14.6%	1,222	16.7%	9.6%	895	14.3%	6.6%
Real estate - commercial	3,367	42.2%	50.4%	2,412	33.0%	51.0%	2,193	35.1%	51.2%
Real estate - residential	217	2.7%	3.6%	256	3.5%	3.6%	276	4.4%	4.2%
Consumer	811	10.2%	7.2%	880	12.0%	10.0%	793	12.7%	11.9%
Unallocated	106	1.3%	0.0%	92	1.3%	0.0%	8	0.2%	0.0%
Total	$ 7,984	100.0%	100.0%	$ 7,310	100.0%	100.0%	$ 6,246	100.0%	100.0%

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	December 31, 2009			December 31, 2008		
		Percent of			Percent of	
(dollars in thousands)	Amount	Allowance to total allowance	Loans to total loans	Amount	Allowance to total allowance	Loans to total loans
Balance applicable to :						
Commercial and industrial	$ 1,974	31.9%	24.7%	$ 1,769	26.0%	25.6%
Real estate - construction	945	15.3%	14.4%	2,470	36.2%	18.2%
Real estate - commercial	2,495	40.4%	44.5%	1,617	23.8%	39.6%
Real estate - residential	126	2.0%	3.8%	146	2.1%	4.4%
Consumer	624	10.1%	12.6%	798	11.7%	12.2%
Unallocated	20	0.3%	0.0%	15	0.2%	0.0%
Total	$ 6,184	100.0%	100.0%	$ 6,815	100.0%	100.0%

The Company's allowance for loan losses was $8.0 million at December 31, 2012 and $7.3 million at December 31, 2011. The allowance for loan losses as a percentage of total loans at December 31, 2012 was 1.40%, compared with 1.38% at December 31, 2011. The Company had total provisions to the allowance for loan losses for the year ended December 31, 2012 in the amount of $1.4 million as compared to $2.2 million for the comparable period in 2011. Net charge-offs for the year ended December 31, 2012 were $706,000, compared to $1.1 million for the year ended December 31, 2011. All loans which the Company charged-off or had a direct write-down, had been previously identified and specific reserves were applied. Non-performing loans at December 31, 2012 are either well-collateralized or adequately reserved for in the allowance for loan losses.

Bank-Owned Life Insurance

In November 2004, the Company invested in $3.5 million of bank-owned life insurance as a source of funding for additional life insurance benefits for officers and employee benefit expenses related to the Company's non-qualified Supplemental Executive Retirement Plan ("SERP") for certain executive officers implemented in 2004 that provides for payments upon retirement, death or disability. In 2009, 2010 and 2011 the Company purchased an additional $3.5 million, $1.0 million and $3.5 million, respectively, of bank-owned life insurance in order to provide additional life insurance benefits for additional officers upon death or disability and to provide a source of funding for future enhancements of the benefits under the SERP. Expenses related to the SERP for year ended December 31, 2012 were approximately $214,000 as compared to $91,000 for the year ended December 31, 2011. Bank-owned life insurance involves our purchase of life insurance on a selected group of officers. The Company is the owner and beneficiary of the policies. Increases in the cash surrender values of this investment are recorded in other income in the statements of operations. Income on bank-owned life insurance amounted to $459,000 and $372,000, for years ended December 31, 2012 and 2011, respectively.

Premises and Equipment

Premises and equipment totaled $3.2 million and $2.6 million at December 31, 2012 and 2011, respectively. The $603,000, or 22.8%, increase in our investment in premises and equipment in 2012 compared to 2011 is due primarily to the normal recurring depreciation of existing assets of $680,000, partially offset by purchases made during the current year of $1.3 million.

Goodwill and Intangible Assets

Intangible assets totaled $18.4 million at December 31, 2012 compared to $18.5 million at December 31, 2011. The Company’s intangible assets at December 31, 2012 were comprised of $18.1 million of goodwill and $268,000 of core deposit intangibles, net of accumulated amortization of $1.8 million. At December 31, 2011, the Company’s intangible assets were comprised of $18.1 million of goodwill and $431,000 of core deposit intangibles, net of accumulated amortization of $1.7 million. During 2012, and 2011, the Company analyzed its goodwill for impairment and determined that there was no goodwill impairment. Accordingly, there was no impairment recorded during 2012 and 2011.

There can be no assurance that future testing will not result in additional material impairment charges due to further developments in the banking industry or our markets or otherwise. Additional goodwill discussion can be referenced in Note 5, “Goodwill and Other Intangible Assets”, in the Company’s financial statements.

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Deposits

Deposits are the primary source of funds used by the Company in lending and for general corporate purposes. In addition to deposits, the Company may derive funds from principal repayments on loans, the sale of loans and securities designated as available for sale, maturing investment securities and borrowings from financial intermediaries. The level of deposit liabilities may vary significantly and is dependent upon prevailing interest rates, money market conditions, general economic conditions and competition. The Company's deposits consist of checking, savings and money market accounts along with CD's and individual retirement accounts. Deposits are obtained from individuals, partnerships, corporations, unincorporated businesses and non-profit organizations throughout our market area. We attempt to control the flow of deposits primarily by pricing deposit offerings to be competitive with other financial institutions in the market area but not by necessarily offering the highest rate. The deposit growth experienced since the Company's inception is primarily due to the expansion and maturation of the branch system coupled with targeted sales efforts by our lending and branch personnel.

At December 31, 2012, total deposits amounted to $606.8 million, reflecting an increase of $52.9 million, or 9.6%, from December 31, 2011. Core checking deposits increased $59.1 million, or 40.0%, while savings accounts, inclusive of money market deposits, increased $7.8 million, or 2.7%. Conversely, higher cost CD's decreased $14.0 million, or 12.3%. The Bank has continued to focus on building non-interest bearing deposits, as this lowers the institution's cost of funds. Additionally, our savings accounts and other interest-bearing deposit products, excluding high-cost CD's, provide an efficient and cost-effective source to fund our loan originations.

One of the primary strategies is the accumulation and retention of core deposits. Core deposits consist of all deposits, except CD's in excess of $100,000. Core deposits at December 31, 2012 amounted to $562.5 million and accounted for 92.7% of total deposits as compared to $501.1 million and 90.5% of total deposits at December 31, 2011. During 2012, we continued to price our CD's $100,000 and over at rates that did not exceed our market competition. The balance of CD's $100,000 and over amounted to $44.2 million at December 31, 2012 compared to $52.8 million at December 31, 2011, a decrease of $8.6 million or 16.3%. During the first quarter of 2011, the Company placed $5.0 million in brokered CDs. The term on these CDs ranged from 54 to 66 months with interest rates ranging from 2.15% to 2.25%. During the first quarter of 2012, $3.5 million in brokered CDs were called and $2.7 million of new brokered CDs were placed at substantially lower rates for similar terms. During the second quarter of 2012, $2.1 million of additional brokered CDs were placed at 1.75% for a term of 84 months. At December 31, 2012, the Company has $6.3 million in brokered CDs, with rates ranging from 1.32% to 2.15% with original terms ranging from 54 to 84 months. The Company found this strategy was able to provide a more cost-effective source of longer-term funding as the rates paid for these brokered CDs were lower than current fixed rate term advances at the FHLB of New York.

The following table reflects the average balances and average rates paid on deposits for the years ended December 31, 2012, 2011 and 2010.

	Years ended December 31,					
	2012		2011		2010	
(dollars in thousands)	Average Balance	Average Rate	Average Balance	Average Rate	Average Balance	Average Rate
Non-interest bearing demand	$ 96,967	-	$ 86,687	-	$ 78,052	-
Interest-bearing demand (NOW)	69,063	0.43%	57,378	0.45%	48,638	0.61%
Savings deposits	217,879	0.74%	199,641	0.86%	199,380	1.11%
Money market deposits	83,140	0.38%	88,095	0.58%	99,659	0.89%
Time deposits	106,012	1.75%	116,331	1.89%	117,946	1.94%

Total	$	573,061	0.71%	$	548,132	0.85%	$	543,675	1.05%

The following table sets forth a summary of the maturities of certificates of deposit $100,000 and over at December 31, 2012 (in thousands).

		December 31, 2012
Due in three months or less	$	10,755
Due over three months through twelve months		13,883
Due over one year through three years		17,394
Due over three years		2,197
Total certificates of deposit $100,000 and over	$	44,229

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Borrowings

The Bank utilizes its account relationship with Atlantic Central Bankers Bank to borrow funds through its Federal funds borrowing line in an aggregate amount up to $10.0 million. The Bank also established a $7.0 million credit facility with another correspondent bank during the first quarter of 2011. These borrowings are priced on a daily basis. The Bank also has a remaining borrowing capacity with the Federal Home Loan Bank of New York (“FHLB”) of approximately $38.9 million based on the current loan collateral pledged of $52.4 million at December 31, 2012.

Short-term borrowings consist of Federal funds purchased and short-term borrowings from the FHLB. At December 31, 2012, 2011 and 2010, the Company had no short-term borrowings outstanding.

Long-term debt consisted of the following FHLB fixed rate advances at December 31:

(dollars in thousands)	At December 31,			Rate	Original Term	Maturity
Long-term debt:	2012	2011	2010			
Fixed Rate Note	$ 7,500	$ 7,500	$ 7,500	3.97%	10 years	November 2017
Fixed Rate Note	1,500	1,500	1,500	1.67%	4 years	August 2014
Fixed Rate Note	1,500	1,500	1,500	2.00%	5 years	August 2015
Fixed Rate Note	1,500	1,500	1,500	2.41%	6 years	August 2016
Fixed Rate Note	1,500	1,500	1,500	2.71%	7 years	August 2017
	$ 13,500	$ 13,500	$ 13,500	3.18%		

Repurchase Agreements

Securities sold under agreements to repurchase, which are classified as secured borrowings, generally mature within one to four days from the transaction date. Securities sold under agreements to repurchase are reflected as the amount of cash received in connection with the transaction. The Company may be required to provide additional collateral based on the fair value of the underlying securities.

Repurchase agreements are summarized as follows:

(dollars in thousands)	Years ended December 31, 2012	2011	2010
Repurchase agreements:			
Balance at year-end	$ 16,710	$ 16,218	$ 14,857
Average during the year	18,266	16,593	15,367
Maximum month-end balance	19,860	19,524	17,532
Weighted average rate during the year	0.59%	0.71%	1.07%
Weighted average rate at year end	0.52%	0.55%	0.81%

Liquidity

Liquidity defines our ability to generate funds to support asset growth, meet deposit withdrawals, maintain reserve requirements and otherwise operate on an ongoing basis. An important component of an institution’s asset and liability management structure is the level of liquidity which is available to meet the needs of its customers and requirements of creditors. Our liquidity needs are primarily met by cash on hand, Federal funds sold, maturing investment securities and short-term borrowings on a temporary basis. We invest the funds not needed to meet our cash requirements in overnight Federal funds sold and an interest bearing account with the Federal Reserve Bank of New York. With adequate deposit inflows over the past year coupled with the above-mentioned cash resources, we believe the level of short-term assets are sufficient to meet our liquidity needs. Our liquidity can be affected by a variety of factors, including general economic conditions, market disruption, operational problems affecting third parties or us, unfavorable pricing, competition, our credit rating and regulatory restrictions.

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At December 31, 2012, the Company had $48.5 million in cash and cash equivalents as compared to $38.0 million at December 31, 2011. Cash and cash equivalent balances consisted of $33.2 million and $30.4 million held at the Federal Reserve Bank of New York at December 31, 2012 and December 31, 2011, respectively. It was determined by management during 2010, to transfer most of the Bank's investable funds out of the Federal funds sold position and into the interest bearing deposit account at the Federal Reserve Bank of New York due to primarily to a higher rate of return, which averaged approximately 10 basis points higher. During the second quarter of 2011, the remaining $7.0 million in Federal funds sold was transferred to the Federal Reserve Bank of New York primarily due to the above-mentioned reasons. Additionally, balances at the Federal Reserve Bank of New York provided the highest level of safety for our investable funds. At December 31, 2012 and 2011, there were no Federal funds sold.

Off-Balance Sheet Arrangements

Our financial statements do not reflect off-balance sheet arrangements that we enter into with our customers in the normal course of business. These off-balance sheet arrangements consist of unfunded loans and letters of credit made under the same standards as on-balance sheet instruments. These instruments have fixed maturity dates, and because many of them will expire without being drawn upon, they do not generally present any significant liquidity risk to the Company.

Management believes that any amounts actually drawn upon these commitments can be funded in the normal course of operations. The following table sets forth our off-balance sheet arrangements as of December 31, 2012.

	December 31,	
	2012	2011
	(dollars in thousands)	
Home equity lines of credit	$ 26,415	$ 27,524
Commitments to fund commercial real estate and construction loans	50,032	72,409
Commitments to fund commercial and industrial loans	46,458	56,272
Commercial and financial letters of credit	4,195	5,066
	$ 127,100	$ 161,271

Capital

Shareholders' equity increased by $4.9 million, or 5.6%, to $92.0 million at December 31, 2012 compared to $87.1 million at December 31, 2011. Net income for 2012 added $4.8 million to shareholders' equity. Additionally, stock based compensation expense of $183,000, options exercised of $124,000, net unrealized gains on securities available for sale, net of tax, of $106,000, all contributed to the increase. These increases were partially offset by decreases of $448,000 relating to dividends on the preferred stock Series C.

The Bank is required to maintain cash reserve balances with the Federal Reserve Bank. The total of such reserves was $50,000 at December 31, 2012.

The Company (on a consolidated basis) and the Bank are subject to various regulatory and capital requirements administered by the Federal banking agencies. Our Federal banking regulators, the Board of Governors of the Federal Reserve System (which regulates bank holding companies) and the FDIC (which regulates the Bank), have issued guidelines classifying and defining capital. Failure to meet the minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on our consolidated financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company and the Bank must meet specific capital guidelines that involve quantitative measures of their assets, liabilities and certain off-balance sheet items as calculated under regulatory accounting practices. The capital amounts and classification of the Company and the Bank are also subject to qualitative judgments by the regulators about components, risk-weightings and other factors.

Quantitative measures established by regulations to ensure capital adequacy require the Company and the Bank to maintain minimum amounts and ratios set forth in the following tables of Tier 1 Capital to Average Assets (“Leverage Ratio”), Tier 1 Capital to Risk Weighted Assets, and Total Capital to Risk Weighted Assets. Management believes that, as of December 31, 2012, that the Company and the Bank meet all capital adequacy requirements to which they are subject.

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As of December 31, 2012, the Bank met all regulatory requirements for classification as well-capitalized under the regulatory framework for prompt corrective action. Management believes that there are no conditions or events that have changed the Bank's categories.

Community Partners (on a consolidated basis) and the Bank's actual capital amounts and ratios at December 31, 2012 and 2010 and the minimum amounts and ratios required for capital adequacy purposes and to be well capitalized under the prompt corrective action provisions are as follows:

	Actual		For Capital Adequacy Purposes		To be Well Capitalized under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
	(dollars in thousands, except for percentages)					
As of December 31, 2012						
Total capital (to risk-weighted assets)						
Community Partners Bancorp	$ 80,835	13.28%	$ >48,696	>8.00%	$ N/A	N/A
Two River Community Bank	80,773	13.27%	>48,695	>8.00%	>60,869	>10.00%
Tier 1 capital (to risk-weighted assets)						
Community Partners Bancorp	73,220	12.03%	>24,346	>4.00%	N/A	N/A
Two River Community Bank	73,159	12.02%	>24,346	>4.00%	>36,519	>6.00%
Tier 1 capital (to average assets)						
Community Partners Bancorp	73,220	10.36%	>28,270	>4.00%	N/A	N/A
Two River Community Bank	73,159	10.35%	>28,274	>4.00%	>35,343	>5.00%
As of December 31, 2011						
Total capital (to risk-weighted assets)						
Community Partners Bancorp	$ 75,444	13.26%	$ >45,517	>8.00%	$ N/A	N/A
Two River Community Bank	75,340	13.25%	>45,488	>8.00%	>56,860	>10.00%
Tier 1 capital (to risk-weighted assets)						
	68,332	12.01%	>22,758	>4.00%	N/A	N/A

Community Partners Bancorp						
Two River Community Bank	68,229	12.00%	>22,743	>4.00%	>34,115	>6.00%
Tier 1 capital (to average assets)						
Community Partners Bancorp	68,332	10.39%	>26,307	>4.00%	N/A	N/A
Two River Community Bank	68,229	10.38%	>26,292	>4.00%	>32,866	>5.00%

The Bank is subject to certain legal and regulatory limitations on the amount of dividends that it may declare without prior regulatory approval. Under Federal Reserve regulations, the Bank is limited as to the amount that it may lend affiliates, including the Company, unless such loans are collateralized by specific obligations.

The prompt corrective action regulations define specific capital categories based upon an institution's capital ratios. The capital categories in descending order are "well capitalized", "adequately capitalized", "undercapitalized", "significantly undercapitalized", and "critically undercapitalized." Institutions categorized as "undercapitalized" or lower are subject to certain restrictions, are not able to pay dividends and management fees, are restricted on asset growth and executive compensation and are subject to increased supervisory monitoring, among other matters. The regulators may impose other restrictions. Once an institution becomes "critically undercapitalized," it must be placed in receivership or conservatorship within 90 days. To be considered "adequately capitalized," an institution must generally have Tier 1 capital to total asset ratio of at least 4%, a Tier 1 risk-based capital ratio of at least 4%, and a total risked based capital ratio of at least 8%. An institution is deemed to be "critically undercapitalized" if it has a tangible equity ratio, Tier 1 capital, net of all intangibles, to tangible capital of 2% or less.

Under the risk-based capital guideline regulations, a banking organization's assets and certain off balance sheet items are classified into categories, with the least capital required for the category deemed to have the least risk, and the most capital required for the category deemed to have the most risk. Under current regulations, banking organizations are required to maintain total capital of 8.00% of risk weighted assets, of which 4.00% must be in core or Tier 1 capital.

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On July 26, 2012, the Company filed a shelf Registration Statement on Form S-3 with the Securities and Exchange Commission (SEC). This Registration Statement was declared effective by the SEC on August 6, 2012. The filing of the Registration Statement does not require the Company to issue any securities. The Registration Statement will allow the Company the flexibility to offer and sell, from time to time, in one or more public offerings, up to a total aggregate of $30 million of its common stock, preferred stock, debt securities, or warrants, either separately or together. The debt securities, preferred stock and warrants may be convertible or exercisable or exchangeable for other debt or equity securities of the Company. We will provide the specific terms of the securities offered in one or more supplements to the prospectus contained in the Registration Statement.

We intend to use the net proceeds from the sale of the securities registered by this Registration Statement for general corporate purposes. General corporate purposes may include, among other purposes, contribution to the capital of the Bank to support its lending and investing activities; the repayment of our debt; redemption of our outstanding Series C Preferred Stock; to support or fund acquisitions of other institutions or branches, if opportunities for such transactions become available; and investments in activities that are permitted for bank holding companies. We may temporarily invest funds that we do not immediately need for these purposes in investment securities or use them to make payments on our borrowings. The applicable prospectus supplement will provide details on the use of proceeds of any specific offering.

Federal banking regulators have proposed revisions to the bank capital requirement standards known as Basel III. Basel III strengthens bank capital requirements and introduces new regulatory requirements on bank liquidity and bank leverage. Based on the Company’s current understanding of these proposed regulations, as of December 31, 2012, each of the Company and the Bank anticipates being classified as well-capitalized under the proposed regulation upon finalization and implementation of the Basel III requirements. However, there is still need for clarification of Basel III as well as interpretation and implementation by federal banking regulators, so the ultimate impact of Basel III on the Company is not completely known at this point. On November 9, 2012, federal banking regulators provided guidance that they did not expect Basel III to become effective on January 1, 2013 and will take into account operational and other considerations when determining appropriate implementation dates and associated transition periods. No substitute date of effectiveness has been given.

Interest Rate Risk

Interest rate risk management involves managing the extent to which interest-sensitive assets and interest-sensitive liabilities are matched. Interest rate sensitivity is the relationship between market interest rates and earnings volatility due to the re-pricing characteristics of assets and liabilities. Our net income is affected by changes in the level of market interest rates. In order to maintain consistent earnings performance, we seek to manage, to the extent possible, the re-pricing characteristics of our assets and liabilities.

The management of and authority to assume interest rate risk is the responsibility of the ALCO, which is comprised of senior management and board members. The primary objective of Asset/Liability management is to establish prudent risk management guidelines and to coordinate balance sheet composition with interest rate risk management to sustain a reasonable and stable net interest income throughout various interest rate cycles. We have policies and practices for measuring and reporting interest rate risk exposure, through analysis of the net interest margin, gap position, simulation testing, liquidity ratios and the Economic Value of Portfolio Equity. In addition, we annually review our interest rate risk policy, which includes limits on the impact to earnings from shifts in interest rates.

Gap Analysis

To manage our interest sensitivity position, an asset/liability model called “gap analysis” is used to monitor the difference in the volume of our interest-sensitive assets and liabilities that mature or re-price within given periods. The ratio between assets and liabilities re-pricing in specific time intervals is referred to as an interest rate sensitivity gap. A positive gap (asset-sensitive) indicates that more assets re-price during a given period compared to liabilities, while a negative gap (liability-sensitive) has the opposite effect. During a period of falling interest rates, a positive gap would tend to adversely affect net interest income, while a negative gap would tend to result in an increase in net interest income. During a period of rising interest rates, a positive gap would tend to result in an increase in net interest income, while a negative gap would tend to affect net interest income adversely. We employ net interest income simulation modeling to assist in quantifying interest rate risk exposure. This process measures and quantifies the impact on net interest income through varying interest rate changes and balance sheet compositions. The use of this model assists the ALCO to gauge the effects of the interest rate changes on interest-sensitive assets and liabilities in order to determine what impact these rate changes will have upon the net interest spread.

As of December 31, 2012, the Company’s six month cumulative gap was -12.1% of total assets, or a negative $88.8 million, while its one-year cumulative gap was -2.7% of total assets, or $19.8 million, which is within the ALCO policy guideline of +/-25%.

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Simulation Modeling

We use a simulation model to analyze net interest income sensitivity to movements in interest rates. The simulation model projects net interest income based on various interest rate scenarios over a twelve and twenty-four month period. The model is based on the actual maturity and re-pricing characteristics of rate sensitive assets and liabilities. The model incorporates certain assumptions which management believes to be reasonable regarding the impact of changing interest rates and the prepayment assumptions of certain assets and liabilities as of December 31, 2012. The model assumes changes in interest rates without any proactive change in the composition or size of the balance sheet by management. In the model, the forecasted shape of the yield curve remains static as of December 31, 2012.

Our simulation model is based on market interest rates and prepayment speeds prevalent in the market as of December 31, 2012. The model utilizes an immediate parallel shift in the market interest rates at December 31, 2012. As of December 31, 2012 and 2011, the results of the simulation model were within guidelines prescribed by the ALCO policy. If model results were to fall outside prescribed ranges, action would be required by ALCO.

	Gradual change in interest rates				
December 31, 2012	200 basis point increase		200 basis point decrease		
(dollars in thousands)	Dollar change	Percent of change	Dollar change	Percent of change	ALCO Policy Guideline
Twelve month horizon:					
Net interest income change	$ (774)	-3.0%	$ (573)	-2.2%	-10.0%

	Gradual change in interest rates				
December 31, 2011	200 basis point increase		200 basis point decrease		
(dollars in thousands)	Dollar change	Percent of change	Dollar change	Percent of change	ALCO Policy Guideline
Twelve month horizon:					
Net interest income change	$ (817)	-3.2%	$ (338)	-1.3%	-6.0%

The assumptions used in the net interest income simulation are inherently uncertain. Actual results may differ significantly from those presented in the table above, due to the frequency and timing of changes in interest rates, and changes in spreads between maturity and re-pricing categories. Overall, our net interest income is affected by changes in interest rates and cash flows from our loan and investment portfolios. We actively manage these cash flows in conjunction with our liability mix, duration and interest rates to optimize the net interest income, while structuring the balance sheet in response to actual or potential changes in interest rates.

Additionally, our net interest income is impacted by the level of competition within our market place. Competition can negatively impact the level of interest rates attainable on loans and increase the cost of deposits, which may result in downward pressure on our net interest margin in future periods. Other factors, including, but not limited to, the slope of the yield curve and projected cash flows will impact our net interest income results and may increase or decrease the level of asset sensitivity of our balance sheet.

Economic Value of Equity

To measure the impact of longer-term asset and liability mismatches beyond two years, the Company utilizes Economic Value of Portfolio Equity (“EVPE”) models. EVPE considers the entire maturity spectrum of the Bank’s balance sheet, thereby providing a longer term measure of interest rate risk. The underlying economic value of the Bank’s assets, liabilities and off balance sheet instruments is affected by changes in interest rates. These changes occur because the present value of future cash flows and in some cases, the cash flows themselves, are affected by interest rate changes. The combined effects of the changes in these present values reflect the change in the Bank’s underlying economic value.

In addition to providing a longer-term measurement of interest rate risk, the economic value of equity measurement may highlight the impact of current interest rate changes that may not be accounted for in simulation analysis. In addition, a decline in the economic value of equity may indicate below market returns in the future. Because of balance sheet optionality, an EVPE analysis is used to dynamically model the present value of asset and liability cash flows, with rates ranging up or down 200 basis points. Our analysis of EVPE excludes goodwill and includes only tangible equity. The economic value of equity is likely to be different as interest rates change. Results falling outside prescribed ranges require action by the ALCO.

At December 31, 2012 and 2011, the Company’s variance in the EVPE as a percentage of change from book value of tangible equity compared to no change in interest rates, and to an instantaneous and sustained parallel shift of + or - 200 basis points, is within the Company’s policy guidelines as presented below.

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Economic Value of Portfolio Equity

December 31, 2012

Change in Interest Rates (dollars in thousands)	Base Case (0 bp)	-200bp	+200bp	ALCO Policy Guideline
Economic Value of Equity	$85,997	$ 76,448	$ 84,256	
$ Change		(9,549)	(1,741)	
% Change to Present Value of Equity		-11.1%	-2.0%	-25.0%

December 31, 2011

Change in Interest Rates (dollars in thousands)	Base Case (0 bp)	-200bp	+200bp	ALCO Policy Guideline
Economic Value of Equity	$79,322	$ 69,763	$ 78,345	
$ Change		(9,559)	(977)	
% Change to Present Value of Equity		-12.0%	-1.2%	-25.0%

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

Not required.

Item 8. Financial Statements and Supplementary Data.

Reference is made to Item 15(a)(1) and (2) to page F-1 for a list of financial statements and supplementary data required to be filed pursuant to this Item 8. The information required by this Item 8 is provided beginning on page F-1 hereof.

Item 9. Changes In and Disagreements with Accountants on Accounting and Financial Disclosure.

None.

Item 9A. Controls and Procedures.

The Company has established disclosure controls and procedures designed to ensure that information required to be disclosed in the reports that the Company files or submits under the Securities Exchange Act of 1934, as amended (the “Exchange Act”) is recorded, processed, summarized, and reported within the time periods specified in SEC rules and forms and is accumulated and communicated to management, including the principal executive officer and principal financial officer, to allow timely decisions regarding required disclosure.

The Company’s principal executive officer and its principal financial and accounting officer, with the assistance of other members of the Company’s management, have evaluated the effectiveness of the design and operation of the Company’s disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of the end of the period covered by this annual report. Based upon such evaluation, the Company’s principal executive officer and principal financial and accounting officer have concluded that the Company’s disclosure controls and procedures are effective as of the end of the period covered by this annual report.

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The Company's principal executive officer and principal financial officer have also concluded that there was no change in the Company's internal control over financial reporting (as such term is defined in Rule 13a-15(f) under the Exchange Act) that occurred during the quarter ended December 31, 2012 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

Management's Report on Internal Control over Financial Reporting

Management of the Company is responsible for establishing and maintaining adequate internal control over financial reporting, as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act and for complying with laws and regulations relating to safety and soundness that are designated by the FDIC and the Federal Reserve. The Company's internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and preparation of financial statements for external purposes in accordance with accounting principles generally accepted in the United States of America.

There are inherent limitations in the effectiveness of any internal control, including the possibility of human error and circumvention or overriding of controls. Accordingly, even effective internal control or compliance with banking laws can provide only reasonable assurance with respect to financial statement preparation. Further, because of changes in conditions, the effectiveness of internal control and compliance with banking laws may vary over time.

The Company's management assessed the effectiveness of the Company's internal control over financial reporting and its compliance with laws and regulations relating to safety and soundness that are designated by the FDIC and the Federal Reserve as of December 31, 2012. In making this assessment, management used the criteria set forth in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO"). Based on their assessment using those criteria, management concluded that, as of December 31, 2012, the Company's internal control over financial reporting and its compliance with laws and regulations relating to safety and soundness that are designated by the FDIC and the Federal Reserve was effective.

This annual report does not include an attestation report of the Company's Independent Registered Public Accounting Firm regarding internal control over financial reporting. Management's report was not subject to attestation by the Company's Independent Registered Public Accounting Firm pursuant to the Dodd-Frank Act.

/s/ WILLIAM D. MOSS		/s/ A. RICHARD ABRAHAMIAN	
Name:	William D. Moss	Name:	A. Richard Abrahamian
Title:	President and Chief Executive Officer	Title:	Executive Vice President and Chief Financial Officer
Date:	March 29, 2013	Date:	March 29, 2013

Item 9B. Other Information.

In March 2013, the Company filed the requisite applications to close its existing smaller branch in Red Bank as well as its Cliffwood branch. Management believes that the closure of both offices is in line with the strategic plans of optimizing the profitability of its branch network. The Company expects a minimal loss of customer relationships due to these closures and anticipates annual pre-tax expense savings of approximately $290,000. Both branches are expected to close in June 2013.

PART III

Item 10. Directors, Executive Officers and Corporate Governance.

The information required by this item is incorporated by reference from the Company's Proxy Statement for its 2013 Annual Meeting of Shareholders under the captions "Directors and Executive Officers," "Corporate Governance," "Compliance with Section 16(a) of the Exchange Act," "Code of Ethics" and "Audit Committee."

Item 11. Executive Compensation.

The information required by this item is incorporated by reference from the Company's Proxy Statement for its 2013 Annual Meeting of Shareholders under the caption "Executive Compensation."

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Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Shareholder Matters.

Equity Compensation Plan Information

The following table provides information about the Company's common stock that may be issued upon the exercise of options, warrants and rights under all of the Company's equity compensation plans as of December 31, 2012. The information in the table has been adjusted for all subsequent stock dividends.

Plan category	Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)	Weighted-average exercise price of outstanding options, warrants and rights (b)	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c)
Equity compensation plans approved by security holders	921,605	$ 6.95	245,504 (1)
Equity compensation plans not approved by security holders	-0-	N/A	-0-
Total	921,605	$ 6.95	245,504

(1) The Company may issue these shares pursuant to options and restricted stock awards.

The additional information required by this item is incorporated by reference from the Company's Proxy Statement for its 2013 Annual Meeting of Shareholders under the caption "Stock Ownership of Management and Principal Shareholders."

Item 13. Certain Relationships and Related Transactions, and Director Independence.

The information required by this item is incorporated by reference from the Company's Proxy Statement for its 2013 Annual Meeting of Shareholders under the captions "Certain Transactions With Management" and "Director Independence."

Item 14. Principal Accountant Fees and Services.

The information regarding principal accounting fees and services and the Company's pre-approval policies and procedures for audit and non-audit services provided by the Company's independent registered public accounting firm is incorporated by reference from the Company's Proxy Statement for its 2013 Annual Meeting of Shareholders under the caption "Principal Accountant Fees and Services."

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PART IV

Item 15. Exhibits and Financial Statement Schedules.

(a) Financial Statements and Financial Statement Schedules

The following documents are filed as part of this report:

1. Financial Statements of Community Partners Bancorp

Report of Independent Registered Public Accounting Firm

Consolidated Balance Sheets – December 31, 2012 and 2011

Consolidated Statements of Operations – Years Ended December 31, 2012 and 2011

Consolidated Statements of Comprehensive Income – Years Ended December 31, 2012 and 2011

Consolidated Statements of Shareholders' Equity – Years Ended December 31, 2012 and 2011

Consolidated Statements of Cash Flows – Years Ended December 31, 2012 and 2011

Notes to Consolidated Financial Statements

2. All schedules are omitted because either they are inapplicable or not required, or because the information required therein is included in the Consolidated Financial Statements and Notes thereto.

3. See accompanying Index to Exhibits.

(b) Exhibits

Exhibits required by Section 601 of Regulation S-K (see accompanying Index to Exhibits).

(c) Financial Statement Schedules

See the Notes to the Consolidated Financial Statements included in this report.

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COMMUNITY PARTNERS BANCORP

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

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Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders
of Community Partners Bancorp
Tinton Falls, New Jersey

We have audited the accompanying consolidated balance sheets of Community Partners Bancorp and subsidiaries (the Company) as of December 31, 2012 and 2011, and the related consolidated statements of operations, comprehensive income, shareholders' equity and cash flows for the years then ended. The Company's management is responsible for these consolidated financial statements. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company 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 Community Partners Bancorp and its subsidiaries as of December 31, 2012 and 2011, and the results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

/s/ ParenteBeard LLC

ParenteBeard LLC
Clark, New Jersey
March 29, 2013

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Community Partners Bancorp

Consolidated Balance Sheets

	December 31, 2012	2011
	(In Thousands, Except Share Data)	
Assets		
Cash and due from banks	$ 15,349	$ 7,597
Interest-bearing deposits in bank	33,197	30,425
Cash and Cash Equivalents	48,546	38,022
Securities available for sale	50,756	47,455
Securities held to maturity (fair value of $21,935 and $13,222 at December 31, 2012 and December 31, 2011, respectively)	21,586	13,105
Restricted investments, at cost	3,040	2,237
Loans	571,447	530,130
Allowance for loan losses	(7,984)	(7,310)
Net Loans	563,463	522,820
Other real estate owned	1,752	7,765
Bank-owned life insurance	13,457	12,998
Premises and equipment, net	3,243	2,640
Accrued interest receivable	1,884	1,928
Goodwill	18,109	18,109
Other intangible assets, net of accumulated amortization of $1,838 and $1,675 at December 31, 2012 and December 31, 2011, respectively	268	431
Other assets	7,791	7,044
Total Assets	$ 733,895	$ 674,554
Liabilities		
Deposits:		
Noninterest-bearing	$ 112,746	$ 88,209
Interest-bearing	494,024	465,703
Total Deposits	606,770	553,912
Securities sold under agreements to repurchase	16,710	16,218
Accrued interest payable	70	107
Long-term debt	13,500	13,500
Other liabilities	4,880	3,683
Total Liabilities	641,930	587,420
Shareholders' Equity		
Preferred stock, no par value; 6,500,000 shares authorized;		
Preferred stock, Series B, none issued or outstanding	-	-

Preferred stock, Series C, $12,000,000 liquidation preference; 12,000 shares authorized; 12,000 issued and outstanding at December 31, 2012 and December 31, 2011, respectively	12,000	12,000
Common stock, no par value; 25,000,000 shares authorized; 7,983,778 and 7,942,218 shares issued and outstanding at December 31, 2012 and December 31, 2011, respectively	71,537	71,179
Retained earnings	8,060	3,693
Accumulated other comprehensive income	368	262
Total Shareholders' Equity	91,965	87,134
Total Liabilities and Shareholders' Equity	$ 733,895	$ 674,554

See notes to consolidated financial statements.

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Community Partners Bancorp

Consolidated Statements of Operations

	Years Ended December 31, 2012	2011
	(In Thousands, Except Per Share Data)	
Interest Income		
Loans, including fees	$ 29,192	$ 29,409
Securities:		
Taxable	1,167	1,170
Tax-exempt	398	364
Federal funds sold and interest bearing deposits	81	103
Total Interest Income	30,838	31,046
Interest Expense		
Deposits	4,077	4,687
Securities sold under agreements to repurchase	107	118
Borrowings	434	433
Total Interest Expense	4,618	5,238
Net Interest Income	26,220	25,808
Provision for Loan Losses	1,380	2,205
Net Interest Income after Provision for Loan Losses	24,840	23,603
Non-Interest Income		
Total other-than-temporary impairment losses	(85)	-
Less: Portion included in other comprehensive income (pre-tax)	5	-
Net other-than-temporary impairment charges to earnings	(80)	-
Service fees on deposit accounts	604	542
Other loan fees	773	499
Earnings from investment in life insurance	459	372
Net realized gain on sale of securities	118	324
Net gain on sale of SBA loans	187	101
Other income	566	506
Total Non-Interest Income	2,627	2,344
Non-Interest Expenses		
Salaries and employee benefits	10,915	10,539
Occupancy and equipment	3,200	3,205
Professional	754	851
Advertising	270	225
Data processing	748	641
Insurance	345	390
FDIC insurance and assessments	553	673
Outside service fees	508	422
Amortization of identifiable intangibles	163	201
OREO expenses, OREO impairment and sales, net	699	270
Loan workout expenses	240	166
Other operating	1,452	1,510

Total Non-Interest Expenses		19,847		19,093
Income before Income Taxes		7,620		6,854
Income Tax Expense		2,805		2,546
Net Income	$	4,815	$	4,308
Preferred stock dividends and discount accretion		(448)		(814)
Net income available to common shareholders	$	4,367	$	3,494
Earnings Per Common Share				
Basic	$	0.55	$	0.44
Diluted	$	0.54	$	0.44

See notes to consolidated financial statements.

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Community Partners Bancorp

Consolidated Statements of Comprehensive Income

	Years Ended December 31, 2012	2011
	(In Thousands)	
Net income	$ 4,815	$ 4,308
Other comprehensive income (loss):		
Reclassification adjustment for gains on sales of securities recognized in income, net of income tax benefit 2012: $47; 2011 $133	(71)	(194)
Unrealized holdings gains on securities available for sale, net of income tax 2012: $110; net of income tax 2011: $190	180	288
Unrealized loss on securities for which a portion of the impairment has been recognized in income, net of income tax benefit 2012: $34; 2011: $0	(51)	-
Reclassification adjustment for other-than-temporary credit losses on securities included in net income, net income tax 2012: $32; 2011: $0	48	-
Other comprehensive income	106	94
Total comprehensive income	$ 4,921	$ 4,402

See notes to consolidated financial statements.

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Community Partners Bancorp

Consolidated Statements of Shareholders' Equity

(Dollars in Thousands)	Preferred Stock	Common Stock Outstanding Shares	Common Stock Amount	Retained Earnings	Accumulated Other Comprehensive Income	Total Shareholders' Equity
Balance, January 1, 2011	$ 8,628	7,620,929	$ 70,067	$ 1,325	$ 168	$ 80,188
Net Income	-	-	-	4,308	-	4,308
Other comprehensive income	-	-	-	-	94	94
Preferred stock, Series C issued	12,000	-	-	-	-	12,000
Preferred stock, Series C issuance costs	-	-	-	(48)	-	(48)
Redemption of preferred stock, Series A	(9,000)	-	-	-	-	(9,000)
Redemption of preferred stock, Series A warrant	-	-	(460)	-	-	(460)
Dividends on preferred stock, Series C	-	-	-	(180)	-	(180)
Dividends on preferred stock, Series A	-	-	-	(262)	-	(262)
Preferred stock, Series A discount accretion	372	-	-	(372)	-	-
Common stock dividend – 3%	-	231,328	1,078	(1,078)	-	-
Stock option compensation expense	-	-	154	-	-	154
Options exercised	-	83,138	267	-	-	267
Tax-benefit-exercised non-qualified stock options	-	-	41	-	-	41
Employee stock purchase program	-	6,823	32	-	-	32
Balance, December 31, 2011	$ 12,000	7,942,218	$ 71,179	$ 3,693	$ 262	$ 87,134
Net income	-	-	-	4,815	-	4,815
Other comprehensive income					106	106
Dividends on preferred stock, Series C	-	-	-	(448)	-	(448)
Stock based compensation expense	-	-	183	-	-	183

Options exercised	-	37,130	124	-	-	124
Tax-benefit-exercised non-qualified stock options	-	-	13	-	-	13
Restricted stock awards-forfeiture	-	(4,133)	(8)	-	-	(8)
Employee stock purchase program	-	8,563	46	-	-	46
Balance, December 31, 2012	$ 12,000	7,983,778	$ 71,537	$ 8,060	$ 368	$ 91,965

See notes to consolidated financial statements.

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Community Partners Bancorp

Consolidated Statements of Cash Flows

	Years Ended December 31,	
	2012	2011
	(In Thousands)	
Cash Flows from Operating Activities		
Net income	$ 4,815	$ 4,308
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	680	703
Provision for loan losses	1,380	2,205
Intangible amortization	163	201
Net amortization of securities premiums and discounts	284	178
Other-than-temporary impairment on securities available for sale	80	-
Net realized gain on sale of securities available for sale	(118)	(324)
Deferred income taxes	(697)	(478)
Earnings from investment in life insurance	(459)	(372)
Net realized loss (gain) on sale of other real estate owned	197	(381)
Impairment on property held for sale	-	100
Impairment on other real estate owned	360	275
Stock based compensation expense	175	154
Gain from sale of SBA loans	(187)	(101)
Decrease (increase) in assets:		
Accrued interest receivable	44	(17)
Other assets	(111)	588
(Decrease) increase in liabilities:		
Accrued interest payable	(37)	14
Other liabilities	1,197	(51)
Net Cash Provided by Operating Activities	7,766	7,002
Cash Flows from Investing Activities		
Purchase of securities available for sale	(17,880)	(30,212)
Purchase of securities held to maturity	(12,093)	(5,993)
Proceeds from sales of securities available for sale	2,948	4,048
Proceeds from repayments and maturities of securities available for sale	11,575	14,096
Proceeds from repayments and maturities of securities held to maturity	3,589	3,706
Proceeds from sale of SBA loans	1,987	1,803
Purchase of restricted investments	(803)	(817)
Net increase in loans	(44,348)	(21,667)
Proceeds from the sale of other real estate owned	6,047	2,852
Improvements on other real estate owned	(66)	(725)
Purchase of bank-owned life insurance	-	(3,452)
Purchase of premises and equipment	(1,283)	(254)
Net Cash Used in Investing Activities	(50,327)	(36,615)
Cash Flows from Financing Activities		
Net increase in deposits	52,858	29,441
Net increase in securities sold under agreements to repurchase	492	1,361
Proceeds from issuance of preferred stock, Series C	-	12,000
Preferred stock, Series C, issuance costs	-	(48)

Redemption of preferred stock, Series A		-		(9,000)
Redemption of preferred stock, Series A warrants		-		(460)
Cash dividends paid on preferred stocks		(448)		(442)
Proceeds from employee stock purchase plan		46		32
Proceeds from exercise of stock options		124		267
Tax benefit of stock options exercised		13		41
Net Cash Provided by Financing Activities		53,085		33,192
Net Increase in Cash and Cash Equivalents		10,524		3,579
Cash and Cash Equivalents – Beginning		38,022		34,443
Cash and Cash Equivalents – Ending	$	48,546	$	38,022
Supplementary Cash Flows Information				
Interest paid	$	4,655	$	5,224
Income taxes paid	$	3,270	$	3,302
Supplementary schedule of non-cash activities:				
Other real estate acquired in settlement of loans	$	525	$	1,688

See notes to consolidated financial statements.

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Note 1 – Summary of Significant Accounting Policies

A. Organization and Basis of Presentation

The accompanying consolidated financial statements include the accounts of Community Partners Bancorp (the "Company" or "Community Partners"), a bank holding company, and its wholly-owned subsidiary, Two River Community Bank ("the Bank" or "Two River") and the Bank's wholly-owned subsidiaries, TRCB Investment Corporation, TRCB Holdings One LLC, TRCB Holdings Two LLC, TRCB Holdings Three LLC, TRCB Holdings Four LLC, TRCB Holdings Five LLC, TRCB Holdings Six LLC and wholly-owned trust, Two River Community Bank Employer's Trust. All inter-company balances and transactions have been eliminated in the consolidated financial statements.

B. Nature of Operations

Community Partners is a bank holding company whose principal activity is the ownership of Two River Community Bank. Through its banking subsidiary, the Company provides banking services to small and medium-sized businesses, professionals and individual consumers primarily in Monmouth County, New Jersey and Union County, New Jersey. The Company competes with other banking and financial institutions in its market communities.

The Company and its bank subsidiary are subject to regulations of certain state and federal agencies and, accordingly, they are periodically examined by those regulatory authorities. As a consequence of the extensive regulation of commercial banking activities, the Company's and the Bank's businesses are susceptible to being affected by state and federal legislation and regulations.

C. Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

The principal material estimates that are particularly susceptible to significant change in the near term relate to: the allowance for loan losses, certain intangible assets, such as goodwill and core deposit intangible, the potential impairment of restricted investments, the valuation of deferred tax assets, valuation of other real estate owned and the determination of other-than-temporary impairment on securities.

D. Significant Concentrations of Credit Risk

Most of the Company's activities are with customers located within Monmouth and Union counties of New Jersey. Note 2 discusses the types of securities that the Company invests in. Note 3 discusses the types of lending that the Company engages in. Although the Company actively manages the diversification of its loan portfolio, a substantial portion of its debtors' ability to honor their contracts is dependent upon the strength of the local economy. The loan portfolio includes commercial real estate, which is comprised of owner occupied and investment real estate, including general office, medical, manufacturing and retail space. Construction loans, short-term in nature, comprise another portion of the portfolio, along with commercial and industrial loans. The latter includes lines of credit and equipment loans. From time to time, the Company may purchase or sell an interest in a loan from or to another lender (participation loan) in order to manage its portfolio risk. Loans purchased by the Company are typically located in central New Jersey and meet the Company's own independent underwriting guidelines. The Company does not have any significant concentrations in any one industry or customer.

E. Comprehensive Income

Comprehensive income consists of net income and other comprehensive income. Other comprehensive income includes unrealized gains and losses on securities available for sale and unrealized losses related to factors other than credit or debt securities which have been determined to be other-than-temporarily impaired.

F. Statement of Cash Flows

For purposes of reporting cash flows, cash and cash equivalents include cash on hand, amounts due from banks, interest bearing demand deposits in banks, and Federal funds sold. Interest-bearing deposits are due from the Federal Reserve Bank of New York. Generally, Federal funds are purchased and sold for one-day periods.

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Note 1 – Summary of Significant Accounting Policies (Continued)

G. Securities

Securities classified as available for sale are those securities that the Company intends to hold for an indefinite period of time but not necessarily to maturity. Securities available for sale are carried at fair value. Any decision to sell a security classified as available for sale would be based on various factors, including significant movement in interest rates, changes in maturity mix of the Company's assets and liabilities, liquidity needs, regulatory capital considerations and other similar factors. Unrealized gains or losses are reported as increases or decreases in other comprehensive income, net of the related deferred tax effect. Realized gains or losses, determined on the basis of the cost of the specific securities sold, are included in earnings. Premiums and discounts are recognized in interest income using the interest method over the terms of the securities. Gains and losses on the sale of securities available for sale are recorded on the trade date and are determined using the specific identification method.

Securities classified as held to maturity are those securities the Company has both the intent and ability to hold to maturity regardless of changes in market conditions, liquidity needs or changes in general economic conditions. These securities are carried at cost adjusted for the amortization of premium and accretion of discount, computed by the interest method over the terms of the securities.

Management determines the appropriate classification of debt securities at the time of purchase and re-evaluates such designation as of each balance sheet date.

Other-than-temporary accounting guidance specifies that (a) if a company does not have the intent to sell a debt security prior to recovery and (b) it is more likely than not that it will not have to sell the debt security prior to recovery, the security would not be considered other-than-temporary impaired unless there is a credit loss. When an entity does not intend to sell the security, and it is more likely than not, the entity will not have to sell the security before recovery of its cost basis, it will recognize the credit component of an other-than-temporary impairment of a debt security in earnings and the remaining portion in other comprehensive income. For held to maturity debt securities, the amount of an other-than-temporary impairment recorded in other comprehensive income for the noncredit portion of a previous other-than-temporary impairment should be amortized prospectively over the remaining life of the security on the basis of the timing of future cash flows of the security.

H. Restricted Investments

Restricted investments, which represents the required investment in the common stock of correspondent banks, is carried at cost and as of December 31, 2012 and 2011, consists of the common stock of the Federal Home Loan Bank of New York ("FHLB") and Atlantic Central Bankers Bank ("ACBB"). Federal law requires a member institution of the FHLB to hold stock of its district FHLB according to a predetermined formula. The recorded investment in FHLB common stock was $1,465,000 and $1,405,000 at December 31, 2012 and 2011, respectively.

Restricted investments also include the Solomon Hess SBA Loan Fund, utilized for the purpose of the Bank satisfying its CRA lending requirements. As this fund operates as a private fund, shares in the Fund are not publicly traded and therefore have no readily determinable market value. An investor can have their interest in the Fund redeemed for the balance of their capital account at any quarter end assuming they give the Fund 60 days' notice. The investment in this Fund is recorded at cost which was $1,500,000 and $757,000 at December 31, 2012 and 2011, respectively. The Company does not record the investment at fair value on a recurring basis.

Management evaluates the restricted investments for impairment in accordance with U.S. generally accepted accounting principles. Management's determination of whether these investments are impaired is based on their assessment of the ultimate recoverability of their cost rather than by recognizing temporary declines in value. Management believes no impairment charge is necessary related to restricted investments as of December 31, 2012.

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Note 1 – Summary of Significant Accounting Policies (Continued)

I. Loans Receivable

Loans receivable, which management has the intent and ability to hold for the foreseeable future or until maturity or payoff are stated at their outstanding unpaid principal balances, net of an allowance for loan losses and any deferred fees or costs. Interest income is accrued on the unpaid principal balance. Loan origination fees, net of certain direct origination costs, are deferred and recognized as an adjustment of the yield (interest income) of the related loans. The Company is generally amortizing these amounts over the contractual life of the loan.

The loans receivable portfolio is segmented into commercial and consumer loans. Commercial loans consist of the following classes: commercial and industrial, real estate-construction and real estate-commercial. Consumer loans consist of the following classes: real estate-residential and consumer.

For all classes of loans receivable, the accrual of interest is discontinued when the contractual payment of principal or interest has become 90 days past due or management has serious doubts about further collectability of principal or interest, even though the loan is currently performing. A loan may remain on accrual status if it is in the process of collection and is either guaranteed or well secured. When a loan is placed on nonaccrual status, unpaid interest previously accrued on these loans is reversed from income. Interest received on nonaccrual loans including impaired loans generally is either applied against principal or reported as interest income, according to management's judgment as to the collectability of principal. Generally, loans are restored to accrual status when the obligation is brought current, has performed in accordance with the contractual terms for a reasonable period of time (generally six months) and the ultimate collectability of the total contractual principal and interest is no longer in doubt. The past due status of all classes of loans receivable is determined based on contractual due dates for loan payments.

J. Allowance for Loan Losses

The allowance for credit losses consists of the allowance for loan losses and the reserve for unfunded lending commitments. The allowance for loan losses represents management's estimate of losses inherent in the loan portfolio as of the balance sheet date and is recorded as a reduction to loans. The reserve for unfunded lending commitments represents management's estimate of losses inherent in its unfunded loan commitments and is recorded in other liabilities on the consolidated balance sheet, which at December 31, 2012 and 2011, the Company had no such reserves. The allowance for loan losses is increased by the provision for loan losses, and decreased by charge-offs, net of recoveries. Loans deemed to be uncollectable are charged against the allowance for loan losses, and subsequent recoveries, if any, are credited to the allowance. All, or part, of the principal balance of loans receivable are charged off to the allowance as soon as it is determined that the repayment of all, or part, of the principal balance is highly unlikely.

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

The allowance consists of specific, general and unallocated components. For loans that are classified as impaired, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of the loan. The specific component relates to loans that are classified as impaired. When a loan is impaired, there are three acceptable methods under ASC 310-10-35 for measuring the impairment:

1. The loan's observable market price;
2. The fair value of the underlying collateral; or
3. The present value (PV) of expected future cash flows.

Loans that are considered "collateral-dependent" should be evaluated under the "Fair market value of collateral." Loans that are still expected to be supported by repayment from the borrower should be evaluated under the "Present value of future cash flows."

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Note 1 – Summary of Significant Accounting Policies (Continued)

For the most part, the Company measures impairment under the "Fair market value of collateral" for any loan that would rely on the value of collateral for recovery in the event of default. The individual impairment analysis for each loan is clearly documented as to the chosen valuation method.

The general component covers pools of loans by loan class including commercial and industrial, real estate-construction and real estate-commercial not considered impaired as well as smaller balance homogeneous loans such as real estate-residential and consumer.

These pools of loans are evaluated for loss exposure based upon historical loss rates for each of these categories of loans, adjusted for qualitative factors. These qualitative risk factors include:

1. Changes in lending policy and procedures, including changes in underwriting standards and collection practices not previously considered in estimating credit losses.
2. Changes in relevant economic and business conditions.
3. Changes in nature and volume of the loan portfolio and in the terms of loans.
4. Changes in experience, ability and depth of lending management and staff.
5. Changes in the volume and severity of past due loans, the volume of non-accrual loans and the volume and severity of adversely classified loans.
6. Changes in the quality of the loan review system.
7. Changes in the value of underlying collateral for collateral-dependent loans.
8. The existence and effect of any concentration of credit and changes in the level of such concentrations.
9. The effect of other external forces such as competition, legal and regulatory requirements on the level of estimated credit losses in the existing portfolio.

Each factor is assigned a risk value to reflect low, moderate or high risk assessments based on management's best judgment using current market, macro and other relevant information available at the time of the evaluation. Adjustments to the factors are supported through documentation in each factor and accompanies the allowance for loan loss calculation.

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 specific and general losses in the portfolio.

The Company engages in a variety of lending activities, including commercial and industrial, real estate-commercial, real estate-construction, real estate-residential and consumer loans. The Company focuses its lending activities on individuals, professionals and small to medium sized businesses.

The Company originates commercial business loans to professionals, sole proprietorships and small businesses in our market areas. We extend commercial business loans on a secured and unsecured basis. Secured commercial loans are generally collateralized by residential and nonresidential real estate, marketable securities, accounts receivable, inventory, industrial/commercial machinery and equipment and furniture and fixtures. To further enhance our security position, we generally require personal guarantees of the principal owners of the entities to which we extend credit. These loans are made on both lines of credit and fixed-term basis ranging from one to five years in duration. When making commercial business loans, we consider the financial statements and/or tax returns of the borrower, the borrower's payment history along with the principal owners' payment history, the debt service capabilities of the borrower, the projected cash flows of the business, and the value of the collateral and the financial strength of the guarantor.

Commercial real estate loans are made to local commercial, retail and professional firms and individuals for the acquisition of new property or the refinancing of existing property. These loans are typically related to commercial businesses and secured by the underlying real estate used in these businesses or real property of the principals. Commercial real estate loans typically require a loan to value ratio of not greater than 75%. These loans are generally offered on a fixed or variable rate basis, subject to rate re-adjustments every five years and amortization schedules ranging from 5 to 25 years.

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Note 1 – Summary of Significant Accounting Policies (Continued)

Commercial loans are often larger and may involve greater risks than other types of lending. Because payments of such loans are often dependent on the successful operation of the business involved, repayment of such loans may be more sensitive than other types of loans and are subject to adverse conditions in the real estate market or the general economy. We are also involved with off-balance sheet financial instruments, which include collateralized commercial and standby letters of credit. We seek to minimize these risks through our underwriting guidelines and prudent risk management techniques. Any collateral securing such loans may depreciate over time, may be difficult to appraise and may fluctuate in value. Environmental surveys and inspections are obtained when circumstances suggest that the possibility of the presence of hazardous materials. There can be no assurances, however, of success in the efforts to minimize these risks.

During 2011, the Company was approved and granted Preferred Lending Status by the Small Business Administration ("SBA"), which allows the Company delegated authority to approve and close SBA loans up to $5.0 million. The Company maintains prudent credit risk management to monitor and evaluate the value of real estate and other collateral used to secure SBA loans. All SBA loans are originated in compliance with all applicable federal lending regulations, including but not limited to the Equal Credit Opportunity Act. The Bank currently participates in SBA's 7a and 504 loan programs, which typically provide guarantees up to 75% per loan. The Bank generally sells the guaranteed portion of selected loans to a third party and retains the servicing rights. No servicing asset has been recognized due to immateriality. Our philosophy remains to be prudent and focused on the cash flow of the businesses and financial strength of the guarantors.

The Company originates fixed-rate and adjustable-rate loans to individuals and builders to finance the construction of residential dwellings. We also originate construction loans for commercial development projects, including apartment buildings, restaurants, shopping centers and owner-occupied properties used for businesses. Our construction loans generally provide for the payment of interest only during the construction phase which is usually twelve months for residential properties and twelve to eighteen months for commercial properties. At the end of the construction phase, the loan either converts to a permanent mortgage loan or is paid off. Before making a commitment to fund a construction loan, we require an appraisal of the property by a bank approved independent licensed appraiser, an inspection of the property before disbursement of funds during the stages of the construction process, and approval from an identified source for the permanent takeout.

The Company offers a full range of residential real estate and consumer loans. These loans consist of residential mortgages, home equity lines of credit, equity loans, personal loans, automobile loans and overdraft protection. We do not originate subprime or negative amortization loans. Each residential mortgage loan is evidenced by a promissory note secured by a mortgage or deed of trust creating a first lien on one-to-four family residential property. Residential real estate properties underlying residential mortgage loans consist of single-family detached units, individual condominium units, two-to-four family dwellings units and townhouses. Our home equity revolving lines of credit come with a floating interest rate tied to the prime rate. Lines of credit are available to qualified applicants in amounts up to $350,000 for up to 15 years. We also offer fixed rate home equity loans in amounts up to $350,000 for a term of up to 15 years. Credit is based on the income and cash flow of the individual borrowers, real estate collateral supporting the mortgage debt and past credit history.

Consumer loans may entail greater risk than residential mortgage loans, particularly in the case of consumer loans that are unsecured or secured by assets that depreciate rapidly. In such cases, repossessed collateral for a defaulted consumer loan may not provide an adequate source of repayment for the outstanding loan and the remaining deficiency often does not warrant further substantial collection efforts against the borrower. In addition, consumer loan collections depend on the borrower's continuing financial stability, and therefore are more likely to be adversely affected by job loss, divorce, illness or personal bankruptcy. Furthermore, the application of various federal and state laws, including bankruptcy and insolvency laws, may limit the amount that can be recovered on such loans.

A loan is considered impaired when, based on current information events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant 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. Impairment is measured on a loan by loan basis for commercial and industrial, real estate-commercial, real estate-construction, real estate-residential and consumer 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 for loan losses is established for an impaired loan if its carrying value exceeds its estimated fair value. The estimated fair values of substantially all of the Company's impaired loans are measured based on the estimated fair value of the loan's collateral.

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Note 1 – Summary of Significant Accounting Policies (Continued)

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

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

Loans whose terms are modified are classified as troubled debt restructurings if the Company grants such borrowers concessions and it is deemed that those borrowers are experiencing financial difficulty. Concessions granted under a troubled debt restructuring generally involves a reduction in interest rates or a modification of a loan's amortization schedule. Non-accrual troubled debt restructurings are restored to accrual status if principal and interest payments, under the modified terms, are current for six consecutive months after modification. Loans classified as troubled debt restructurings are designated as impaired.

The allowance calculation methodology includes further segregation of loan classes into risk rating categories. The borrower's overall financial condition, repayment sources, guarantors and value of collateral, if appropriate, are evaluated annually for commercial loans or when credit deficiencies arise, such as delinquent loan payments, for commercial and consumer loans. Credit quality risk ratings include regulatory classifications of special mention, substandard, doubtful and loss. Loans criticized special mention have potential weaknesses that deserve management's close attention. If uncorrected, the potential weaknesses may result in deterioration of the repayment prospects. Loans classified substandard have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They include loans that are inadequately protected by the current sound net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans classified doubtful have all the weaknesses inherent in loans classified substandard with the added characteristics that collection or liquidation in full, on the basis of current conditions and facts, is highly improbable. Loans classified as a loss are considered uncollectable and are charged to the allowance for loan losses. Loans not classified are rated pass.

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

K. Transfers of Financial Assets

Transfers of financial assets, including loan participation sales, are accounted for as sales, when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the Company, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets and (3) the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity. The balance of participations sold to other banks that are serviced by the Company was $6,923,000 and $1,678,000 at December 31, 2012 and 2011, respectively.

L. Other Real Estate Owned

Other Real Estate Owned ("OREO") includes real estate acquired through foreclosure or by deed in lieu of foreclosure. Real estate owned is carried at the lower of cost or fair value, less estimated costs to sell. When a property is acquired, the excess of the loan balance over fair value, less selling costs, is charged to the allowance for loan losses. Operating results from real estate owned, including rental income, operating expenses, and gains and losses realized from the sales of real estate owned are recorded as incurred. OREO is periodically reviewed to ensure that the fair value of the property supports the carrying value.

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Note 1 – Summary of Significant Accounting Policies (Continued)

M. Bank-Owned Life Insurance

The Company invests in bank-owned life insurance ("BOLI") as a source of funding for employee benefit expenses. BOLI involves the purchasing of life insurance by the Company's wholly-owned trust on a chosen group of employees. The Company is the owner and beneficiary of the policies. This life insurance investment is carried at the cash surrender value of the underlying policies. Income generated from the increase in cash surrender value of the policies is included in non-interest income on the statements of operations.

N. Bank Premises and Equipment

Premises and equipment are stated at cost less accumulated depreciation. Depreciation is charged to operations on a straight-line basis over the estimated useful lives of the respective assets. Leasehold improvements are amortized over the shorter of their estimated life or the lease term.

O. Advertising

The Company expenses advertising costs as incurred.

P. Income Taxes

Deferred income taxes are provided on the liability method whereby deferred tax assets are recognized for deductible temporary differences and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the reported amounts of assets and liabilities and their tax basis. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion of the deferred tax assets will not be realized. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment. The Company and its subsidiary file a consolidated Federal income tax return.

The Company analyzes each tax position taken in its tax returns and determines the likelihood that the position will be realized. Only tax positions that are "more likely than not" to be realized can be recognized in the Company's financial statements. For tax positions that do not meet this recognition threshold, the Company will record an unrecognized tax benefit for the difference between the position taken on the tax return and the amount recognized in the financial statements. The Company does not have any material unrecognized tax benefits or accrued interest or penalties at December 31, 2012 or 2011 or during the years then ended. No unrecognized tax benefits are expected to arise within the next twelve months. The Company's policy is to account for interest as a component of interest expense and penalties as a component of other expenses. The Company and its subsidiaries are subject to U.S. Federal income tax as well as income tax of the State of New Jersey. The Company is no longer subject to examination by taxing authorities for the years before January 1, 2009.

Q. Off-Balance Sheet Financial Instruments

In the ordinary course of business, the Company has entered into off-balance sheet financial instruments consisting of commitments to extend credit and letters of credit. Such financial instruments are recorded in the balance sheet when they are funded.

R. Earnings per Common Share

Earnings per common share are calculated on the basis of the weighted average number of common shares outstanding during the year. All weighted average, actual shares or per share information in the financial statements have been adjusted retroactively for the effect of stock dividends. Basic earnings per common share excludes dilution and is calculated by dividing income available to common shareholders by the weighted average common shares outstanding excluding restricted stock awards outstanding during the period. Diluted earnings per common share takes into account the potential dilution that could occur if certain outstanding securities to issue common stock were exercised and converted into common stock. Potential common shares relate to outstanding stock options, warrants and restricted stock awards, and are determined using the treasury stock method.

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Note 1 – Summary of Significant Accounting Policies (Continued)

S. Stock-Based Compensation

Stock compensation accounting guidance requires that the compensation cost relating to share-based payment transactions be recognized in financial statements. That cost will be measured based on the grant date fair value of the equity or liability instruments issued. The stock compensation accounting guidance covers a wide range of share-based compensation arrangements including stock options, restricted share plans, performance-based awards, share appreciation rights, and employee share purchase plans.

The stock compensation accounting guidance requires that compensation cost for all stock awards be calculated and recognized over the employees' service period, generally defined as the vesting period. For awards with graded-vesting, compensation cost is recognized on a straight-line basis over the requisite service period for the entire award. A Black-Sholes model is used to estimate the fair value of stock options, while the market price of the Company's common stock at the date of grant is used for restricted stock awards.

T. Reclassification

Certain amounts in the 2011 financial statements have been reclassified to conform to the presentation used in the 2012 financial statements. These reclassifications had no effect on net income.

U. Goodwill and Other Intangible Assets

The Company's goodwill was recognized in connection with the acquisition of the Town Bank in April 2006. Accounting principles generally accepted in the United States of America requires that goodwill be tested for impairment annually or more frequently if impairment indicators arise utilizing a two-step methodology. Step one requires the Company to determine the fair value of the reporting unit and compare it to the carrying value, including goodwill, of such reporting unit. The reporting unit was determined to be our community banking operations, which is our only operating segment. If the fair value of the reporting unit exceeds the carrying value, goodwill is not impaired. If the carrying value exceeds fair value, there is an indication of impairment and the second step is performed to determine the amount of impairment, if any. The second step compares the fair value of the reporting unit to the aggregate fair values of its individual assets, liabilities and identified intangibles.

The Company performed its annual goodwill impairment analysis as of September 30, 2012. Based on the results of the step one goodwill impairment analysis, the Company determined that there was no impairment on the current goodwill balance. See Note 5 for additional details.

V. Segment Reporting

The Company acts as an independent community financial services provider, and offers traditional banking and related financial services to individual, business and government customers. Through its branch, automated teller machine networks, and internet banking services, the Company offers a full array of commercial and retail financial services, including taking of time, savings and demand deposits; the making of commercial, consumer and mortgage loans; and the providing of other financial services. Management does not separately allocate expenses, including the cost of funding loan demand, between the commercial, retail, and consumer banking operations of the Company. Accordingly, all significant operating decisions are based upon analysis of the Bank as one segment or unit.

W. Subsequent Events

The Company has evaluated events and transactions occurring subsequent to the balance sheet date of December 31, 2012 for items that should potentially be recognized or disclosed in these financial statements.

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Note 1 – Summary of Significant Accounting Policies (Continued)

X. Recent Accounting Pronouncements

ASU 2011-04; This ASU amends FASB ASC Topic 820, Fair Value Measurements, to bring U.S. GAAP for fair value measurements in line with International Accounting Standards. The ASU clarifies existing guidance for items such as: the application of the highest and best use concept to non-financial assets and liabilities; the application of fair value measurement to financial instruments classified in a reporting entity's stockholder's equity; and disclosure requirements regarding quantitative information about unobservable inputs used in the fair value measurements of level 3 assets. The ASU also creates an exception to Topic 820 for entities which carry financial instruments within a portfolio or group, under which the entity is now permitted to base the price used for fair valuation upon a price that would be received to sell the net asset position or transfer a net liability position in an orderly transaction. The ASU also allows for the application of premiums and discounts in a fair value measurement if the financial instrument is categorized in level 2 or 3 of the fair value hierarchy. Lastly, the ASU contains new disclosure requirements regarding fair value amounts categorized as level 3 in the fair value hierarchy such as: disclosure of the valuation process used; effects of and relationships between unobservable inputs; usage of nonfinancial assets for purposes other than their highest and best use when that is the basis of the disclosed fair value; and categorization by level of items disclosed at fair value, but not measured at fair value for financial statement purposes. For public entities, this ASU is effective for interim and annual periods beginning after December 15, 2011. The adoption of this ASU did not have a material impact on our financial position or results of operation and resulted in expanded fair value disclosures.

ASU 2011-05; The provisions of this ASU amend FASB ASC Topic 220, Comprehensive Income, to facilitate the continued alignment of U.S. GAAP with International Accounting Standards. The ASU prohibits the presentation of the components of comprehensive income in the statement of stockholder's equity. Reporting entities are allowed to present either: a statement of comprehensive income, which reports both net income and other comprehensive income; or separate, but consecutive, statements of net income and other comprehensive income. Under previous GAAP, all 3 presentations were acceptable. Regardless of the presentation selected, the Reporting Entity is required to present all reclassifications between other comprehensive and net income on the face of the new statement or statements. The provisions of this ASU are effective for fiscal years and interim periods beginning after December 31, 2011 for public entities. The adoption of this ASU did not have a material impact on our financial position or results of operation and resulted in the Consolidated Statements of Comprehensive Income.

ASU 2011-08; In September, 2011, the FASB issued ASU 2011-08, Testing Goodwill for Impairment. The purpose of this ASU is to simplify how entities test goodwill for impairment by adding a new first step to the pre-existing goodwill impairment test under ASC Topic 350, Intangibles – Goodwill and Other. This amendment gives the entity the option to first assess a variety of qualitative factors such as economic conditions, cash flows, and competition to determine whether it was more likely than not that the fair value of goodwill has fallen below its carrying value. If the entity determines that it is not likely that the fair value has fallen below its carrying value, then the entity will not have to complete the original two-step test under Topic 350. The amendments in this ASU are effective for impairment tests performed for fiscal years beginning after December 15, 2011. This ASU did not have an impact on its consolidated financial statements.

ASU 2011-12; In December, 2011, the FASB issued ASU 2011-12, Deferral of the Effective Date to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update 2011-05. In response to stakeholder concerns regarding the operational ramifications of the presentation of these reclassifications for current and previous years, the FASB has deferred the implementation date of this provision to allow time for further consideration. The requirement in ASU 2011-05, Presentation of Comprehensive Income, for the presentation of a combined statement of comprehensive income or separate, but consecutive, statements of net income and other comprehensive income is still effective for fiscal years and interim periods beginning after

December 15, 2011 for public companies. The implementation of ASU 2011-12 is not expected to have a material impact on our financial position or results of operation.

ASU 2013-02; In February, 2013, the FASB issued ASU 2013-02, Comprehensive Income (Topic 220): Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income. This ASU requires disclosure of the effects of reclassifications out of accumulated other comprehensive income ("AOCI") on net income line items only for those items that are reported in their entirety in net income in the period of reclassification. For AOCI reclassification items that are not reclassified in their entirety into net income, a cross reference will be required to other U.S. GAAP disclosures. The amendments are effective for reporting periods beginning on or after December 15, 2012. The implementation of ASU 2013-02 is not expected to have a material impact on our financial position or results of operation.

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Note 2 – Securities

The amortized cost, gross unrealized gains and losses, and fair values of the Company's securities are summarized as follows:

December 31, 2012:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses Noncredit OTTI (In Thousands)	Gross Unrealized Losses Other	Fair Value
Securities available for sale:					
Municipal securities	$ 1,255	55	$ -	$ -	$ 1,310
U.S. Government-sponsored enterprises ("GSE") - Residential mortgage-backed securities	19,881	505	-	(12)	20,374
Collateralized residential mortgage obligations	22,655	342	-	(1)	22,996
Corporate debt securities, primarily financial institutions	4,017	49	(164)	(247)	3,655
	47,808	951	(164)	(260)	48,335
Community Reinvestment Act ("CRA") mutual fund	2,344	77	-	-	2,421
	$ 50,152	$ 1,028	$ (164)	$ (260)	$ 50,756
Securities held to maturity:					
Municipal securities	$ 17,799	$ 619	$ -	$ (4)	$ 18,414
GSE - Residential mortgage-backed securities	1,083	12	-	-	1,095
Collateralized residential mortgage obligations	892	2	-	-	894
Corporate debt securities, primarily financial institutions	1,812	-	-	(280)	1,532
	$ 21,586	$ 633	$ -	$ (284)	$ 21,935

December 31, 2011:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses Noncredit OTTI (In Thousands)	Gross Unrealized Losses Other	Fair Value
Securities available for sale:					
U.S. Government agency securities	$ 2,250	$ 8	$ -	$ -	$ 2,258
Municipal securities	1,261	46	-	-	1,307
GSE - Residential mortgage-backed securities	21,317	581	-	(20)	21,878
Collateralized residential mortgage obligations	16,865	298	-	-	17,163
Corporate debt securities, primarily financial institutions	3,067	-	(183)	(356)	2,528
	44,760	933	(183)	(376)	45,134

CRA mutual fund		2,258		63		-		-	2,321
	$	47,018	$	996	$	(183)	$	(376)	$ 47,455
Securities held to maturity:									
Municipal securities	$	11,296	$	613	$	-	$	(2)	$ 11,907
Corporate debt securities, primarily financial institutions		1,809		-		-		(494)	1,315
	$	13,105	$	613	$	-	$	(496)	$ 13,222

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Note 2 – Securities (Continued)

The amortized cost and fair value of the Company's debt securities at December 31, 2012, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Available for Sale		Held to Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
	(In Thousands)			
Due in one year or less	$ -	$ -	$ 9,032	$ 9,034
Due in one year through five years	1,791	1,805	1,922	2,049
Due in five years through ten years	1,464	1,485	4,967	5,211
Due after ten years	2,017	1,675	3,690	3,652
	5,272	4,965	19,611	19,946
GSE - Residential mortgage-backed securities	19,881	20,374	1,083	1,095
Collateralized residential mortgage obligations	22,655	22,996	892	894
	$ 47,808	$ 48,335	$ 21,586	$ 21,935

The Company had six securities sales in 2012 totaling $2,948,000 and recorded a gross realized gain of $118,000 from these sales as compared to nine sales totaling $4,048,000 recording a gross realized gain of $324,000 during 2011.

Certain of the Company's GSE residential mortgage-backed securities and collateralized residential mortgage obligations, totaling $23,827,000 and $27,412,000 at December 31, 2012 and 2011, respectively, were pledged as collateral to secure securities sold under agreements to repurchase and public deposits as required or permitted by law.

The tables below indicate the length of time individual securities have been in a continuous unrealized loss position at December 31, 2012 and 2011:

	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
December 31, 2012:	(In Thousands)					
Municipal securities	$ 2,222	$ (4)	$ -	$ -	$ 2,222	$ (4)
GSE – Residential mortgage-backed securities	2,320	(12)	-	-	2,320	(12)
Collateralized residential mortgage obligations	4,184	(1)	-	-	4,184	(1)
Corporate debt securities, primarily financial institutions	-	-	2,805	(691)	2,805	(691)
Total Temporarily Impaired Securities	$ 8,726	$ (17)	$ 2,805	$ (691)	$ 11,531	$ (708)

	Less than 12 Months		12 Months or More		Total	
	Fair	Unrealized	Fair	Unrealized	Fair	Unrealized

		Value		Losses		Value		Losses		Value		Losses
December 31, 2011:						(In Thousands)						
Municipal securities	$	969	$	(2)	$	-	$	-	$	969	$	(2)
GSE – Residential mortgage-backed securities		3,490		(20)		-		-		3,490		(20)
Corporate debt securities, primarily financial institutions		1,252		(50)		2,591		(983)		3,843		(1,033)
Total Temporarily Impaired Securities	$	5,711	$	(72)	$	2,591	$	(983)	$	8,302	$	(1,055)

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Note 2 – Securities (Continued)

The Company had 15 securities in an unrealized loss position at December 31, 2012. In management's opinion, the unrealized losses in municipal and GSE residential mortgage-backed securities reflect changes in interest rates subsequent to the acquisition of specific securities. The unrealized loss for corporate debt securities also reflects a widening of spreads due to the liquidity and credit concerns in the financial markets. The Company does not intend to sell these debt securities prior to recovery and it is more likely than not that the Company will not have to sell these debt securities prior to recovery.

Included in corporate debt securities are four individual trust preferred securities issued by large financial institutions with Moody's ratings from Baa1 to Ba2. As of December 31, 2012, all of these securities are current with their scheduled interest payments. These single issue securities are from large money center banks. Management concluded that these securities were not other-than-temporarily impaired as of December 31, 2012. These four securities have an amortized cost value of $2.8 million and a fair value of $2.3 million at December 31, 2012.

The Company also has one pooled trust preferred security with a Moody's rating of Ca included in corporate debt securities with an amortized cost basis of $192,000 and a fair value of $28,000 at December 31, 2012. This pooled trust preferred security has been remitting reduced amounts of interest as some individual participants of the pool have deferred interest payments. The pooled instrument consists of securities issued by financial institutions and insurance companies and we hold the mezzanine tranche of such security. Senior tranches generally are protected from defaults by over-collateralization and cash flow default protection provided by subordinated tranches, with senior tranches having the greatest protection and mezzanine tranches subordinated to the senior tranches. For the pooled trust preferred security, management reviewed expected cash flows and credit support and determined it was not probable that all principal and interest would be repaid. The most significant input to the expected cash flow model was the assumed default rate for each pooled trust preferred security. Financial metrics, such as capital ratios and non-performing asset ratios, of each individual financial institution issuer that comprises the pooled trust preferred securities were evaluated to estimate the expected default rates for each security. In this pooled trust preferred security, there are 28 out of 39 banks and insurance companies that are performing at December 31, 2012. The deferrals and defaults as a percentage of original collateral at December 31, 2012 was 29.2%. Total other-than-temporary impairment on this security was $472,000 at December 31, 2012, of which $308,000 was determined to be a credit loss and charged to operations and $164,000 was determined to be non-credit related and recognized in the other comprehensive income component. There was an $80,000 other-than-temporary impairment charge to earnings during 2012, as compared to none for the same period in 2011. Future deterioration in the cash flow of these instruments or the credit quality of the financial institution issuers could result in additional impairment charges in the future.

The following roll forward reflects the amounts related to other-than-temporary credit losses recognized in earnings for the years ended December 31, 2012 and 2011 (in thousands):

Beginning balance, January 1, 2011	$	228
Additional increases to the amount related to the credit loss for which an other-than-temporary impairment was previously recognized		-
Ending balance, December 31, 2011		228
Additional increases to the amount related to the credit loss		

for which an other-than-temporary impairment was previously recognized		80
Ending balance, December 31, 2012	$	308

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Note 3 – Loans Receivable and Allowance for Loan Losses

The components of the loan portfolio at December 31, 2012 and 2011 are as follows:

	2012	2011
	(In Thousands)	
Commercial and industrial	$ 138,438	$ 136,869
Real estate – construction	83,755	51,180
Real estate – commercial	288,060	270,688
Real estate – residential	20,875	19,201
Consumer	40,975	52,853
	572,103	530,791
Allowance for loan losses	(7,984)	(7,310)
Unearned fees	(656)	(661)
Net Loans	$ 563,463	$ 522,820

The performance and credit quality of the loan portfolio is monitored by analyzing the age of the loans receivable as determined by the length of time a recorded payment is past due. The following table presents the classes of the loan portfolio summarized by the past due status as of December 31, 2012 and 2011:

December 31, 2012:

(In Thousands)	30-59 Days Past Due	60-89 Days Past Due	Greater than 90	Total Past Due	Current	Total Loans Receivable	Loans Receivable >90 Days and Accruing
Commercial and industrial	$ 350	$ 2,132	$ 1,681	$ 4,163	$ 134,275	$ 138,438	$ -
Real estate – construction	-	324	-	324	83,431	83,755	-
Real estate – commercial	2,609	231	3,542	6,382	281,678	288,060	-
Real estate – residential	590	-	263	853	20,022	20,875	-
Consumer	201	-	1,988	2,189	38,786	40,975	2
Total	$ 3,750	$ 2,687	$ 7,474	$ 13,911	$ 558,192	$ 572,103	$ 2

December 31, 2011:

(In Thousands)	30-59 Days Past Due	60-89 Days Past Due	Greater than 90	Total Past Due	Current	Total Loans Receivable	Loans Receivable >90 Days and Accruing
Commercial and industrial	$ 538	$ 1,776	$ 2,349	$ 4,663	$ 132,206	$ 136,869	$ -
Real estate – construction	-	-	292	292	50,888	51,180	-
Real estate – commercial	5,499	-	145	5,644	265,044	270,688	-

Real estate – residential	-	998	263	1,261	17,940	19,201	-
Consumer	375	50	2,191	2,616	50,237	52,853	-
Total	$ 6,412	$ 2,824	$ 5,240	$ 14,476	$ 516,315	$ 530,791	$ -

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Note 3 – Loans Receivable and Allowance for Loan Losses (Continued)

The following table presents non-accrual loans by classes of the loan portfolio at December 31, 2012 and 2011:

	2012	2011
	(In Thousands)	
Commercial and industrial	$ 1,681	$ 2,349
Real estate – construction	-	292
Real estate – commercial	3,542	145
Real estate – residential	263	263
Consumer	1,986	2,191
Total	$ 7,472	$ 5,240

The following table summarizes information in regards to impaired loans by loan portfolio class as of December 31, 2012 and 2011:

December 31, 2012:	Recorded Investment, Net of Charge-offs	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
(In Thousands)					
With no related allowance recorded:					
Commercial and industrial	$ 4,774	$ 4,774	$ -	$ 4,905	$ 193
Real estate – construction	-	-	-	-	-
Real estate – commercial	4,971	4,971	-	5,003	138
Real estate – residential	-	-	-	-	-
Consumer	352	352	-	361	16
With an allowance recorded:					
Commercial and industrial	$ 1,140	$ 1,140	$ 295	$ 1,185	$ 138
Real estate – construction	-	-	-	-	-
Real estate – commercial	4,121	4,121	470	4,170	206
Real estate – residential	263	263	60	263	-
Consumer	1,780	1,780	233	1,794	-
Total:					
Commercial and industrial	$ 5,914	$ 5,914	$ 295	$ 6,090	$ 331
Real estate – construction	-	-	-	-	-
Real estate – commercial	9,092	9,092	470	9,173	344
Real estate – residential	263	263	60	263	-
Consumer	2,132	2,132	233	2,155	16
	$ 17,401	$ 17,401	$ 1,058	$ 17,681	$ 691

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Note 3 – Loans Receivable and Allowance for Loan Losses (Continued)

December 31, 2011:	Recorded Investment, Net of Charge-offs	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
(In Thousands)					
With no related allowance recorded:					
Commercial and industrial	$ 3,423	$ 3,423	$ -	$ 3,436	$ 139
Real estate – construction	-	-	-	-	-
Real estate – commercial	3,510	3,510	-	3,529	160
Real estate – residential	225	225	-	225	4
Consumer	251	251	-	251	8
With an allowance recorded:					
Commercial and industrial	$ 2,914	$ 3,161	$ 928	$ 2,876	$ 55
Real estate – construction	292	292	63	414	20
Real estate – commercial	4,228	4,228	188	4,265	244
Real estate – residential	263	263	15	263	5
Consumer	1,938	1,938	254	1,938	-
Total:					
Commercial and industrial	$ 6,337	$ 6,584	$ 928	$ 6,312	$ 194
Real estate – construction	292	292	63	414	20
Real estate – commercial	7,738	7,738	188	7,794	404
Real estate – residential	488	488	15	488	9
Consumer	2,189	2,189	254	2,189	8
	$ 17,044	$ 17,291	$ 1,448	$ 17,197	$ 635

The following table presents the classes of the loan portfolio summarized by the aggregate pass rating and the classified ratings of special mention, substandard and doubtful within the Company's internal risk rating system as of December 31, 2012 and 2011:

	Pass	Special Mention	Substandard (In Thousands)	Doubtful	Total
December 31, 2012:					
Commercial and industrial	$ 119,195	$ 7,196	$ 12,047	$ -	$ 138,438
Real estate – construction	78,119	1,443	4,193	-	83,755
Real estate – commercial	267,768	4,648	15,644	-	288,060
Real estate – residential	20,507	-	368	-	20,875
Consumer	38,394	140	2,441	-	40,975
Total:	$ 523,983	$ 13,427	$ 34,693	$ -	$ 572,103

	Pass		Special Mention		Substandard (In Thousands)		Doubtful		Total
December 31, 2011:									
Commercial and industrial	$	119,531	$	4,683	$	12,655	$	-	$ 136,869
Real estate – construction		50,346		-		834		-	51,180
Real estate – commercial		255,877		4,300		10,511		-	270,688
Real estate – residential		18,938		-		263		-	19,201
Consumer		49,973		144		2,736		-	52,853
Total:	$	494,665	$	9,127	$	26,999	$	-	$ 530,791

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Note 3 – Loans Receivable and Allowance for Loan Losses (Continued)

As part of the allowance computation at December 31, 2012, the Company undertook a comprehensive review and inspection of all loans with collateral identified as being located within certain impact zones of Superstorm Sandy that impacted the region in October 2012. In the analysis, the Company reviewed a total of $26.1 million in loans, comprised of $20.4 million of commercial real estate and commercial and industrial loans, which represented 4.0% of this segment of the loan portfolio, $4.9 million of consumer loans, consisting primarily of home equity products, which represented 12.0% of this segment of the portfolio, and $800,000 of residential mortgage loans, which represented 4.0% of this segment of our portfolio. In total, the $26.1 million of identified loans represented 4.6% of the total loan portfolio. The Company evaluated the impact of the storm relative to the adequacy of the allowance for loan losses. Based on that evaluation, there were no loan charge-offs or specific losses identified at this time. Although the ultimate amount of loan losses relating to the storm is uncertain and difficult to predict, as information continues to be gathered, the Company recorded an additional provision for loan losses of $204,000 for the quarter and year ended December 31, 2012, solely related to the impact of the storm.

The following table presents the change in the allowance for loan losses by classes of loans as of December 31, 2012 and 2011:

Allowance for Credit Losses	Commercial and Industrial	Real Estate - Commercial	Real Estate - Construction	Real Estate – Residential	Consumer	Unallocated	Total
	(In Thousands)						
Beginning balance, January 1, 2012	$ 2,448	$ 2,412	$ 1,222	$ 256	$ 880	$ 92	$ 7,310
Charge-offs	(552)	-	(59)	-	(285)	-	(896)
Recoveries	18	-	169	-	3	-	190
Provision	(77)	955	314	(39)	213	14	1,380
Ending balance, December 31, 2012	$ 1,837	$ 3,367	$ 1,646	$ 217	$ 811	$ 106	$ 7,984

Allowance for Credit Losses	Commercial and Industrial	Real Estate - Commercial	Real Estate - Construction	Real Estate - Residential	Consumer	Unallocated	Total
	(In Thousands)						
Beginning balance, January 1, 2011	$ 2,081	$ 2,193	$ 895	$ 276	$ 793	$ 8	$ 6,246
Charge-offs	(482)	-	(82)	-	(688)	-	(1,252)
Recoveries	1	-	58	-	52	-	111
Provision	848	219	351	(20)	723	84	2,205
Ending balance, December 31, 2011	$ 2,448	$ 2,412	$ 1,222	$ 256	$ 880	$ 92	$ 7,310

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Note 3 – Loans Receivable and Allowance for Loan Losses (Continued)

The following table presents the balance in the allowance for loan losses at December 31, 2012 and 2011 disaggregated on the basis of the Company's impairment method by class of loans receivable along with the balance of loans receivable by class disaggregated on the basis of the Company's impairment methodology:

	Allowance for Loan Losses			Loans Receivable		
December 31, 2012:	Balance	Balance Related to Loans Individually Evaluated for Impairment	Balance Related to Loans Collectively Evaluated for Impairment	Balance	Balance Individually Evaluated for Impairment	Balance Collectively Evaluated for Impairment
	(In Thousands)					
Commercial and industrial	$ 1,837	$ 295	$ 1,542	$ 138,438	$ 5,914	$ 132,524
Real estate – construction	1,646	-	1,646	83,755	-	83,755
Real estate – commercial	3,367	470	2,897	288,060	9,092	278,968
Real estate – residential	217	60	157	20,875	263	20,612
Consumer	811	233	578	40,975	2,132	38,843
Unallocated	106	-	106	-	-	-
Total:	$ 7,984	$ 1,058	$ 6,926	$ 572,103	$ 17,401	$ 554,702

	Allowance for Loan Losses			Loans Receivable		
December 31, 2011:	Balance	Balance Related to Loans Individually Evaluated for Impairment	Balance Related to Loans Collectively Evaluated for Impairment	Balance	Balance Individually Evaluated for Impairment	Balance Collectively Evaluated for Impairment
	(In Thousands)					
Commercial and industrial	$ 2,448	$ 928	$ 1,520	$ 136,869	$ 6,337	$ 130,532
Real estate – construction	1,222	63	1,159	51,180	292	50,888
Real estate – commercial	2,412	188	2,224	270,688	7,738	262,950
Real estate – residential	256	15	241	19,201	488	18,713
Consumer	880	254	626	52,853	2,189	50,664
Unallocated	92	-	92	-	-	-
Total:	$ 7,310	$ 1,448	$ 5,862	$ 530,791	$ 17,044	$ 513,747

Loans whose terms are modified are classified as troubled debt restructurings if the Company grants such borrowers concessions and it is deemed that those borrowers are experiencing financial difficulty. Concessions granted under a troubled debt restructuring generally involves a temporary reduction in interest rates or a modification of a loan's amortization schedule. Non-accrual troubled debt restructurings are restored to accrual status if principal and interest payments, under the modified terms, are current for six consecutive months after modification. Loans identified as troubled debt restructurings are designated as impaired and classified as substandard loans.

Modifications involving troubled borrowers may include extension of maturity date, reduction in the stated interest rate, rescheduling of future cash flows, and reduction in the face amount of the debt or reduction of past accrued interest.

The Company's troubled debt restructured modifications are made on short terms (12 month terms) in order to aggressively monitor and track performance. The short-term modifications performances are monitored for continued payment performance for an additional period of time after the expiration of the concession. Balance reductions and annualized loss rates are also important metrics that are monitored. The main objective of the modification programs is to reduce the payment burden for the borrower and improve the net present value of the Company's expected cash flows.

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Note 3 – Loans Receivable and Allowance for Loan Losses (Continued)

The following tables present newly troubled debt restructured loans that occurred during the years ended December 31, 2012 and 2011:

Troubled Debt Restructuring:	Number of Contracts	December 31, 2012 Pre-Modification Outstanding Recorded Investment (Dollars in Thousands)	Post-Modification Outstanding Recorded Investment
Commercial and industrial	4	$ 2,167	$ 2,142
Real estate – construction	-	-	-
Real estate – commercial	2	279	277
Real estate – residential	-	-	-
Consumer	1	155	146
Total	7	$ 2,601	$ 2,565

Troubled Debt Restructuring:	Number of Contracts	December 31, 2011 Pre-Modification Outstanding Recorded Investment (Dollars in Thousands)	Post-Modification Outstanding Recorded Investment
Commercial and industrial	2	$ 374	$ 361
Real estate – construction	-	-	-
Real estate – commercial	1	2,630	2,626
Real estate – residential	-	-	-
Consumer	-	-	-
Total	3	$ 3,004	$ 2,987

The Company classifies all troubled debt restructurings as impaired loans. Impaired loans are individually assessed to determine that the loan's carrying value is not in excess of the estimated fair value of the collateral (less cost to sell), if the loan is collateral dependent, or the present value of the expected future cash flows, if the loan is not collateral dependent. Management performs a detailed evaluation of each impaired loan and generally obtains updated appraisals as part of the evaluation. In addition, management adjusts estimated fair value down to appropriately consider recent market conditions, our willingness to accept a lower sales price to effect a quick sale, and costs to dispose of any supporting collateral.

As a result of our impairment evaluation, the Company established a reserve amount of $45,000 against one loan classified as troubled debt restructuring as of December 31, 2012. Our troubled debt restructured loans are generally agreed to a short-term payment plan. The extent of these plans are generally limited to twelve-month payments and all the loans identified as troubled debt restructured as of December 31, 2012, were rate modifications. The Company does not extend maturities, recast legal documents and/or forgive any interest or principal.

As of December 31, 2012, loans modified in a troubled debt restructuring totaled $9.6 million, including $5.9 million that are current, $3.0 million that are 30-59 days past due, $221,000 that are 60-89 days past due and one non-accrual loan totaling $476,000. All loans modified in a troubled debt restructuring as of December, 2012 were current at the time of the modifications and were never reported as a non-accrual loan prior to modification.

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Note 3 – Loans Receivable and Allowance for Loan Losses (Continued)

The following tables represent financing receivables modified as troubled debt restructurings and with a payment default, with the payment default occurring within 12 months of the restructure date, and the payment default occurring during year ended December 31, 2012 and 2011:

	As of December 31, 2012	
Troubled Debt Restructuring That Subsequently Defaulted:	Number of Contracts	Recorded Investment
	(Dollars in Thousands)	
Commercial and industrial	-	$ -
Real estate – construction	-	-
Real estate – commercial	1	476
Real estate – residential	-	-
Consumer	-	-
Total	1	$ 476

	As of December 31, 2011	
Troubled Debt Restructuring That Subsequently Defaulted:	Number of Contracts	Recorded Investment
	(Dollars in Thousands)	
Commercial and industrial	-	$ -
Real estate – construction	-	-
Real estate – commercial	-	-
Real estate – residential	-	-
Consumer	2	252
Total	2	$ 252

As of December 31, 2012, there was one real estate commercial loan totaling $476,000 which was placed on non-accrual status that was previously a troubled debt restructured loan. This loan was individually analyzed for impairment at the time of default and it was determined that the collateral was in excess of the combined outstanding principal and interest of the loans and therefore no specific reserve was recorded nor charge-off was taken. It is the Company’s policy to classify a troubled debt restructured loan that is either 90 days or greater delinquent or that has been placed in a non-accrual status as a subsequently defaulted troubled debt restructured loan.

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Note 4 – Bank Premises and Equipment

Premises and equipment at December 31, 2012 and 2011 are as follows:

	Estimated Useful Lives	2012	2011
		(In Thousands)	
Land	Indefinite	$ 400	$ 400
Buildings	30 years	899	899
Leasehold improvements	5-15 years	4,516	4,281
Furniture and equipment	2 - 7 years	7,490	6,442
		13,305	12,022
Less accumulated depreciation and amortization		(10,062)	(9,382)
		$ 3,243	$ 2,640

The Company has land held for sale with an aggregate value of $1,000,000 at December 31, 2012 and 2011, which is included in other assets and is carried at the net realizable value, based on its current appraised value. No impairment charge was recorded during 2012 as compared to a $100,000 during 2011, which reflected the declining valuations in the current real estate market.

Note 5 – Goodwill and Other Intangible Assets

The Company's goodwill was recognized in connection with the acquisition of The Town Bank ("Town Bank") in April 2006. GAAP requires that goodwill be tested for impairment annually or more frequently if impairment indicators arise utilizing a two-step methodology. Step one requires the Company to determine the fair value of the reporting unit and compare it to the carrying value, including goodwill, of such reporting unit. The reporting unit was determined to be our community banking operations, which is our only operating segment. If the fair value of the reporting unit exceeds the carrying value, goodwill is not impaired. If the carrying value exceeds fair value, there is an indication of impairment and the second step is performed to determine the amount of impairment, if any. The second step compares the fair value of the reporting unit to the aggregate fair values of its individual assets, liabilities and identified intangibles.

The Company performed its annual step one goodwill impairment analysis as of September 30, 2012, and uses the fair value of the reporting unit based on the income approach and market approach. The income approach uses a dividend discount analysis. This approach calculates cash flows based on anticipated financial results assuming a change of control transaction. This change of control assumes that an acquirer will achieve an expected base level of earnings, achieve integration cost savings and incur certain transaction costs (including such items as legal and financial advisors fees, contract cancellations, severance and employment obligations, and other transaction costs). The present value of all excess cash flows generated by the Company (above the minimum tangible capital ratio) plus the present value of a terminal sale value is calculated to arrive at the fair value for the income approach.

The market approach is used to calculate the fair value of a company by calculating median earnings and book value pricing multiples for recent actual acquisitions of companies of similar size and performance and then applying these multiples to our community banking reporting unit. No company or transaction in the analysis is identical to our community banking reporting unit and, accordingly, the results of the analysis are only indicative of comparable value. This technique uses historical data to create a current pricing level and is thus a trailing indicator. Results of the market approach need to be understood in this context, especially in periods of rapid price change and market uncertainty. The Company applied the market valuation approach to our then current stock price adjusted by an appropriate control premium and also to a peer group adjusted by an appropriate control premium.

Based on the results of the step one goodwill impairment analysis, the Company determined that the potential for goodwill impairment did not exist and therefore a step two test was not required. Accordingly, no goodwill impairment was recorded on the goodwill balance of $18,109,000 for the years ended December 31, 2012 and 2011, respectively.

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Note 5 – Goodwill and Other Intangible Assets (Continued)

The Company acquired core deposit intangible assets in conjunction with the acquisition of Town Bank. This intangible asset has a carrying value of $268,000, net of accumulated amortization of $1,838,000, as of December 31, 2012 and a carrying value of $431,000, net of accumulated amortization of $1,675,000, as of December 31, 2011. Amortization expense related to intangible assets was $163,000 and $201,000 for the years ended December 31, 2012 and 2011, respectively.

The aggregate estimated amortization expense for the next four fiscal years is expected to be as follows (in thousands):

2013	$ 124
2014	86
2015	48
2016	10

Note 6 – Deposits

The components of deposits at December 31, 2012 and 2011 are as follows:

	2012	2011
	(In Thousands)	
Demand, non-interest bearing	$ 112,746	$ 88,209
Demand, interest bearing, money market and savings	394,317	352,025
Time, $100,000 and over	44,229	52,794
Time, other	55,478	60,884
	$ 606,770	$ 553,912

At December 31, 2012, the scheduled maturities of time deposits are as follows (in thousands):

2013	$ 52,519
2014	26,514
2015	11,320
2016	3,830
2017	3,393
Thereafter	2,131
	$ 99,707

The aggregate amounts of demand deposit overdrafts that have been reclassified as loan balances are $882,000 and $191,000 as of December 31, 2012 and 2011, respectively.

Note 7 – Securities Sold Under Agreements to Repurchase

Securities sold under agreements to repurchase, which are classified as secured borrowings, generally mature within one to four days from the transaction date. Securities sold under agreements to repurchase are reflected as the amount of cash received in connection with the transaction. Securities sold under these agreements are retained under the

Company's control at its safekeeping agent. The Company may be required to provide additional collateral based on the fair value of the underlying securities. Information concerning repurchase agreements for the years ended December 31, 2012 and 2011 is as follows:

	2012	2011
	(Dollars In Thousands)	
Repurchase agreements:		
Balance at year-end	$ 16,710	$ 16,218
Average during the year	18,266	16,593
Maximum month-end balance	19,860	19,524
Weighted average rate during the year	0.59 %	0.71 %
Weighted average rate at December 31	0.52 %	0.55 %

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Note 8 – Borrowings

Borrowings consist of long-term debt fixed rate advances from the FHLB. Information concerning long-term borrowings for the years ended December 31, 2012 and 2011 is as follows:

	2012	2011	Rate	Original Term	Maturity
	(Dollars In Thousands)				
Fixed Rate Note	$ 7,500	$ 7,500	3.97%	10 years	November 2017
Fixed Rate Note	1,500	1,500	1.67%	4 years	August 2014
Fixed Rate Note	1,500	1,500	2.00%	5 years	August 2015
Fixed Rate Note	1,500	1,500	2.41%	6 years	August 2016
Fixed Rate Note	1,500	1,500	2.71%	7 years	August 2017
	$ 13,500	$ 13,500	3.18%		

The Company has unsecured lines of credit totaling $17,000,000 with two financial institutions that bear interest at a variable rate and are renewed annually. There were no borrowings under these lines of credit at December 31, 2012 and 2011.

The Company has a remaining borrowing capacity with the FHLB of approximately $38,909,000 based on $52,409,000 loans pledged at December 31, 2012. There were no short-term borrowings from the FHLB at December 31, 2012 and 2011.

Note 9 – Employee Benefit Plans

Under the 401(k) plan, all employees are eligible to contribute up to 100% of their pay and bonus up to the IRS yearly limit. Annually, the Company matches a percentage of employee contributions. The Company contributed $241,000 and $229,000 for the years ended December 31, 2012 and 2011, respectively. Each year, the Company, may at its discretion, elect to contribute profit sharing amounts into the 401(k) plan. For the year ended December 31, 2012 and 2011, the Company has not contributed any profit sharing amounts.

The Company has a non-qualified Supplemental Executive Retirement Plan for certain executive officers that provides for payments upon retirement, death or disability. At December 31, 2012 and 2011, other liabilities included approximately $767,000 and $582,000, respectively, accrued under this plan. For the year ended December 31, 2012, expenses related to this plan included in the consolidated statements of operations are approximately $214,000 as compared to $91,000 for year ended December 31, 2011.

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Note 10 – Income Taxes

The components of income tax expense for the years ended December 31, 2012 and 2011 are as follows:

	2012	2011
	(In Thousands)	
Current	$ 3,502	$ 3,024
Deferred	(697)	(478)
	$ 2,805	$ 2,546

A reconciliation of the statutory income tax at a rate of 34% to the income tax expense included in the statements of operations is as follows for the years ended December 31, 2012 and 2011:

	2012		2011	
	Amount	%	Amount	%
	(Dollars In Thousands)			
Pre-tax book income	$ 2,591	34.0%	$ 2,330	34.0%
Tax exempt interest	(168)	(2.2)	(124)	(1.8)
Bank-owned life insurance income	(156)	(2.0)	(126)	(1.8)
State income taxes, net of federal income tax benefit	419	5.5	379	5.5
Other	119	1.5	87	1.2
	$ 2,805	36.8%	$ 2,546	37.1%

The components of the net deferred tax asset, included in other assets, as of December 31, 2012 and 2011, were as follows:

	2012	2011
	(In Thousands)	
Deferred tax assets:		
Allowance for loan losses	$ 3,210	$ 2,940
Depreciation and amortization	1,541	1,460
Deferred compensation	128	25
Other real estate owned (“OREO”) write-downs	327	183
Other	194	162
	5,400	4,770
Deferred tax liabilities:		
Purchase accounting adjustments	(333)	(402)
Unrealized gain on investment securities available for sale	(237)	(176)
Other	(247)	(245)

		(817)		(823)
Net Deferred Tax Asset	$	4,583	$	3,947

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Note 11 – Earnings Per Common Share

The following sets forth the computation of basic and diluted earnings per common share for the years ended December 31, 2012 and 2011:

	Years Ended December 31, 2012	2011
	(In Thousands, Except Per Share Data)	
Net income	$ 4,815	$ 4,308
Preferred stock dividends and discount accretion	(448)	(814)
Net income applicable to common shareholders	$ 4,367	$ 3,494
Weighted average common shares outstanding	7,950	7,900
Effect of dilutive securities, stock options	174	115
Weighted average common shares outstanding used to calculate diluted earnings per share	8,124	8,015
Basic earnings per common share	$ 0.55	$ 0.44
Diluted earnings per common share	$ 0.54	$ 0.44

Dilutive securities in the table above exclude common stock options with exercise prices that exceed the average market price of the Company's common stock during the periods presented. Inclusion of these common stock options would be anti-dilutive to the diluted earnings per common share calculation. Stock options that had no intrinsic value because their effect was anti-dilutive and, therefore, were not included in the diluted earnings per common share calculation were 345,000 and 474,000 for 2012 and 2011, respectively.

Note 12 – Lease Commitments and Total Rental Expense

The Company leases banking facilities under non-cancelable operating lease agreements expiring through 2022. Aggregate rent expense was $1,478,000 and $1,368,000 for the years ended December 31, 2012 and 2011, respectively.

The approximate future minimum rental commitments under operating leases at December 31, 2012 are as follows (in thousands):

2013	$ 1,223
2014	1,240
2015	1,215
2016	1,197
2017	1,493
Thereafter	3,360
	$ 9,728

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Note 13 – Stock Option Plans

Prior to the Company's formation in 2006, its banking subsidiaries had stock option plans, with outstanding stock options, for the benefit of their employees and directors. The plans provided for the granting of both incentive and non-qualified stock options. There are no shares of common stock remaining and available for future issuances under these plans.

On March 20, 2007, the Board of Directors adopted the Community Partners Bancorp 2007 Equity Incentive Plan (the "Plan"), which was approved by the Company's shareholders at the 2007 annual meeting. This plan provides that the Compensation Committee of the Board of Directors (the "Committee") may grant to those individuals who are eligible under the terms of the Plan stock options, shares of restricted stock, or such other equity incentive awards as the Committee may determine. As of December 31, 2012, the number of shares of Company common stock remaining and available for future issuance under the Plan is 245,504 after adjusting for subsequent stock dividends.

Options awarded under the Plan may be either options that qualify as incentive stock options ("ISOs") under section 422 of the Internal Revenue Code of 1986, as amended (the "Code"), or options that do not, or cease to, qualify as incentive stock options under the Code ("nonqualified stock options" or "NQSOs"). Awards may be granted under the Plan to directors and employees.

Shares reserved under the Plan will be issued out of authorized and unissued shares, or treasury shares, or partly out of each, as determined by the Board. The exercise price per share purchasable under either an ISO or a NQSO may not be less than the fair market value of a share of stock on the date of grant of the option. The Committee will determine the vesting period and term of each option, provided that no ISO may have a term in excess of ten years after the date of grant.

Restricted stock is stock which is subject to certain transfer restrictions and to a risk of forfeiture. The Committee will determine the period over which any restricted stock which is issued under the Plan will vest, and will impose such restrictions on transferability, risk of forfeiture and other restrictions as the Committee may in its discretion determine. Unless restricted by the Committee, a participant granted restricted stock will have all of the rights of a shareholder, including the right to vote the restricted stock and the right to receive dividends with respect to that stock.

Unless otherwise provided by the Committee in the award document or subject to other applicable restrictions, in the event of a Change in Control (as defined in the Plan) all non-forfeited options and awards carrying a right to exercise that was not previously exercisable and vested will become fully exercisable and vested as of the time of the Change in Control, and all restricted stock and awards subject to risk of forfeiture will become fully vested.

On December 11, 2012, the Committee granted officers incentive stock options to purchase an aggregate of 62,400 shares of Company common stock. These options are scheduled to vest 20% per year over five years beginning December 11, 2013. The options were granted with an exercise price of $5.49 per share based upon the average trading price of Company's common stock on the grant date.

On August 15, 2012, the Committee granted an officer incentive stock options to purchase an aggregate of 3,000 shares of Company's common stock. These options are scheduled to vest 25% per year over four years beginning August 14, 2014. These options were granted with an exercise price of $5.56 per share based upon the average trading price of Company's common stock on the grant date.

On March 21, 2012, the Committee granted an officer incentive stock options to purchase an aggregate of 3,000 shares of Company's common stock. These options are scheduled to vest 20% per year over five years beginning April 12, 2013. These options were granted with an exercise price of $5.75 per share based upon the average trading price of

Company's common stock on the grant date.

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Note 13 – Stock Option Plans (Continued)

On December 12, 2011, the Committee granted stock options to purchase an aggregate of 133,179 shares, after adjusting for the 3% stock dividend declared in November 2011, of Company common stock under the Plan to directors and officers of the Company, as follows:

- The Company granted to directors non-qualified stock options to purchase an aggregate of 61,800 shares of Company common stock. These options are scheduled to vest 20% per year over five years beginning December 12, 2012. These options were granted with an exercise price of $5.19 per share based upon the $4.69 trading price of Company’s common stock on the grant date.

- The Company granted to employees incentive stock options to purchase an aggregate of 71,379 shares of Company common stock. These options are scheduled to vest 20% per year over five years beginning December 12, 2012. The options were granted with an exercise price of $5.19 per share based upon the $4.69 trading price of Company’s common stock on the grant date.

Stock based compensation expense related to the stock option grants, was approximately $158,000 and $121,000 for the years ended December 31, 2012 and 2011, respectively, and is included in salaries and employee benefits on the statement of operations. There was no deferred tax benefit recognized during years ended December 31, 2012 and 2011 to the stock based compensation.

Total unrecognized compensation cost related to non-vested options under the Plan was $417,000 as of December 31, 2012 and will be recognized over the subsequent 3.2 years.

The following table summarizes information about outstanding options from all plans at and for the years ended December 31, 2012 and 2011, as adjusted for the 3% stock dividend in 2011:

	Number of Shares	Weighted Average Price	Weighted Average Remaining Contractual Life	Aggregate Intrinsic Value
Options outstanding, December 31, 2011	917,581	$6.82		
Options granted	68,400	5.50		
Options exercised	(37,130)	3.34		
Options forfeited	(27,246)	3.91		
Options outstanding, December 31, 2012	921,605	$6.95	4.9 years	$911,624
Options exercisable, end of year	610,593	$8.23	3.3 years	$552,848
Options price range at end of year	$3.01 to $14.17			

The total intrinsic value of stock options exercised was $76,000 and $137,000 during the years ended December 31, 2012 and 2011, respectively. Cash received from such exercises was $124,000 and $267,000, respectively. A tax benefit of $13,000 was recognized during the year ended December 31, 2012, as compared to $41,000 for the same period in 2011.

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Note 13 – Stock Option Plans (Continued)

The following summarizes information about stock options outstanding at December 31, 2012:

	Options Outstanding		
Range of Exercise Prices	Number Outstanding at December 31, 2012	Weighted-Average Remaining Contractual Life	Weighted-Average Exercise Price
\$3.01 - \$3.91	373,275	6.0 years	\$ 3.35
\$4.39 - \$4.94	14,156	4.8 years	4.39
\$5.01 - \$5.95	195,153	9.2 years	5.30
\$6.11 - \$6.38	563	0.8 years	6.27
\$7.23 - \$7.95	1,095	1.3 years	7.39
\$8.13 - \$9.86	61,664	0.2 years	8.27
\$11.17 - \$14.17	275,699	1.2 years	12.83
	921,605		

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model.

The following assumptions were used to estimate the fair value of the stock options granted on December 11, 2012:

Dividend yield	0.00%
Expected volatility	29.39%
Risk-free interest rate	1.06%
Forfeiture rate	5.00%
Expected life	7.5 years
Fair value of options granted	\$ 1.87

The following assumptions were used to estimate the fair value of the stock options granted on August 15, 2012:

Dividend yield	0.00%
Expected volatility	29.97%
Risk-free interest rate	1.18%
Forfeiture rate	0.00%
Expected life	7.5 years
Fair value of options granted	\$ 1.94

The following assumptions were used to estimate the fair value of the stock options granted on March 21, 2012:

Dividend yield	0.00%
Expected volatility	30.82%
Risk-free interest rate	1.40%
Forfeiture rate	0.00%
Expected life	7.5 years
Fair value of options granted	\$ 2.09

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Note 13 – Stock Option Plans (Continued)

The following assumptions were used to estimate the fair value of the stock options granted on December 12, 2011:

Dividend yield		0.00%
Expected volatility		30.58%
Risk-free interest rate		1.45%
Forfeiture rate		5.00%
Expected life		7.5 years
Fair value of options granted	$	1.53

The dividend yield assumption is based on the Company's history and expectations of cash dividends. The expected volatility is based on historical volatility. The risk-free interest rate is based on the U.S. Treasury yield curve for the expected life of the grants which is based on historical exercise experience.

Restricted stock is valued at the market value on the date of grant and expense is evenly attributed to the period in which the restrictions lapse.

Total unrecognized compensation cost related to restricted stock options under the Plan was $11,000 as of December 31, 2012 and will be recognized over the subsequent 0.9 years. As of December 31, 2011, all restricted stock shares were unvested.

On August 18, 2010, the Company awarded officers 20,600 shares of the Company's restricted common stock, which were subsequently issued on September 30, 2010. These awards are scheduled to vest on the first day of the fourth year following the grant date, with the award of 7,725 of these shares subject to an earnings condition. During 2012, the award of 3,863 of these shares were forfeited because earning conditions were not met.

On October 20, 2010, the Company awarded officers 1,442 shares of the Company's restricted common stock. These awards are scheduled to vest on the first day of the fourth year following the grant date, with the award of 541 of these shares subject to an earnings condition. During 2012, the award of 270 of these shares were forfeited because earning conditions were not met.

Compensation expense related to the restricted stock was to $25,000 and $33,000 for the years ended December 31, 2012 and 2011, respectively, and is included in salaries and employee benefits on the statement of operations. An $8,000 reversal of compensation expense was recorded during the first quarter of 2012 due to the forfeiture of restricted stock. There was no deferred tax benefit recognized during years ended December 31, 2012 and 2011 related to the restricted stock compensation.

The following table summarizes information about restricted stock for the year ended December 31, 2012:

	Number of Shares		Weighted Average Price
Unvested at December 31, 2010	22,042	$	3.93
Granted	-		-
Unvested at December 31, 2011	22,042	$	3.93
Forfeited	(4,133)		3.93

Unvested at December 31, 2012	17,909	$	3.93

All 2012 share and per share data have been retroactively adjusted to reflect the 3% stock dividend declared on November 10, 2011 payable on December 30, 2011 to shareholders of record as of December 13, 2011.

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Note 14 – Transactions with Executive Officers, Directors and Principal Shareholders

Certain directors and executive officers of Community Partners and its affiliates, including their immediate families and companies in which they are principal owners (more than 10%), are indebted to the Bank. In the opinion of management, such loans are consistent with sound banking practices and are within applicable regulatory bank lending limitations and in compliance with applicable rules and regulations of the Securities and Exchange Commission. Community Partners relies on such directors and executive officers for the identification of their associates. These loans at December 31, 2012 were current as to principal and interest payments, and did not involve more than normal risk of collectability. At December 31, 2012 and 2011, loans to related parties amounted to $12,930,000 and $12,771,000 respectively. During 2012, new loans and advances to such related parties totaled $327,000 and repayments and other reductions aggregated $168,000.

A director of the Bank is the principal of a company that provides leasehold improvement construction services for certain of the Bank's offices. The Bank paid $1,000 and $10,000 for these construction services for the years ended December 31, 2012 and 2011, respectively. Most costs are capitalized to leasehold improvements and are amortized over a ten to fifteen year period. Construction costs incurred are comparable to similarly outfitted bank office space in the market area.

Note 15 – Financial Instruments with Off-Balance Sheet Risk

The Company is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit and letters of credit. Those instruments involve, to varying degrees, elements of credit risk in excess of the amount recognized in the financial statements.

The Company's exposure to credit loss in the event of non-performance by the other party to the financial instrument for commitments to extend credit and letters of credit is represented by the contractual amount of those instruments. The Company uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. The Company evaluates each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Company upon extension of credit, is based on management's credit evaluation. Collateral held varies but may include personal or commercial real estate, accounts receivable, inventory and equipment. The Company had commitments to extend credit, including unused lines of credit, of approximately $122,905,000 and $156,205,000 at December 31, 2012 and 2011, respectively.

Standby letters of credit are conditional commitments issued by the Company to guarantee the financial performance of a customer to a third party. Those guarantees are primarily issued to support contracts entered into by customers. Most guarantees extend for one year. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. The Company defines the fair value of these letters of credit as the fees paid by the customer or similar fees collected on similar instruments. The Company amortizes the fees collected over the life of the instrument. The Company generally obtains collateral, such as real estate or liens on customer assets for these types of commitments. The Company's potential liability would be reduced by any proceeds obtained in liquidation of the collateral held. The Company had commercial and similar letters of credit for customers aggregating $4,195,000 and $5,066,000 at December 31, 2012 and 2011, respectively. The approximate value of underlying collateral upon liquidation that would be expected to cover this maximum potential exposure was $4,195,000 and $5,066,000 at December 31, 2012 and 2011, respectively. The current amounts of the liability related to guarantees under standby letters of credit issued are not material as of December 31, 2012 and 2011.

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Note 16 – Regulatory Matters

The Bank is required to maintain a cash reserve balance in vault cash or with the Federal Reserve Bank. The total of this reserve balance was $50,000 at December 31, 2012.

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

Quantitative measures established by regulations to ensure capital adequacy require the Company and the Bank maintain minimum amounts and ratios (set forth below) of total and Tier l capital (as defined in the regulations) to risk-weighted assets, and of Tier l capital to average assets. Management believes, as of December 31, 2012 that the Company and its bank subsidiary meet all capital adequacy requirements to which they are subject.

As of December 31, 2012, the Bank met all regulatory requirements for classification as well-capitalized under the regulatory framework for prompt corrective action. There are no conditions or events that management believes have changed the institutions' categories. Community Partners and the Bank's actual capital amounts and ratios at December 31, 2012 and 2011 and the minimum amounts and ratios required for capital adequacy purposes and to be well capitalized under the prompt corrective action provisions are as follows:

	Actual		For Capital Adequacy Purposes		To be Well Capitalized under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
			(Dollars in Thousands)			
As of December 31, 2012						
Total capital (to risk-weighted assets)						
Community Partners Bancorp	$ 80,835	13.28%	$ >48,696	>8.00%	$ N/A	N/A
Two River Community Bank	80,773	13.27%	>48,695	>8.00%	>60,869	>10.00%
Tier 1 capital (to risk-weighted assets)						
Community Partners Bancorp	73,220	12.03%	>24,346	>4.00%	N/A	N/A
Two River Community Bank	73,159	12.02%	>24,346	>4.00%	>36,519	>6.00%
Tier 1 capital (to average assets)						
Community Partners Bancorp	73,220	10.36%	>28,270	>4.00%	N/A	N/A
Two River Community Bank	73,159	10.35%	>28,274	>4.00%	>35,343	>5.00%
As of December 31, 2011						
Total capital (to risk-weighted assets)						
Community Partners Bancorp	$ 75,444	13.26%	$ >45,517	>8.00%	$ N/A	N/A
Two River Community Bank	75,340	13.25%	>45,488	>8.00%	>56,860	>10.00%

Tier 1 capital (to risk-weighted assets)						
Community Partners Bancorp	68,332	12.01%	>22,758	>4.00%	N/A	N/A
Two River Community Bank	68,229	12.00%	>22,743	>4.00%	>34,115	>6.00%
Tier 1 capital (to average assets)						
Community Partners Bancorp	68,332	10.39%	>26,307	>4.00%	N/A	N/A
Two River Community Bank	68,229	10.38%	>26,292	>4.00%	>32,866	>5.00%

The Bank is subject to certain legal and regulatory limitations on the amount of dividends that it may declare without prior regulatory approval. Under Federal Reserve regulations, the Bank is limited as to the amount it may lend affiliates, including the Company, unless such loans are collateralized by specific obligations.

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Note 17 – Fair Value of Financial Instruments

Accounting guidance establishes a fair value hierarchy that prioritizes the inputs to valuation methods used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are as follows:

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

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

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

An asset's or liability's level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement. For financial assets measured at fair value on a recurring basis, the fair value measurements by level within the fair value hierarchy used at December 31, 2012 and 2011 are as follows:

Description	(Level 1) Quoted Prices in Active Markets for Identical Assets	(Level 2) Significant Other Observable Inputs	(Level 3) Significant Unobservable Inputs	Total
		(In Thousands)		
At December 31, 2012				
Securities available for sale:				
Municipal securities	$ -	$ 1,310	$ -	$ 1,310
GSE: Residential mortgage-backed securities	-	20,374	-	20,374
Collateralized residential mortgage obligations		22,996	-	22,996
Corporate debt securities, primarily financial institutions	-	3,627	28	3,655
CRA mutual fund	2,421	-	-	2,421
Total	$ 2,421	$ 48,307	$ 28	$ 50,756
At December 31, 2011				
Securities available for sale:				
U.S. Government agency securities	$ -	$ 2,258	$ -	$ 2,258

Municipal securities		-		1,307		-		1,307
GSE: Residential mortgage-backed securities		-		21,878		-		21,878
Collateralized residential mortgage obligations				17,163		-		17,163
Corporate debt securities, primarily financial institutions		-		2,439		89		2,528
CRA mutual fund		2,321		-		-		2,321
Total	$	2,321	$	45,045	$	89	$	47,455

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Note 17 – Fair Value of Financial Instruments (Continued)

The following table presents a reconciliation of the securities available for sale measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the year ended December 31, 2012 and 2011:

	Fair Value Measurements Using Significant Unobservable Inputs (Level 3) Securities available for sale December 31, 2012	December 31, 2011
	(In Thousands)	
Beginning balance January 1	$ 89	$ 29
Total gains/(losses):		
Included in earnings	(80)	-
Included in other comprehensive income	19	60
Ending Balance	$ 28	$ 89

For assets measured at fair value on a nonrecurring basis, the fair value measurements by level within the fair value hierarchy used at December 31, 2012 and 2011 are as follows:

Description	(Level 1) Quoted Prices in Active Markets for Identical Assets	(Level 2) Significant Other Observable Inputs	(Level 3) Significant Unobservable Inputs	Total
		(In Thousands)		
At December 31, 2012				
Impaired loans	$ -	$ -	$ 6,246	$ 6,246
Other real estate owned	-	-	1,752	1,752
At December 31, 2011				
Impaired loans	$ -	$ -	$ 8,187	$ 8,187
Other real estate owned	-	-	7,765	7,765
Property held for sale	-	-	1,000	1,000

The following valuation techniques were used to measure fair value of assets in the tables above:

- Impaired loans – Impaired loans measured at fair value are those loans in which the Company has measured impairment generally based on the fair value of the loan's collateral. This method of fair value measurement is used on all of the Company's impaired loans. Fair value is generally determined based upon either independent third party appraisals of the properties or discounted cash flows based upon the expected proceeds. The appraisals may be adjusted by management for qualitative factors such as economic conditions and estimated liquidation expenses.

The discount range for appraisal values range from 0.0% to 5.0% (weighted average of 1.5%), and liquidation expenses range from 2.2% to 13.6% (weighted average of 6.7%). These assets are included as Level 3 fair values, based upon the lowest level of input that is significant to the fair value measurements.

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Note 17 – Fair Value of Financial Instruments (Continued)

- Other Real Estate Owned ("OREO") – Real estate properties acquired through, or in lieu of, loan foreclosure are to be sold and carried at fair value less cost to sell. Fair value is based upon the appraised value of the collateral, adjusted by management for factors such as economic conditions and other market factors. The discount range for collateral adjustment to OREO ranges from 3.5% to 8.5% (weighted average of 5.7%). These assets are included in Level 3 fair value based upon the lowest level of input that is significant to the fair value measurement. At December 31, 2012, properties totaling $1,752,000 as compared to $7,765,000 at December 31, 2011, were acquired through foreclosure and are carried at fair value less estimated selling costs based on current appraisals.

- Property held for sale – This real estate property is carried in other assets as property held for sale at fair value based upon the appraised value of the property.

The following information should not be interpreted as an estimate of the fair value of the entire Company since a fair value calculation is only provided for a limited portion of the Company's assets and liabilities. Due to a wide range of valuation techniques and the degree of subjectivity used in making the estimates, comparisons between the Company's disclosures and those of other companies may not be meaningful. The following methods and assumptions were used to estimate the fair values of the Company's financial instruments at December 31, 2012 and December 31, 2011:

Cash and Cash Equivalents (carried at cost):

The carrying amounts reported in the balance sheet for cash and short-term instruments approximate those assets' fair values.

Securities:

The fair value of securities available-for-sale (carried at fair value) and held to maturity (carried at amortized cost) are determined by obtaining quoted market prices on nationally recognized securities exchanges (Level 1), or matrix pricing (Level 2), which is a mathematical technique used widely in the industry to value debt securities without relying exclusively on quoted market prices for the specific securities but rather by relying on the securities' relationship to other benchmark quoted prices. For certain securities which 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 (Level 3). At December 31, 2012 and December 31, 2011, the Company determined that no active market existed for our one pooled trust preferred security. This security is classified as a Level 3 investment. Management's best estimate of fair value consists of both internal and external support on the Level 3 investment. Internal cash flow models project expected future interest and principal receivables due to our security based on the application of assumptions, including default probabilities, on the underlying preferred securities. The models then apply the resulting distributions from the underlying securities through the liability model, according to the deal's "priority of payments." For fair value purposes, a present value formula is then applied to our security's cash flows, steeply discounting the cash flows in accordance with the level of risk a reasonable market participant may demand for an investment such as ours. Due to the subordination of the security, discount margins contemplated in the valuation at December 31, 2012 ranged from Libor +15% to Libor +25%, with a midpoint of Libor +20%. The resultant fair values have been validated by means of comparison to indicative exit pricing obtained from broker/dealers (where available) were used to support the fair value of the Level 3 investment.

Restricted Investments (carried at cost):

The carrying amount of restricted investment in Federal Home Loan Bank stock, Atlantic Central Bankers Bank stock and Solomon Hess SBA Loan Fund approximates fair value, and considers the limited marketability of such securities.

Loans Receivable (carried at cost):

The fair values of loans, excluding collateral dependent impaired loans, are estimated using discounted cash flow analyses, using market rates at the balance sheet date that reflect the credit and interest rate-risk inherent in the loans, including liquidity. Projected future cash flows are calculated based upon contractual maturity or call dates, projected repayments and prepayments of principal. The valuation of the loan portfolio reflects discounts that the Company believes are consistent with transactions occurring in the marketplace for both performing and distressed loan types. The carrying value that fair value is compared to is net of the allowance for loan losses and other associated premiums and discounts. Generally, for variable rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying values. Due to the significant judgment involved in evaluating credit quality risk, loans are classified within level 3 of the fair value hierarchy.

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Note 17 – Fair Value of Financial Instruments (Continued)

Accrued Interest Receivable and Payable (carried at cost):

The carrying amount of accrued interest receivable and accrued interest payable approximates its fair value.

Deposit Liabilities (carried at cost):

The fair values disclosed for demand deposits (e.g., interest and noninterest checking, passbook savings and money market accounts) are, by definition, equal to the amount payable on demand at the reporting date, (i.e., their carrying amounts). Fair values for fixed-rate certificates of deposit are estimated using a discounted cash flow calculation that applies interest rates currently being offered in the market on certificates to a schedule of aggregated expected monthly maturities on time deposits.

Securities Sold Under Agreements to Repurchase (carried at cost):

The carrying amounts of these short-term borrowings approximate their fair values.

Long-term Debt (carried at cost):

Fair values of FHLB advances are estimated using discounted cash flow analysis, based on quoted prices for new FHLB advances with similar credit risk characteristics, terms and remaining maturity. These prices obtained from this active market represent a market value that is deemed to represent the transfer price if the liability were assumed by a third party.

Off-Balance Sheet Financial Instruments (disclosed at cost):

Fair values for the Company’s off-balance sheet financial instruments (lending commitments and letters of credit) are based on fees currently charged in the market to enter into similar agreements, taking into account, the remaining terms of the agreements and the counterparties’ credit standing. The fair values of such fees are not material at December 31, 2012 and 2011.

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Note 17 – Fair Value of Financial Instruments (Continued)

The estimated fair values of the Company’s financial instruments at December 31, 2012 were as follows:

		Fair Value Measurements at December 31, 2012			
(in thousands)	Carrying Amount	Estimated Fair Value	(Level 1) Quoted Prices in Active Markets for Identical Assets	(Level 2) Significant Other Observable Inputs	(Level 3) Significant Unobservable Inputs
Financial assets:					
Cash and cash equivalents	$ 48,546	$ 48,546	$ 48,546	$ -	$ -
Securities available for sale	50,756	50,756	2,421	48,307	28
Securities held to maturity	21,586	21,935	-	21,935	-
Restricted investments	3,040	3,040	-	-	3,040
Loans receivable	563,463	565,653	-	-	565,653
Accrued interest receivable	1,884	1,884	-	237	1,647
Financial liabilities:					
Deposits	606,770	608,329	-	608,329	-
Securities sold under agreements to repurchase	16,710	16,710	-	16,710	-
Long-term debt	13,500	14,921	-	14,921	-
Accrued interest payable	70	70	-	70	-
Off-balance sheet financial instruments:					
Commitments to extend credit and outstanding letters of credit	-	-	-	-	-

The estimated fair value of the Company’s financial instruments at December 31, 2011 were as follows:

	2011	
(in thousands)	Carrying Amount	Estimated Fair Value
Financial assets:		
Cash and cash equivalents	$ 38,022	$ 38,022
Securities available for sale	47,455	47,455
Securities held to maturity	13,105	13,222
Restricted investments	2,237	2,237
Loans receivable	522,820	516,174
Accrued interest receivable	1,928	1,928
Financial liabilities:		
Deposits	553,912	556,442

Securities sold under agreements to repurchase	16,218	16,218
Long-term debt	13,500	14,950
Accrued interest payable	107	107
Off-balance sheet financial instruments:		
Commitments to extend credit and outstanding letters of credit	-	-

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Note 18 – Shareholders' Equity

On August 11, 2011, the Company received $12 million under the Small Business Lending Fund ("SBLF"). The SBLF was created in the fall of 2010 as part of the Small Business Jobs Act. The SBLF provides Tier 1 capital to community banks with assets of $10 billion or less, and provides incentives for making small business loans, defined as certain loans of up to $10 million to businesses with up to $50 million in annual revenues. In exchange for the $12 million, the Company issued to the U.S. Department of the Treasury ("Treasury") 12,000 shares of its Non-Cumulative Perpetual Preferred Stock, Series C, having a $1,000 liquidation preference per share (the "SBLF Preferred Shares"). The SBLF Preferred Shares qualify as Tier 1 capital.

Dividend rates on the SBLF Preferred Shares are determined by the bank's lending practices with small business loans. The Company used a portion of the proceeds of the SBLF funds to redeem the full $9.0 million of its outstanding shares of Senior Preferred Stock, Series A, (the "TARP Preferred Shares"), previously issued to the Treasury under the Troubled Asset Relief Program Capital Purchase Plan ("TARP CPP"). The TARP Preferred Shares, issued under TARP CPP, qualified as Tier 1 capital and paid cumulative dividends at a rate of 5% per annum for the first five years.

The terms of the SBLF Preferred Shares impose limits on the ability of the Company to pay dividends and repurchase shares of common stock. Under the terms of the SBLF Preferred Shares, no repurchases may be effected, and no dividends may be declared or paid on preferred shares ranking pari passu with the SBLF Preferred Shares, junior preferred shares, or other junior securities (including the common stock) during the current quarter and for the next three quarters following the failure to declare and pay dividends on the SBLF Preferred Shares, except that, in any such quarter in which the dividend is paid, dividend payments on shares ranking pari passu may be paid to the extent necessary to avoid any resulting material covenant breach.

Under the terms of the SBLF Preferred Shares, the Company may only declare and pay a dividend on the common stock or other stock junior to the SBLF Preferred Shares, or repurchase shares of any such class or series of stock, if, after payment of such dividend, the dollar amount of the Company's Tier 1 Capital would be at least 90% of the Signing Date Tier 1 Capital, which is approximately $54.4 million, excluding any subsequent net charge-offs and any redemption of the SBLF Preferred Shares (the "Tier 1 Dividend Threshold"). Beginning on the first day of the eleventh dividend period, the amount of the Tier 1 Dividend Threshold will be reduced by 10% for each one percent increase in qualified small business lending from the baseline level through the ninth dividend period.

The noncumulative dividend rate on the SBLF Preferred Shares will be adjusted to reflect the amount of a change in the Company's qualified small business lending from its baseline, determined based upon the Company's qualified small business lending for each of the four full quarters ending June 30, 2010. Accordingly, the dividend rate will change as follows:

	Dividend Rate Following Investment Date		
Increase in Qualified Small Business Lending from the Baseline	First 9 Quarters*	Quarter 10 to Year 4.5	After Year 4.5
0% or less	5%	7%	9%
More than 0%, but less than 2.5%	5%	5%	9%
2.5% or more, but less than 5%	4%	4%	9%
5% or more, but less than 7.5%	3%	3%	9%
7.5% or more, but less than 10%	2%	2%	9%
10% or more	1%	1%	9%

* For the first nine quarters, the dividend rate will be adjusted quarterly.

After 10 years, if the SBLF Preferred Shares are not redeemed, the dividend rate will increase to the highest possible dividend rate as permitted by the Company's regulators. Dividends are payable quarterly on January 1, April 1, July 1 and October 1 of each year. During the three months ended December 31, 2012, the dividend rate was 4.323% and will be 3.511% and 2.000% for the first and second quarter of 2013, respectively.

On August 1, 2011, the Company distributed a dividend of one right (a "Right") for each outstanding share of the Company's common stock, to shareholders of record at the close of business on August 1, 2011 (the "Record Date"). Each Right entitles the registered holder to purchase from the Company one one-thousandth of a share of Series B Junior Participating Preferred Stock, at a purchase price of $25.00, subject to adjustment, (as so adjusted, the "Exercise Price"). The Rights are designed to protect shareholders from abusive takeover tactics and attempts to acquire control of the Company at an inadequate price. The Rights are not exercisable or transferable unless certain specified events occur.

Additionally, on October 26, 2011, the Company redeemed the TARP CPP warrant issued to the U.S. Treasury for $460,000.

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Note 19 – Condensed Financial Statements of Parent Company

Condensed financial information pertaining to the parent company, Community Partners, is as follows:

Condensed Balance Sheets

	December 31, 2012	2011
	(In Thousands)	
Assets		
Cash and cash equivalents	$ 114	$ 190
Investments in subsidiaries	91,904	87,031
Other assets	25	39
Total assets	$ 92,043	$ 87,260
Liabilities and Shareholders' Equity		
Other liabilities	$ 78	$ 126
Shareholders' equity	91,965	87,134
Total liabilities and shareholders' equity	$ 92,043	$ 87,260

Condensed Statements of Income

	December 31, 2012	2011
	(In Thousands)	
Other operating expenses	$ 175	$ 152
Loss before income taxes	(175)	(152)
Income tax expense	2	2
Loss before undistributed income of subsidiaries	(177)	(154)
Equity in undistributed income of subsidiaries	4,992	4,462
Net income	$ 4,815	$ 4,308

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Note 19 – Condensed Financial Statements of Parent Company (Continued)

Condensed Statements of Cash Flows

	December 31, 2012	December 31, 2011
	(In Thousands)	
Cash flows from operating activities:		
Net income	$ 4,815	$ 4,308
Adjustments to reconcile net income to net cash provided by operating activities:		
Equity in undistributed net income of subsidiaries	(4,992)	(4,462)
Stock option compensation expense	175	154
Other, net	191	578
Net cash provided by operating activities	189	578
Cash flows from investing activities:		
Contributions to subsidiary, net	-	(3,000)
Net cash used in investing activities	-	(3,000)
Cash flows from financing activities:		
Proceeds from exercise of stock options	124	267
Tax benefit of stock options exercised	13	41
Proceeds from issuance of preferred stock, Series C	-	12,000
Preferred stock, Series C issuance costs	-	(48)
Redemption of preferred stock, Series A	-	(9,000)
Redemption of preferred stock, Series A warrants	-	(460)
Proceeds from employee stock purchase program	46	32
Cash dividends paid on preferred stocks	(448)	(442)
Net cash (used in) provided by financing activities	(265)	2,390
Decrease in cash and cash equivalents	(76)	(32)
Cash and cash equivalents at beginning of period	190	222
Cash and cash equivalents at end of year	$ 114	$ 190

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Note 20 – Summary of Quarterly Results (Unaudited)

The following summarizes the consolidated results of operations during 2012 and 2011, on a quarterly basis, for Community Partners. Note that certain balances may not cross-foot due to rounding.

(in thousands, except per share data):

	2012			
	Fourth Quarter	Third Quarter	Second Quarter	First Quarter
Interest income	$ 7,762	$ 7,739	$ 7,609	$ 7,728
Interest expense	1,113	1,126	1,157	1,222
Net interest income	6,649	6,613	6,452	6,506
Provision for loan losses	430	330	270	350
Net interest income after provision for loan losses	6,219	6,283	6,182	6,156
Non-interest income	702	597	760	568
Non-interest expense	4,963	4,919	5,063	4,902
Income before income taxes	1,958	1,961	1,879	1,822
Income taxes	718	727	693	667
Net income	1,240	1,234	1,186	1,155
Preferred stock dividends	(130)	(31)	(150)	(137)
Net income available to common shareholders	$ 1,110	$ 1,203	$ 1,036	$ 1,018
Per common share data:				
Basic earnings	$ 0.14	$ 0.15	$ 0.13	$ 0.13
Diluted earnings	$ 0.14	$ 0.15	$ 0.13	$ 0.13

	2011			
	Fourth Quarter	Third Quarter	Second Quarter	First Quarter
Interest income	$ 7,739	$ 7,819	$ 7,843	$ 7,645
Interest expense	1,276	1,302	1,348	1,312
Net interest income	6,463	6,517	6,495	6,333
Provision for loan losses	350	730	600	525
Net interest income after provision for loan losses	6,113	5,787	5,895	5,808
Non-interest income	522	899	868	436
Non-interest expense	4,716	4,920	5,052	4,786
Income before income taxes	1,919	1,766	1,711	1,458
Income taxes	717	661	633	535

Net income		1,202		1,105		1,078		923
Preferred stock dividends & discount accretion		(126)		(402)		(143)		(143)
Net income available to common shareholders	$	1,076	$	703	$	935	$	780
Per common share data:								
Basic earnings	$	0.14	$	0.09	$	0.12	$	0.10
Diluted earnings	$	0.13	$	0.09	$	0.12	$	0.10

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SIGNATURES

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

COMMUNITY PARTNERS BANCORP

Date: March 29, 2013	By:	/s/ WILLIAM D. MOSS William D. Moss President and Chief Executive Officer

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.

Signature	Capacity	Date
/s/ FRANK J. PATOCK, JR. Frank J. Patock, Jr.	Chairman of the Board	March 29, 2013
/s/ CHARLES T. PARTON Charles T. Parton	Vice Chairman of the Board	March 29, 2013
/s/ JAMES M. BOLLERMAN James M. Bollerman	Director	March 29, 2013
/s/ ROBERT E. GREGORY Robert E. Gregory	Director	March 29, 2013
/s/ ROBERT B. GROSSMAN, MD Robert B. Grossman, MD	Director	March 29, 2013
/s/ JOHN E. HOLOBINKO, ESQ. John E. Holobinko, ESQ.	Director	March 29, 2013
/s/ WILLIAM F. LaMORTE William F. LaMorte	Director	March 29, 2013
/s/ JOSEPH F.X. O'SULLIVAN Joseph F.X. O'Sullivan	Director	March 29, 2013
/s/ JOHN J. PERRI, JR. CPA John J. Perri, Jr. CPA	Director	March 29, 2013
/s/ WILLIAM STATTER	Director	March 29, 2013

William Statter

/s/ ANDREW A. VITALE, CPA Andrew A. Vitale, CPA	Director	March 29, 2013
/s/ ROBIN ZAGER Robin Zager	Director	March 29, 2013

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/s/ WILLIAM D. MOSS William D. Moss	President, Chief Executive Officer, Director	March 29, 2013
/s/ A. RICHARD ABRAHAMIAN A Richard Abrahamian	Executive Vice President, Chief Financial Officer (Principal Financial and Accounting Officer)	March 29, 2013

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INDEX TO EXHIBITS

Exhibit No.		Description
3.1		Amended and Restated Certificate of Incorporation of the Registrant (incorporated by reference to Exhibit 3.1 to the Registrant's Registration Statement on Form S-3 (File No. 333-182855) filed with the SEC on July 26, 2012)
3.2		By-laws of the Registrant, as amended (incorporated by reference to Exhibit 3.2 to the Registrant's Quarterly Report on Form 10-Q (File No. 000-51889) for the quarterly period ended September 30, 2011 filed with the SEC on November 10, 2011)
4.1		Specimen certificate representing the Registrant's common stock, no par value per share (incorporated by reference to Exhibit 4.1 to the Registrant's Registration Statement on Form S-4/A filed with the SEC on January 6, 2006 (the "January S-4/A"))
4.2		Specimen certificate representing the Registrant's Senior Non-Cumulative Perpetual Stock, Series C, without par value (incorporated by reference to Exhibit 4.1 to the Registrant's Current Report on Form 8-K filed with the SEC on August 12, 2011)
4.3		Shareholder Rights Agreement, dated as of July 20, 2011, by and between the Registrant and Registrar and Transfer Company (incorporated by reference to Exhibit 4.1 to the Registrant's Current Report on Form 8-K filed with the SEC on July 26, 2011)
4.4		Form of Rights Certificate of the Registrant (incorporated by reference to Exhibit B to Exhibit 4.1 to the Registrant's Current Report on Form 8-K filed with the SEC on July 26, 2011)
10.0	#	Community Partners Bancorp Employee Stock Purchase Plan (incorporated by reference to Exhibit 4.3 to the Registrant's Registration Statement on Form S-8 filed with the SEC on February 18, 2011).
10.1	#	Supplemental Executive Retirement Agreement between Two River Community Bank and William D. Moss (incorporated by reference to Exhibit 10.5 to the S-4)
10.2	#	Supplemental Executive Retirement Agreement between Two River Community Bank and Alan Turner (incorporated by reference to Exhibit 10.8 to the S-4)
10.3	#	Two River Community Bank 2003 Incentive Stock Option Plan (incorporated by reference to Exhibit 10.9 to the S-4)
10.4	#	Two River Community Bank 2003 Non-qualified Stock Option Plan (incorporated by reference to Exhibit 10.10 to the S-4)
10.5		Services agreement between Two River Community Bank and Phoenix International Ltd., Inc. dated November 18, 1999, and subsequent amendment #1 dated February 1, 2005 (incorporated by reference to Exhibit 10.24 to the S-4)

10.6		Remote processing services agreement between Harland Financial Solutions, Inc. and Two River Community Bank, dated February 27, 2006
10.7	#	Community Partners Bancorp 2007 Equity Incentive Plan (incorporated by reference to Exhibit A to the Registrant's Definitive Proxy Statement on Schedule 14A filed with the SEC on April 17, 2007)
10.8		Form of Incentive Stock Option Agreement under 2007 Equity Incentive Plan
10.9		Form of Non-qualified Stock Option Agreement under 2007 Equity Incentive Plan

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10.10		Securities Purchase Agreement, effective August 11, 2011, between the Registrant and the United States Department of the Treasury (incorporated by reference to Exhibit 10.1 to the Registrant's Current Report on Form 8-K filed with the SEC on August 12, 2011)
10.11	#	First Amendment to the Two River Community Bank Supplemental Executive Retirement Agreement dated July 7, 2005 by and between Two River Community Bank and William D. Moss, effective as of January 1, 2005 (incorporated by reference to Exhibit 10.13 to the Registrant's Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2009 filed with the SEC on May 15, 2009)
10.12	#	First Amendment to the Two River Community Bank Supplemental Executive Retirement Agreement dated January 1, 2005 by and between Two River Community Bank and Alan B. Turner, effective as of January 1, 2005 (incorporated by reference to Exhibit 10.20 to the Registrant's Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2009 filed with the SEC on May 15, 2009)
10.13	#	Employment Agreement, effective as of May 28, 2010, by and between Community Partners Bancorp, Two River Community Bank and William D. Moss (incorporated by reference to Exhibit 10.1 to the Registrant's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2010 filed with SEC on August 16, 2010)
10.14	#	First Amendment to Employment Agreement, effective as of July 22, 2010, by and between Community Partners Bancorp, Two River Community Bank and William D. Moss (incorporated by reference to Exhibit 10.2 to the Registrant's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2010 filed with SEC on August 16, 2010)
10.15	#	Change in Control Agreement, effective as of June 1, 2010, by and between Community Partners Bancorp, Two River Community Bank and Alan B. Turner (incorporated by reference to Exhibit 10.3 to the Registrant's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2010 filed with SEC on August 16, 2010)
10.16	#	First Amendment to Change in Control Agreement, effective as of July 22, 2010, by and between Community Partners Bancorp, Two River Community Bank and Alan B. Turner (incorporated by reference to Exhibit 10.4 to the Registrant's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2010 filed with SEC on August 16, 2010)
10.17	#	Second Amendment to the Two River Community Bank Supplemental Executive Retirement Agreement dated March 1, 2010 by and between Two River Community Bank and Alan Turner
10.18	#	Second Amendment to the Two River Community Bank Supplemental Executive Retirement Agreement dated June 11, 2010 by and between Two River Community Bank and William D. Moss, effective as of June 1, 2010(incorporated by reference to Exhibit 10.5 to the Registrant's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2010 filed with SEC on August 16, 2010)
10.19	#	Third Amendment to the Two River Community Bank Supplemental Executive Retirement Agreement dated June 11, 2010 by and between Two River Community Bank and Alan B. Turner, effective as of June 1, 2010(incorporated by reference to Exhibit 10.6 to the

		Registrant's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2010 filed with SEC on August 16, 2010)
10.20	#	Change in Control Agreement, effective as of July 20, 2010, by and between Community Partners Bancorp, Two River Community Bank and A. Richard Abrahamian (incorporated by reference to Exhibit 10.7 to the Registrant's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2010 filed with SEC on August 16, 2010)
10.21	#	Restricted Stock Agreement, dated as of September 30, 2010, by and between Community Partners Bancorp, Two River Community Bank and William D. Moss and supplemented effective October 20, 2010 (incorporated by reference to Exhibit 10.1 to the Registrant's Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2010 filed with SEC on November 15, 2010)
10.22	#	Form of Restricted Stock Agreement (incorporated by reference to Exhibit 10.2 to the Registrant's Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2010 filed with SEC on November 15, 2010)
10.23	#	Change in Control Agreement, effective as of April 20, 2011, by and between Community Partners Bancorp, Two River Community Bank and Robert C. Werner (incorporated by reference to Exhibit 10.1 to the Registrant's Current Report on Form 8-K filed with SEC on April 21, 2011)

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10.24	#	Two River Community Bank 2012 Incentive Bonus Program (incorporated by reference to Exhibit 10.1 to the Registrant's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2012 filed with SEC on August 14, 2012)
21	*	Subsidiaries of the Registrant
23	*	Consent of Independent Registered Public Accounting Firm
31.1	*	Certification of William D. Moss, President and Chief Executive Officer of the Registrant, pursuant to Securities Exchange Act Rule 13a-14(a)
31.2	*	Certification of A. Richard Abrahamian, Chief Financial Officer of the Registrant, pursuant to Securities Exchange Act Rule 13a-14(a)
32	*	Certifications pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of The Sarbanes-Oxley Act of 2002, signed by William D. Moss, President and Chief Executive Officer of the Registrant, and A. Richard Abrahamian, Chief Financial Officer of the Registrant

101.INS**	XBRL Instance Document
101.SCH**	XBRL Taxonomy Extension Schema
101.CAL**	XBRL Taxonomy Extension Calculation Linkbase
101.DEF**	XBRL Taxonomy Extension Definition Linkbase
101.LAB**	XBRL Taxonomy Extension Label Linkbase
101.PRE**	XBRL Taxonomy Extension Presentation Linkbase

* Filed herewith.

** Pursuant to Rule 406T of Regulation S-T, these interactive data files are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933 or Section 18 of the Securities Exchange Act of 1934 and otherwise are not subject to liability.

\# Management contract or compensatory plan or arrangement.