

Colonial American Bank

Financial Statements

December 31, 2012 and 2011



Colonial American Bank

Table of Contents

December 31, 2012 and 2011

	<u>Page</u>
Independent Auditors' Report	1
Financial Statements	
Balance Sheets	3
Statements of Operations and Comprehensive Loss	4
Statements of Shareholders' Equity	5
Statements of Cash Flows	6
Notes to Financial Statements	7

Independent Auditors' Report

Board of Directors
Colonial American Bank

Report on the Financial Statements

We have audited the accompanying financial statements of Colonial American Bank which comprise the balance sheet as of December 31, 2012 and 2011, and the related statements of operations and other comprehensive loss, changes in shareholders' equity, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Colonial American Bank as of December 31, 2012 and 2011 and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Parente Beard LLC

Philadelphia, Pennsylvania
March 21, 2013

COLONIAL AMERICAN BANK
Balance Sheets

	At December 31,	
	2012	2011
	(In thousands, except share data)	
Assets		
Cash and due from banks	\$ 373	\$ 360
Interest-bearing deposits with banks	4,922	4,700
Cash and cash equivalents	5,295	5,060
Securities available-for-sale, at estimated fair value	52,683	5,267
Loans held-for-sale	4,015	-
Loans held-for-investment, net	71,444	32,508
Allowance for loan losses	(1,226)	(466)
Net loans held-for-investment	70,218	32,042
Premises and equipment, net	2,297	563
Federal Home Loan Bank of Pittsburgh stock, at cost	726	345
Foreclosed assets	189	189
Accrued interest receivable and other assets	763	582
Total assets	\$ 136,186	\$ 44,048
Liabilities and Shareholders' Equity		
Liabilities		
Deposits:		
Noninterest-bearing demand	\$ 5,015	\$ 1,265
Interest-bearing demand	2,144	1,202
Money market deposit accounts	31,179	9,092
Savings	2,903	7,001
Time	64,306	10,802
Total deposits	105,547	29,362
Borrowings	14,000	-
Due to broker	4,562	-
Accrued interest payable and other accrued liabilities	490	646
Total liabilities	124,599	30,008
Shareholders' Equity		
Common stock, \$1 par value, \$7,500,000 shares authorized; 1,804,850 shares issued and outstanding at December 31, 2012 and 2011, respectively	1,805	1,805
Additional paid-in-capital	23,220	22,989
Accumulated deficit	(13,925)	(10,897)
Accumulated other comprehensive income	487	143
Total shareholders' equity	11,587	14,040
Total liabilities and shareholders' equity	\$ 136,186	\$ 44,048

See notes to financial statements

COLONIAL AMERICAN BANK
Statements of Operations and Comprehensive Loss

	Years Ended December 31,	
	2012	2011
	(In thousands)	
Interest Income		
Loans, including fees	\$ 2,314	\$ 1,169
Securities	680	95
Deposits in other financial institutions	4	11
Total interest income	2,998	1,275
Interest Expense		
Deposits	941	320
Borrowings	5	-
Total interest expense	946	320
Net interest income	2,052	955
Provision For Loan Losses	905	741
Net interest income after provision for loan losses	1,147	214
Non-Interest Income		
Service charges and fees	13	16
Gain on securities transactions, net	555	-
Gain on sales of loans, net	133	-
Other	21	9
Total non-interest income	722	25
Non-Interest Expense		
Compensation and benefits, net	2,725	1,810
Occupancy	570	284
Data processing	310	291
Professional services	426	610
Other	866	1,082
Total non-interest expense	4,897	4,077
Income Tax Expense	-	-
Net loss	\$ (3,028)	\$ (3,838)
Preferred stock dividends and discount accretion	\$ -	\$ (23)
Net loss attributable to common shareholders	\$ (3,028)	\$ (3,861)
Other comprehensive income, before tax:		
Unrealized gains on securities:		
Net unrealized holding gains on securities	\$ 344	\$ 143
Other comprehensive income, before tax	344	143
Income tax expense related to items of other comprehensive income	-	-
Other comprehensive income, net of tax	344	143
Comprehensive loss	\$ (2,684)	\$ (3,695)

See notes to financial statements

COLONIAL AMERICAN BANK
Statements of Changes in Shareholders' Equity

Years Ended December 31, 2012 and 2011

	Preferred Stock	Common Stock	Additional Paid-in Capital	Accumulated Deficit	Accumulated Other Comprehensive Income	Total
	(In thousands, except share data)					
Balance, January 1, 2011	\$ 1	\$ 50	\$ 8,520	\$ (7,059)	\$ -	\$ 1,512
Sale of 1,754,138 shares of common stock as part of the recapitalization		1,754	14,957			\$ 16,711
Common stock issued		1	4			\$ 5
Redemption of preferred stock (TARP)	(574)					\$ (574)
Accretion of discount on preferred stock and redemption charge	573		(602)			\$ (29)
Dividends on preferred stock			(20)			\$ (20)
Stock compensation expense			130			\$ 130
Net loss				(3,838)		\$ (3,838)
Other comprehensive income (net of tax of \$0)					143	\$ 143
Balance, December 31, 2011	<u>\$ -</u>	<u>\$ 1,805</u>	<u>\$ 22,989</u>	<u>\$ (10,897)</u>	<u>\$ 143</u>	<u>\$ 14,040</u>
Stock compensation expense			231			\$ 231
Net loss				(3,028)		\$ (3,028)
Other comprehensive income (net of tax of \$0)					344	\$ 344
Balance, December 31, 2012	<u>\$ -</u>	<u>\$ 1,805</u>	<u>\$ 23,220</u>	<u>\$ (13,925)</u>	<u>\$ 487</u>	<u>\$ 11,587</u>

See notes to financial statements

COLONIAL AMERICAN BANK
Statements of Cash Flows

	Years Ended December 31,	
	2012	2011
	(In thousands)	
Operating Activities		
Net loss	\$ (3,028)	\$ (3,838)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation & amortization	231	117
Provision for loan losses	905	741
Amortization of premiums and discounts on securities, and deferred loan fees and costs	251	13
Stock compensation expense	231	130
Net gain on sale of loans held-for-sale	(133)	-
Proceeds from sale of loans held-for-sale	7,037	-
Origination of loans held-for-sale	(10,919)	-
Gain on securities transactions, net	(555)	-
Write-down of other real estate owned	-	21
Increase in accrued interest receivable and other assets	(181)	(338)
Increase in accrued interest payable and other accrued liabilities	4,406	467
Net cash used in operating activities	(1,755)	(2,687)
Investing Activities		
Purchases of securities available-for-sale	(82,204)	(5,959)
Proceeds from maturities and principal repayments of securities available-for-sale	3,741	819
Proceeds from sales of securities available-for-sale	31,904	-
(Purchase) redemption of Federal Home Loan Bank of Pittsburgh stock, net	(381)	78
Net increase in loans	(39,290)	(16,401)
Purchases of premises and equipment	(1,965)	(540)
Proceeds from sales of foreclosed assets	-	48
Net cash used in investing activities	(88,195)	(21,955)
Financing Activities		
Redemption of preferred stock	-	(603)
Cash dividends on preferred stock	-	(20)
Net proceeds from sale of common stock	-	16,716
Net increase in deposits	76,185	9,991
Net increase in borrowings	14,000	-
Net cash provided by financing activities	90,185	26,084
Net increase in cash and cash equivalents	235	1,442
Cash and Cash Equivalents, Beginning of Year	5,060	3,618
Cash and Cash Equivalents, End of Year	\$ 5,295	\$ 5,060
Supplementary Cash Flow Information		
Cash paid during the year for:		
Interest paid	\$ 944	\$ 313
Dividends	-	20
Non-cash transactions:		
Transfer of loan to other real estate owned	-	189

See notes to financial statements

Colonial American Bank

Notes to Financial Statements
December 31, 2012 and 2011

1. Nature of Operations

Colonial American Bank (the "Bank") is a state chartered bank, which was incorporated on September 1, 2006 under the laws of the Commonwealth of Pennsylvania. The Bank commenced operations on February 9, 2007. The Bank is chartered by the Pennsylvania Department of Banking and insured by the Federal Deposit Insurance Corporation ("FDIC"). The Bank maintains its principal branch office in Horsham, Pennsylvania and provides financial services primarily in Montgomery County and the surrounding counties of the Greater Delaware Valley. In January 2012, the Bank received regulatory approval to expand its branch network into the State of New Jersey, and opened a branch in Middletown, New Jersey in March 2012. In connection with the opening of the branch, the Bank established a second trade area in Monmouth County, New Jersey. The Bank currently has a second New Jersey branch under construction and has recently been approved by the New Jersey Department of Banking and Insurance to convert from a Pennsylvania chartered commercial bank to a New Jersey chartered commercial bank. As a result, the Bank will close its office located in Horsham, Pennsylvania effective on, or about, March 29, 2013. The Bank's new principal office will be located in Middletown, New Jersey.

On September 7, 2010, the Bank executed a Securities Purchase Agreement (the "Agreement") with a group of investors unrelated to Colonial American Bank to purchase up to \$25.0 million of newly issued common stock of Colonial American Bank directly from the Bank. The Agreement was subject to certain terms and conditions as outlined in the Agreement, and subject to regulatory approvals. On April 15, 2011, the Bank closed upon the Agreement, with the investor group raising \$17.5 million in new capital for the Bank (the "Recapitalization"). In connection with the closing of the Recapitalization, the entire Board of Directors immediately prior to the closing resigned, and a new slate of directors was appointed to the Board. In addition, a new management team was hired subsequent to the Recapitalization.

2. Summary of Significant Accounting Policies

The following significant accounting and reporting policies of the Bank, conform to accounting principles generally accepted in the United States of America, or ("GAAP"), and are used in preparing and presenting these financial statements.

Basis of Presentation

In preparing the financial statements, management is required 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 periods. Actual results may differ significantly from those estimates and assumptions. Material estimates that are particularly susceptible to significant change in the near term are the allowance for loan losses, estimates of fair value of financial instruments, other-than-temporary impairment of investment securities, and the realization of net deferred tax assets. In connection with the determination of this allowance, management generally obtains independent appraisals for significant properties. Judgments related to securities valuation and impairment, and deferred income taxes involve a higher degree of complexity and subjectivity and require estimates and assumptions about highly uncertain matters. Actual results may differ from the estimates and assumptions.

Certain prior year balances have been reclassified to conform to the current year presentation.

Colonial American Bank

Notes to Financial Statements
December 31, 2012 and 2011

Cash and Cash Equivalents

Cash and cash equivalents include cash on hand, interest bearing deposits with other banks, and federal funds sold, all of which mature within ninety days.

Investment Securities

In accordance with applicable accounting standards, the Bank classifies its investment securities into one of three portfolios: held to maturity; available for sale or trading. Investments in debt securities that we have the positive intent and ability to hold to maturity are classified as held to maturity securities and reported at amortized cost. Debt and equity securities that are bought and held principally for the purpose of selling them in the near term are classified as trading securities and reported at fair value, with unrealized holding gains and losses included in earnings. Debt and equity securities not classified as trading securities or as held to maturity securities are classified as available for sale securities and reported at fair value, with unrealized holding gains or losses, net of deferred income taxes, reported in the accumulated other comprehensive income ("OCI") component of shareholders' equity.

If the fair value of a security is less than its amortized cost, the security is deemed to be impaired. Management evaluates all securities with unrealized losses quarterly to determine if such impairments are "temporary" or "other-than-temporary".

The Bank accounts for temporary impairments based upon their classification as either available for sale, held to maturity or managed within a trading portfolio. Temporary impairments on "available for sale" securities are recognized, on a tax-effected basis, through OCI with offsetting entries adjusting the carrying value of the security and the balance of deferred taxes. Conversely, the Bank does not adjust the carrying value of "held to maturity" securities for temporary impairments, although information concerning the amount and duration of impairments on held to maturity securities is generally disclosed in periodic financial statements. The carrying value of securities held in a trading portfolio is adjusted to their fair value through earnings on a daily basis. However, the Bank did not maintain a trading or held-to-maturity portfolio at or during the periods presented in these financial statements.

The Bank accounts for other-than-temporary impairments based upon several considerations. First, other-than-temporary impairments on securities that the Bank has decided to sell as of the close of a fiscal period, or will, more likely than not, be required to sell prior to the full recovery of their fair value to a level equal to or exceeding their amortized cost, are recognized in earnings. If neither of these conditions regarding the likelihood of the securities' sale are applicable, then, for debt securities, the other-than-temporary impairment is bifurcated into credit-related and noncredit-related components. A credit-related impairment generally represents the amount by which the present value of the cash flows that are expected to be collected on a debt security fall below its amortized cost. The noncredit-related component represents the remaining portion of the impairment not otherwise designated as credit-related. The Bank recognizes credit-related, other-than-temporary impairments in earnings. However, noncredit-related related component is recognized in OCI.

Colonial American Bank

Notes to Financial Statements
December 31, 2012 and 2011

Premiums and discounts on all securities are generally amortized/accreted to maturity by use of the level-yield method considering the impact of principal amortization and prepayments on mortgage-backed securities. Premiums on callable securities are generally amortized to the call date whereas discounts on such securities are accreted to the maturity date. Gain or loss on sales of securities is based on the specific identification method.

Federal Home Loan Bank and Atlantic Central Bankers Bank Stock

Federal law requires a member institution of the Federal Home Loan Bank (“FHLB”) system to hold restricted stock of its district Federal Home Loan Bank according to a predetermined formula. Restricted stock of the Federal Home Loan Bank of Pittsburgh in the amount of \$726,000 and \$345,000 is carried at cost at December 31, 2012 and 2011, respectively.

Management’s determination of whether these investments are impaired is based on an assessment of the ultimate recoverability of their cost, rather than by recognizing temporary declines in value. The determination of whether a decline affects the ultimate recoverability of cost is influenced by criteria such as (1) the significance of the decline in net assets of the FHLB as compared to the capital stock amount for the FHLB and the length of time this situation has persisted, (2) commitments by the FHLB to make payments required by law or regulation and the level of such payments in relation to the operating performance of the FHLB, and (3) the impact of legislative and regulatory changes on institutions and, accordingly, on the customer base of the FHLB.

The Bank also held \$50,000 of stock in the Atlantic Central Bankers Bank (“ACBB”), at December 31, 2012 and 2011. Management believes no impairment charge is necessary related to the FHLB restricted stock or the ACBB stock as of December 31, 2012 or 2011.

Loans Held-for-Sale

Loans originated and intended for sale in the secondary market are carried at the lower of cost or estimated fair value. For loans carried at the lower of cost or estimated fair value, gains and losses on loan sales (sales proceeds minus carrying value) are recorded in non-interest income, and direct loan origination costs and fees are deferred at origination of the loan and are recognized in non-interest income upon sale of the loan.

Loans Receivable and Allowance for Loan Losses

Loans receivable, which management has the intent and ability to hold for the foreseeable future or until maturity or payoff, are stated at unpaid principal balance, adjusted by unamortized premiums and unearned discounts, deferred origination fees and certain direct origination costs, and the allowance for loan losses. The loan receivable portfolio is segmented into residential mortgages, commercial real estate, home equity and lines of credit, construction, multifamily, commercial and industrial, and consumer loans.

Residential mortgage loans and home equity and lines of credit involve certain risks such as interest rate risk and risk of nonrepayment. Adjustable-rate loans decrease the interest rate risk to the Bank that is associated with changes in interest rates but involve other risks, primarily because as interest rates rise, the payment by the borrower rises to the extent permitted by the terms of the loan, thereby increasing the potential for default. At the same time, the marketability of the underlying property may be adversely affected by higher interest rates. Repayment risk can be affected by job loss, divorce, illness and personal bankruptcy or the borrower.

Colonial American Bank

Notes to Financial Statements
December 31, 2012 and 2011

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

Construction lending is generally considered to involve a high degree of risk due to the concentration of principal in a limited number of loans and borrowers and the effects of general economic conditions on developers and builders. Moreover, a construction loan can involve additional risks because of the inherent difficulty in estimating both a property's value at completion of the project and the estimated cost (including interest) of the project. The nature of these loans is such that they are generally difficult to evaluate and monitor. In addition, speculative construction loans to a builder are not necessarily for projects which are pre-sold or leased, and thus pose a greater potential risk to the Bank than construction loans to individuals on their personal residences.

Multifamily lending entails additional risks as compared with single-family residential property lending, but less when compared to commercial real estate lending. The payment experience on such loans is typically dependent on the successful operation of the multifamily project. The success of such projects is sensitive to changes in supply and demand conditions in the market as well as economic conditions generally.

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

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

Interest income on loans is accrued and credited to income as earned. Net loan origination fees/costs are deferred and accreted/amortized to interest income over the loan's contractual life using the level-yield method, adjusted for actual prepayments.

Colonial American Bank

Notes to Financial Statements
December 31, 2012 and 2011

The Bank defines an impaired loan as a loan for which it is probable, based on current information, that the Bank will not collect all amounts due in accordance with the contractual terms of the loan agreement. The Bank has defined the population of impaired loans to be all non-accrual loans, loans risk rated 8 (Doubtful) or 9 (Loss), and all loans subject to a troubled debt restructuring. Impaired loans are individually assessed to determine that the loan's carrying value is not in excess of the expected future cash flows, discounted at the loan's original effective interest rate, or the underlying collateral (less estimated costs to sell) if the loan is collateral dependent. Impairments are recognized through a charge to the provision for loan losses for the amount that the loan's carrying value exceeds the discounted cash flow analysis or estimated fair value of collateral (less estimated costs to sell) if the loan is collateral dependent.

The allowance for loan losses is increased by the provision for loan losses charged against income and is decreased by charge-offs, net of recoveries. Loan losses are charged-off in the period the loans, or portion thereof, are deemed uncollectible. Generally, the Bank will record a loan charge-off (including a partial charge-off) to reduce a loan to the estimated fair value of the underlying collateral, less cost to sell, if it is determined that it is probable that recovery will come primarily from the sale of such collateral. The provision for loan losses is based on management's evaluation of the adequacy of the allowance which considers, among other things, impaired loans, past loan loss experience, known and inherent risks in the portfolio, existing adverse situations that may affect the borrower's ability to repay, and estimated fair value of any underlying collateral securing loans. Additionally, management evaluates changes, if any, in underwriting standards, collection, charge-off and recovery practices, the nature or volume of the portfolio, lending staff, concentration of loans, as well as current economic conditions, and other relevant factors. Management believes the allowance for loan losses is adequate to provide for probable and reasonably estimable losses at the date of the balance sheets. The Bank also maintains an allowance for estimated losses on off-balance sheet credit risks related to loan commitments and standby letters of credit. Management utilizes a methodology similar to its allowance for loan loss adequacy methodology to estimate losses on these commitments. The allowance for estimated credit losses on off-balance sheet commitments is included in other liabilities and any changes to the allowance are recorded as a component of other non-interest expense.

While management uses available information to recognize probable and reasonably estimable losses on loans, future additions may be necessary based on changes in conditions, including changes in economic conditions, particularly in the counties in which the Bank operates. Accordingly, as with most financial institutions in the market area, the ultimate collectibility of a substantial portion of the Bank's loan portfolio is susceptible to changes in conditions in the Bank's marketplace. In addition, future changes in laws and regulations could make it more difficult for the Bank to collect all contractual amounts due on its loans and mortgage-backed securities.

In addition, various regulatory agencies, as an integral part of their examination process, periodically review the Bank's allowance for loan losses. Such agencies may require the Bank to recognize additions to the allowance based on their judgments about information available to them at the time of their examination.

Colonial American Bank

Notes to Financial Statements
December 31, 2012 and 2011

A loan modification is deemed a troubled debt restructuring (“TDR”) when two conditions are met: 1) the borrower is experiencing financial difficulty; and 2) a concession is made by the Bank that would not otherwise be considered for a borrower or collateral with similar credit risk characteristics. Once an obligation has been restructured, it continues to be considered restructured until paid in full or, if the obligation yields a market rate (a rate equal to or greater than the rate the Bank was willing to accept at the time of the restructuring for a new loan with comparable risk), until the year subsequent to the year in which the restructuring takes place, provided the borrower has performed under the modified terms for a six-month period. The Bank records an impairment charge equal to the difference between the present value of estimated future cash flows under the restructured terms discounted at the original loan’s effective interest rate, or the underlying collateral value less costs to sell, if the loan is collateral dependent. Changes in present values attributable to the passage of time are recorded as a component of the provision for loan losses.

A loan is considered past due when it is not paid in accordance with its contractual terms. The accrual of income on loans, including impaired loans, and other loans in the process of foreclosure, is generally discontinued when a loan becomes 90 days or more delinquent, or when certain factors indicate that the ultimate collection of principal and interest is in doubt. Loans on which the accrual of income has been discontinued are designated as non-accrual loans. All previously accrued interest is reversed against interest income, and income is recognized subsequently only in the period that cash is received, provided no principal payments are due and the remaining principal balance outstanding is deemed collectible. A non-accrual loan is not returned to accrual status until both principal and interest payments are brought current and factors indicating doubtful collection no longer exist, including performance by the borrower under the loan terms for a six-month period.

Premises and Equipment

Premises and equipment are stated at cost less accumulated depreciation and amortization. Depreciation is computed using the straight-line method and charged to expense over the estimated useful lives of the assets. Leasehold improvements are amortized to expense over the shorter of the term of the respective lease or the estimated useful life of the improvements. The estimated useful lives of furniture and equipment is five to fifteen years.

Foreclosed Assets

Foreclosed assets are comprised of property acquired through a foreclosure proceeding or acceptance of a deed-in-lieu of foreclosure. Foreclosed assets are held for sale and are initially recorded at estimated fair value, net of estimated selling costs, at the date of foreclosure establishing a new cost basis. Costs after acquisition are generally expensed. If the estimated fair value of the asset declines, a write-down is recorded through other non-interest expense.

Colonial American Bank

Notes to Financial Statements
December 31, 2012 and 2011

Income Taxes

The Bank accounts for income taxes in accordance with income tax accounting guidance (Financial Accounting Standards Board (“FASB”) Accounting Standards Codification (“ASC”) Topic 740, *Income Taxes*).

Federal and state income taxes have been provided on the basis of reported income or loss. The amounts reflected on the tax returns differ from these provisions due principally to temporary differences in the reporting of certain items for financial reporting and income tax reporting purposes. The tax effect of these temporary differences is accounted for as deferred taxes applicable to future periods. Deferred income tax expense or benefit is determined by recognizing deferred tax assets and liabilities for the estimated future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred assets and liabilities of a change in tax rates is recognized in earnings in the period that includes the enactment date. The realization of deferred tax assets is assessed and a valuation allowance provided for the full amount which is not more likely than not to be realized.

The Bank had no material unrecognized tax benefits or accrued interest and penalties as of December 31, 2012 and 2011. The Bank’s policy is to account for interest as a component of interest expense and penalties as a component of other expense.

The Bank files both federal and state income tax returns. The Bank is no longer subject to examination by taxing authorities for the years before January 1, 2009.

Stock-Based Compensation

The Bank accounts for its stock based compensation plans under the provisions of FASB ASC Topic 718, Compensation — Stock Compensation, which requires recognizing expense for options granted equal to the grant-date fair value of the unvested amounts over their remaining vesting period. The expense related to stock options is based on the estimated fair value of the options at the date of the grant using the Black-Scholes pricing model. The awards are fixed in nature and compensation cost related to stock based awards is recognized on a straight-line basis over the requisite service periods. Excess tax benefits arising from increases in the value of equity instruments issued under stock-based payment arrangements are treated as cash inflows from financing activities.

Comprehensive Income (Loss)

Comprehensive income (loss) consists of net income (loss) and other comprehensive income (loss). Other comprehensive income (loss) includes unrealized gains or losses on securities available-for-sale which are also recognized as a separate component of shareholders’ equity.

Colonial American Bank

Notes to Financial Statements
December 31, 2012 and 2011

Fair Value of Financial Instruments

For information on the fair value of the Bank's financial instruments refer to Note 11 – "Fair Value Measurement" of the financial statements.

Restrictions on Cash and Amounts Due from Banks

The Bank does not have any requirements to maintain balances with the Federal Reserve Bank at December 31, 2012 and 2011.

Recent Accounting Pronouncements

In October 2012, the FASB issued Accounting Standard Update ("ASU") 2012-04, "Technical Corrections and Improvements". This Update represents changes to clarify the Codification, correct unintended application of guidance, and make minor improvements to the Codification that are not expected to have a significant effect on current accounting practice or create a significant administrative cost to most entities. Additionally, this Update will make the Codification easier to understand and the fair value measurement guidance easier to apply by eliminating inconsistencies and providing needed clarifications. The amendments in this Update that will not have transition guidance will be effective upon issuance for both public entities and nonpublic entities. For public entities, the amendments that are subject to the transition guidance will be effective for fiscal periods beginning after December 15, 2012. For nonpublic entities, the amendments that are subject to the transition guidance will be effective for fiscal periods beginning after December 15, 2013. The adoption of ASU 2012-04 is not expected to have a significant impact on the Bank's financial statements.

In December 2011, the FASB issued ASU 2011-12, "Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05". The amendments in ASU 2011-12 effectively defer only those changes in ASU 2011-05 that relate to the presentation of reclassification adjustments out of accumulated other comprehensive income. The amendments will be temporary to allow the Board time to redeliberate the presentation requirements for reclassifications out of accumulated other comprehensive income for annual and interim financial statements for public, private, and non-profit entities. All other requirements in ASU 2011-05 are not affected by ASU 2011-12, including the requirement to report comprehensive income either in a single continuous financial statement or in two separate but consecutive financial statements. The provisions of ASU No. 2011-12 are effective for the Bank's fiscal years ending after December 15, 2012, and did not have a significant impact on the Bank's financial statements.

Colonial American Bank

Notes to Financial Statements
December 31, 2012 and 2011

In June 2011, the FASB issued ASU 2011-05, "Presentation of Comprehensive Income" which amends ASC Topic 220 "Comprehensive Income". To increase the prominence of items reported in other comprehensive income and to facilitate convergence of U.S. GAAP and IFRS, the FASB decided to eliminate the option to present components of other comprehensive income as part of the statement of changes in stockholders' equity, among other amendments in ASU 2011-05. The amendments require that all non-owner changes in stockholders' equity be presented either in a single continuous statement of comprehensive income or in two separate but consecutive statements. In the two-statement approach, the first statement should present total net income and its components followed consecutively by a second statement that should present total other comprehensive income, the components of other comprehensive income, and the total of comprehensive income. The provisions of ASU No. 2011-05 are effective for the Bank's fiscal years ending after December 15, 2012, with retrospective application required. The adoption of ASU No. 2011-05 has resulted in presentation changes to the Bank's statements of operations. The adoption of ASU No. 2011-05 did not have a significant impact on the Bank's financial statements.

Subsequent Events

The Bank has evaluated subsequent events for potential recognition and/or disclosure through March 21, 2013, the date the financial statements were available to be issued, and has determined that no recognized or non-recognized subsequent events warranted inclusion or disclosure in these financial statements.

3. Consent Order with the Federal Deposit Insurance Corporation

On August 11, 2010 the Bank entered into a Consent Order with the Federal Deposit Insurance Corporation. Under the terms of the Consent Order the Bank agreed to take certain actions relating to management, capital levels, policies, and planning. The Bank complied with all of the requirements of the Consent Order, and on June 29, 2012, the Consent Order was terminated by the FDIC.

4. Cash and Due from Banks

The Bank maintains various deposit accounts with other banks to meet normal funds transaction requirements, to satisfy minimum deposit requirements, and to compensate other banks for certain correspondent services. The Federal Deposit Insurance Corporation insures these accounts up to \$250,000 per account. Management is responsible for assessing the credit risk of its correspondent banks. The withdrawal or usage restrictions of these balances did not have a significant impact on the operations of the Bank as of December 31, 2012 and 2011.

Colonial American Bank

Notes to Financial Statements
December 31, 2012 and 2011

5. Securities Available-for-Sale

The amortized cost and estimated fair value of securities at December 31, 2012 and 2011 is summarized below (in thousands). All of the Bank's securities are classified as available-for-sale.

	2012			Estimated Fair Value
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	
Mortgage-backed securities:				
U.S. government agencies	\$ 12,117	151	-	\$ 12,268
Other securities:				
Collateralized loan obligations	37,955	383	(118)	38,220
Corporate bonds	1,624	71	-	1,695
Equity - Small business investment company (SBIC)	500	-	-	500
Total securities available-for-sale	<u>\$ 52,196</u>	<u>605</u>	<u>(118)</u>	<u>52,683</u>

	2011			Estimated Fair Value
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	
Mortgage-backed securities:				
U.S. government agencies	\$ 5,124	145	(2)	\$ 5,267
Total securities available-for-sale	<u>\$ 5,124</u>	<u>145</u>	<u>(2)</u>	<u>\$ 5,267</u>

The following is a summary of the expected maturity distribution of debt securities available-for-sale, other than mortgage-backed securities, at December 31, 2012 (in thousands):

Available-for-sale	Amortized Cost	Estimated Fair Value
Due after one year through five years	\$ 1,624	\$ 1,695
Due after five years through ten years	33,337	33,628
Due after ten years	4,618	4,592
	<u>\$ 39,579</u>	<u>\$ 39,915</u>

Expected maturities on mortgage-backed securities will differ from contractual maturities as borrowers may have the right to call or prepay obligations with or without penalties.

No securities were pledged to secure borrowings at December 31, 2012 and 2011.

Colonial American Bank

Notes to Financial Statements December 31, 2012 and 2011

For the year ended December 31, 2012, the Bank had gross proceeds of \$31.9 million on sales of securities available-for-sale with gross realized gains of approximately \$625,000. The Bank had gross realized losses of \$70,000 for the year ended December 31, 2012. There were no sale of securities available-for-sale during the year ended December 31, 2011. The Bank routinely sells securities when market pricing presents, in management's assessment, an economic benefit that outweighs holding such security, and when smaller balance securities become cost prohibitive to carry. The Bank did not recognize any other-than-temporary impairment charges during the years ended December 31, 2012 or 2011.

Gross unrealized losses on available-for-sale securities, and the estimated fair value of the related securities, aggregated by security category and length of time that individual securities have been in a continuous unrealized loss position, at December 31, 2012 and 2011, were as follows (in thousands):

	December 31, 2012					
	Less than 12 months		12 months or more		Total	
	Unrealized Losses	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses	Estimated Fair Value
Collateralized loan obligations	\$ 118	\$ 17,087	\$ -	\$ -	\$ 118	\$ 17,087
Total	\$ 118	\$ 17,087	\$ -	\$ -	\$ 118	\$ 17,087

	December 31, 2011					
	Less than 12 months		12 months or more		Total	
	Unrealized Losses	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses	Estimated Fair Value
Mortgage-backed securities: U.S. government agencies	\$ 2	\$ 1,116	\$ -	\$ -	\$ 2	\$ 1,116
Total	\$ 2	\$ 1,116	\$ -	\$ -	\$ 2	\$ 1,116

At December 31, 2012, the Bank held ten collateralized loan obligations that were in a gross unrealized loss position of \$118,000. All of these securities were purchased during 2012, and, as a result, were in a loss position for a period of less than twelve months. Each of these securities is rated investment grade, and the Bank continues to receive principal and interest payments in accordance with the contractual terms of each of these securities. The estimated fair value of collateralized loan obligations are obtained from a nationally recognized third-party pricing service utilizing matrix pricing (Level 2), which is a mathematical technique used 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, and the utilization of other observable inputs such as trades, bid price spread, discount rates and loan level information. Management believes that the unrealized losses on these investments relate to the general interest rate environment, and are not related to credit, and as such, are considered to be temporary. As the Bank does not intend to sell these securities, and it is not more likely than not that the Bank would be required to sell these securities before recovery of its amortized cost basis, which may be at maturity, the Bank does not consider these investments to be other-than-temporarily impaired at December 31, 2012.

Colonial American Bank

Notes to Financial Statements
December 31, 2012 and 2011

6. Loans

Loans receivable, net of allowance for loan losses, consist of the following at December 31, 2012 and 2011 (in thousands):

	December 31,	
	2012	2011
Residential mortgages	\$ 38,217	\$ 12,361
Commercial real estate	19,081	13,967
Home equity and lines of credit	3,114	3,044
Construction	2,571	-
Multifamily	1,949	-
Commercial and industrial	6,052	3,124
Consumer	470	23
	<u>71,454</u>	<u>32,519</u>
Deferred loan fees, net	(10)	(11)
Total loans held-for-investment, net	<u>71,444</u>	<u>32,508</u>
Allowance for loan losses	<u>1,226</u>	<u>466</u>
Net loans held-for-investment	<u>\$ 70,218</u>	<u>\$ 32,042</u>

The Bank had \$4.0 million and \$0 in loans held-for-sale at December 31, 2012 and 2011, respectively. Loans held-for-sale included no non-accrual loans at December 31, 2012 and 2011.

The Bank provides for loan losses based on the consistent application of our documented allowance for loan loss methodology. Loan losses are charged to the allowance for loans losses and recoveries are credited to it. Additions to the allowance for loan losses are provided by charges against income based on various factors which, in our judgment, deserve current recognition in estimating probable losses. Loan losses are charged-off in the period the loans, or portion thereof, are deemed uncollectible. Generally, the Bank will record a loan charge-off (including a partial charge-off) to reduce a loan to the estimated fair value of the underlying collateral, less cost to sell, for collateral dependent loans. Management regularly reviews the loan portfolio and makes adjustments for loan losses in order to maintain the allowance for loan losses in accordance with U.S. generally accepted accounting principles ("GAAP"). The allowance for loan losses consists primarily of the following two components:

- (1) Specific allowances are established for impaired loans, generally defined by the Bank to be all nonaccrual loans, loans risk rated 8 (Doubtful) or 9 (Loss), and all loans subject to a troubled debt restructuring. The amount of impairment provided for as an allowance is represented by the deficiency, if any, between the present value of expected future cash flows discounted at the original loan's effective interest rate or the underlying collateral value (less estimated costs to sell,) if the loan is collateral dependent, and the carrying value of the loan. Impaired loans that have no impairment losses are not considered for general valuation allowances described below.

Colonial American Bank

Notes to Financial Statements
December 31, 2012 and 2011

(2) General allowances are established for loan losses on a portfolio basis for loans that do not meet the definition of impaired. The portfolio is grouped into similar risk characteristics, primarily loan segment and internal credit risk ratings. We apply an estimated loss rate to each loan group. The loss rates applied are based on our cumulative prior two year loss experience adjusted, as appropriate, for the environmental factors discussed below. This evaluation is inherently subjective, as it requires material estimates that may be susceptible to significant revisions based upon changes in economic and real estate market conditions. Actual loan losses may be significantly more than the allowance for loan losses we have established, which could have a material negative effect on our financial results. Within general allowances is an unallocated reserve established to recognize losses related to the inherent subjective nature of the appraisal process and the internal credit risk rating process.

In underwriting a loan secured by real property, the Bank requires an appraisal (or an automated valuation model) of the property by an independent licensed appraiser approved by the Bank's board of directors. The appraisal is subject to review by an independent third party hired by the Bank. Management reviews and inspects properties before disbursement of funds during the term of a construction loan. Generally, management obtains updated appraisals when a loan is deemed impaired. These appraisals may be more limited than those prepared for the underwriting of a new loan. In addition, when the Bank acquires other real estate owned, it generally obtains a current appraisal to substantiate the net carrying value of the asset at the time of foreclosure.

The adjustments to the Bank's loss experience is based on management's evaluation of several environmental factors, including:

- changes in local, regional, national, and international economic and business conditions and developments that affect the collectability of our portfolio, including the condition of various market segments;
- changes in the nature and volume of the Bank's portfolio and in the terms of the Bank's loans;
- changes in the experience, ability, and depth of lending management and other relevant staff;
- changes in the volume and severity of past due loans, the volume of nonaccrual loans, and the volume and severity of adversely classified or graded loans;
- changes in the quality of the Bank's loan review system;
- changes in the value of underlying collateral for collateral-dependent loans;
- the existence and effect of any concentrations of credit, and changes in the level of such concentrations; and
- the effect of other external factors such as competition and legal and regulatory requirements on the level of estimated credit losses in the Bank's existing portfolio.

Colonial American Bank

Notes to Financial Statements
December 31, 2012 and 2011

In evaluating the estimated loss factors to be utilized for each loan segment, management also reviews actual loss history over an extended period of time as reported by the FDIC for institutions in the Bank's market area for periods that are believed to have experienced similar economic conditions.

Management evaluates the allowance for loan losses based on the combined total of the specific and general components. Generally when the loan portfolio increases, absent other factors, the Bank's allowance for loan loss methodology results in a higher dollar amount of estimated probable losses. Conversely, when the loan portfolio decreases, absent other factors, the Bank's allowance for loan loss methodology results in a lower dollar amount of estimated probable losses.

Each quarter management evaluates the allowance for loan losses and adjusts the allowance as appropriate through a provision for loan losses. While management uses the best information available to make evaluations, future adjustments to the allowance may be necessary if conditions differ substantially from the information used in making the evaluations. In addition, as an integral part of their examination process, the Bank's regulators will periodically review the allowance for loan losses. The regulators may require the Bank to adjust the allowance based on their analysis of information available to them at the time of their examination. Based on management's comprehensive analysis of the loan portfolio, management believes the current level of the allowance for loan losses is adequate.

A summary of changes in the allowance for loan losses for the years ended December 31, 2012 and 2011 follows (in thousands):

	December 31,	
	2012	2011
Balance at beginning of year	\$ 466	\$ 225
Provision for loan losses	905	741
Charge-offs	(145)	(502)
Recoveries	-	2
Balance at end of year	<u>\$ 1,226</u>	<u>\$ 466</u>

On October 29, 2012, Hurricane Sandy caused destruction along the East Coast, including New Jersey, and resulted in, among other things, severe property damage and the closure of many businesses and financial markets. The Bank assessed the impact of the storm on its loan customers in the affected areas and its borrowers' ability to repay their loans and any adverse impact on collateral values. The Bank requires flood insurance on all properties in a flood zone. The Bank has evaluated the impact of the storm relative to the adequacy of the allowance for loan losses. There were no loan charge-offs or specific losses identified. The ultimate amount of loan losses relating to the storm is uncertain and additional provisions for loan losses may be required.

Colonial American Bank

Notes to Financial Statements December 31, 2012 and 2011

The following tables set forth activity in the Bank's allowance for loan losses, by loan type, for the years ended December 31, 2012 and 2011. The following tables also detail the amount of loans held-for-investment, net of deferred loan fees and costs, that are evaluated individually, and collectively, for impairment, and the related portion of the allowance for loan losses that is allocated to each loan portfolio segment (in thousands).

	December 31, 2012								Total
	Residential Mortgages	Commercial Real Estate	Home Equity and Lines of Credit	Construction	Multifamily	Commercial and Industrial	Consumer	Unallocated	
Allowance for loan losses:									
Beginning balance	\$ 197	\$ 138	\$ 19	\$ -	\$ -	\$ 54	\$ 3	\$ 55	\$ 466
Provisions	220	526	47	32	17	74	3	(14)	905
Charge-offs	-	(111)	(34)	-	-	-	-	-	(145)
Recoveries	-	-	-	-	-	-	-	-	-
Ending Balance	<u>\$ 417</u>	<u>\$ 553</u>	<u>\$ 32</u>	<u>\$ 32</u>	<u>\$ 17</u>	<u>\$ 128</u>	<u>\$ 6</u>	<u>\$ 41</u>	<u>\$ 1,226</u>
Ending balance: individually evaluated for impairment	\$ -	\$ 249	\$ -	\$ -	\$ -	\$ 23	\$ -	\$ -	\$ 272
Ending balance: collectively evaluated for impairment	<u>\$ 417</u>	<u>\$ 304</u>	<u>\$ 32</u>	<u>\$ 32</u>	<u>\$ 17</u>	<u>\$ 105</u>	<u>\$ 6</u>	<u>\$ 41</u>	<u>\$ 954</u>
Loans held-for-investment, net									
Ending balance	\$ 38,213	\$ 19,066	\$ 3,127	\$ 2,568	\$ 1,945	\$ 6,055	\$ 470	\$ -	\$ 71,444
Ending balance: individually evaluated for impairment	\$ -	\$ 2,221	\$ 641	\$ -	\$ -	\$ 144	\$ -	\$ -	\$ 3,006
Ending balance: collectively evaluated for impairment	<u>\$ 38,213</u>	<u>\$ 16,845</u>	<u>\$ 2,486</u>	<u>\$ 2,568</u>	<u>\$ 1,945</u>	<u>\$ 5,911</u>	<u>\$ 470</u>	<u>\$ -</u>	<u>\$ 68,438</u>

	December 31, 2011								Total
	Residential Mortgages	Commercial Real Estate	Home Equity and Lines of Credit	Construction	Multifamily	Commercial and Industrial	Consumer	Unallocated	
Allowance for loan losses:									
Beginning balance	\$ 111	\$ 86	\$ 13	\$ 13	\$ -	\$ -	\$ 2	\$ -	\$ 225
Provisions	292	139	15	62	-	54	124	55	741
Charge-offs	(208)	(87)	(9)	(75)	-	-	(123)	-	(502)
Recoveries	2	-	-	-	-	-	-	-	2
Ending Balance	<u>\$ 197</u>	<u>\$ 138</u>	<u>\$ 19</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 54</u>	<u>\$ 3</u>	<u>\$ 55</u>	<u>\$ 466</u>
Ending balance: individually evaluated for impairment	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Ending balance: collectively evaluated for impairment	<u>\$ 197</u>	<u>\$ 138</u>	<u>\$ 19</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 54</u>	<u>\$ 3</u>	<u>\$ 55</u>	<u>\$ 466</u>
Loans receivable, net									
Ending balance	\$ 12,363	\$ 13,951	\$ 3,048	\$ -	\$ -	\$ 3,123	\$ 23	\$ -	\$ 32,508
Ending balance: individually evaluated for impairment	\$ -	\$ 1,641	\$ 64	\$ -	\$ -	\$ -	\$ 6	\$ -	\$ 1,711
Ending balance: collectively evaluated for impairment	<u>\$ 12,363</u>	<u>\$ 12,310</u>	<u>\$ 2,984</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 3,123</u>	<u>\$ 17</u>	<u>\$ -</u>	<u>\$ 30,797</u>

During the year ended December 31, 2012 the Bank recorded charge-offs totaling \$145,000. The Bank wrote down one home equity loan to \$0 by recording a \$34,000 charge-off. The Bank also recorded an \$111,000 charge-off on a commercial real estate loan that currently remains in the Bank's portfolio at December 31, 2012. During the year ended December 31, 2011, the Bank recorded charge-offs totaling \$502,000. The Bank recorded \$208,000 of charge-offs on two loan relationships that were subsequently sold or paid-off prior to December 31, 2011. In addition, the Bank wrote down one loan by \$75,000 prior to taking possession of the collateral. At December 31, 2012, this property is classified as other real estate owned. The remaining \$219,000 of charge-offs were recorded on three loans that currently remain in the Bank's portfolio at December 31, 2012.

The Bank continuously monitors the credit quality of its loan receivables. Credit quality is monitored by reviewing certain credit quality indicators. Management has determined that internally assigned credit risk ratings by loan segment are the key credit quality indicators that best help management monitor the credit quality of the Bank's loan receivables.

Colonial American Bank

Notes to Financial Statements
December 31, 2012 and 2011

The Bank has adopted a credit risk rating system as part of the risk assessment of its loan portfolio. The Bank's lending officers are required to assign a credit risk rating to each loan in their portfolio at origination. When the lender learns of important financial developments, the risk rating is reviewed accordingly, and adjusted if necessary. Monthly, management presents monitored assets to the loan committee and board of directors. In addition, the Bank engages a third party independent loan reviewer that performs semi-annual reviews of a sample of loans, validating the credit risk ratings assigned to such loans. The credit risk ratings play an important role in the establishment of the loan loss provision and to confirm the adequacy of the allowance for loan losses. After determining the general reserve loss factor for each portfolio segment (segregated by credit risk rating), the portfolio segment balance collectively evaluated for impairment (for each credit risk rating) is multiplied by the general reserve loss factor for the respective portfolio segment in order to determine the general reserve.

When assigning a risk rating to a loan, management utilizes the Bank's internal nine-point credit risk rating system.

1. Minimal
2. Modest
3. Average
4. Acceptable
5. Acceptable with care
6. Special mention
7. Substandard
8. Doubtful
9. Loss

Loans rated 1 — 5 are considered pass ratings. An asset is considered substandard if it is inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Substandard assets have well defined weaknesses based on objective evidence, and are characterized by the distinct possibility that the Bank will sustain some loss if the deficiencies are not corrected. Assets classified as doubtful have all of the weaknesses inherent in those classified substandard with the added characteristic that the weaknesses present make collection or liquidation in full highly questionable and improbable based on current circumstances. Assets classified as loss are those considered uncollectible and of such little value that their continuance as assets is not warranted. Assets which do not currently expose the Bank to sufficient risk to warrant classification in one of the aforementioned categories, but possess weaknesses, are required to be designated special mention.

The Bank also maintains an unallocated component related to the general loss allocation. Management does not target a specific unallocated percentage of the total general allocation, or total allowance for loan losses. The primary purpose of the unallocated component is to account for the inherent imprecision of the loss estimation process related primarily to periodic updating of appraisals on impaired loans, as well as periodic updating of commercial loan credit risk ratings by loan officers and the Bank's internal credit audit process.

Colonial American Bank

Notes to Financial Statements December 31, 2012 and 2011

The following tables detail the recorded investment of loans held-for-investment, net of deferred fees and costs, by loan type and credit quality indicator at December 31, 2012 and 2011 (in thousands).

	December 31, 2012							Total
	Residential Mortgages	Commercial Real Estate	Home Equity and Lines of Credit	Construction	Multifamily	Commercial and Industrial	Consumer	
Internal Risk Rating								
Pass	\$ 38,062	\$ 15,884	\$ 2,486	\$ 2,568	\$ 1,945	\$ 5,674	\$ 470	\$ 67,089
Special Mention	-	115	94	-	-	223	-	432
Substandard	151	3,067	547	-	-	158	-	3,923
Loans held-for-investment, net	<u>\$ 38,213</u>	<u>\$ 19,066</u>	<u>\$ 3,127</u>	<u>\$ 2,568</u>	<u>\$ 1,945</u>	<u>\$ 6,055</u>	<u>\$ 470</u>	<u>\$ 71,444</u>

	December 31, 2011							Total
	Residential Mortgages	Commercial Real Estate	Home Equity and Lines of Credit	Construction	Multifamily	Commercial and Industrial	Consumer	
Internal Risk Rating								
Pass	\$ 12,363	\$ 11,990	\$ 2,397	\$ -	\$ -	\$ 3,026	\$ 17	\$ 29,793
Special Mention	-	320	587	-	-	97	-	1,004
Substandard	-	1,641	64	-	-	-	6	1,711
Loans held-for-investment, net	<u>\$ 12,363</u>	<u>\$ 13,951</u>	<u>\$ 3,048</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 3,123</u>	<u>\$ 23</u>	<u>\$ 32,508</u>

Included in loans receivable are loans for which the accrual of interest income has been discontinued due to deterioration in the financial condition of the borrowers. The recorded investment of these nonaccrual loans was \$2.9 million and \$1.2 million at December 31, 2012 and 2011, respectively. Generally, loans are placed on non-accruing status when they become 90 days or more delinquent, and remain on non-accrual status until they are brought current, have six months of performance under the loan terms, and factors indicating reasonable doubt about the timely collection of payments no longer exist. Therefore, loans may be current in accordance with their loan terms, or may be less than 90 days delinquent and still be on a non-accruing status. These non-accrual amounts were all deemed to be impaired at December 31, 2012 and 2011, respectively. There were no loans past due ninety days or more and still accruing interest December 31, 2012 and 2011.

Colonial American Bank

Notes to Financial Statements December 31, 2012 and 2011

The following tables set forth the detail, and delinquency status, of non-performing loans (non-accrual loans and loans past due ninety days or more and still accruing), net of deferred fees and costs, at December 31, 2012 and 2011 (in thousands).

	December 31, 2012				
	Non-Accruing Loans			> 90 Days Past Due and Accruing	Total Non- Performing Loans
	0-29 Days Past Due	30-89 Days Past Due	≥ 90 Days Past Due		
Commercial mortgage					
Substandard	\$ 617	-	1,604	-	\$ 2,221
Total commercial mortgage	617	-	1,604	-	2,221
Home equity and lines of credit					
Substandard	4	53	490	-	547
Total home equity and lines of credit	4	53	490	-	547
Commercial and industrial					
Substandard	144	-	-	-	144
Total commercial and industrial	144	-	-	-	144
Total Non-Performing Loans	<u>\$ 765</u>	<u>53</u>	<u>2,094</u>	<u>-</u>	<u>\$ 2,912</u>

	December 31, 2011				
	Non-Accruing Loans			> 90 Days Past Due and Accruing	Total Non- Performing Loans
	0-29 Days Past Due	30-89 Days Past Due	≥ 90 Days Past Due		
Commercial mortgage					
Substandard	\$ -	\$ 1,082	\$ -	\$ -	\$ 1,082
Total home equity and lines of credit	-	1,082	-	-	1,082
Home equity and lines of credit					
Substandard	64	-	-	-	64
Total commercial mortgage	64	-	-	-	64
Consumer					
Substandard	6	-	-	-	6
Total consumer	6	-	-	-	6
Total Non-Performing Loans	<u>\$ 70</u>	<u>\$ 1,082</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 1,152</u>

Colonial American Bank

Notes to Financial Statements December 31, 2012 and 2011

The following tables set forth the detail and delinquency status of loans held-for-investment, net of deferred fees and costs, by performing and non-performing loans at December 31, 2012 and 2011 (in thousands).

	December 31, 2012				
	Performing (Accruing) Loans			Non-Performing Loans	Total Loans Receivable, net
	0-29 Days Past Due	30-89 Days Past Due	Total		
Residential mortgages					
Pass	\$ 37,942	\$ 120	\$ 38,062	\$ -	\$ 38,062
Special mention	-	-	-	-	-
Substandard	-	151	151	-	151
Total residential mortgages	37,942	271	38,213	-	38,213
Commercial real estate					
Pass	15,884	-	15,884	-	15,884
Special mention	115	-	115	-	115
Substandard	479	367	846	2,221	3,067
Total commercial real estate	16,478	367	16,845	2,221	19,066
Home equity and lines of credit					
Pass	2,414	72	2,486	-	2,486
Special mention	94	-	94	-	94
Substandard	-	-	-	547	547
Total home equity and lines of credit	2,508	72	2,580	547	3,127
Construction					
Pass	2,568	-	2,568	-	2,568
Special mention	-	-	-	-	-
Substandard	-	-	-	-	-
Total commercial and industrial	2,568	-	2,568	-	2,568
Multifamily					
Pass	1,945	-	1,945	-	1,945
Special mention	-	-	-	-	-
Substandard	-	-	-	-	-
Total commercial and industrial	1,945	-	1,945	-	1,945
Commercial and industrial					
Pass	5,674	-	5,674	-	5,674
Special mention	223	-	223	-	223
Substandard	14	-	14	144	158
Total commercial and industrial	5,911	-	5,911	144	6,055
Consumer					
Pass	470	-	470	-	470
Special mention	-	-	-	-	-
Substandard	-	-	-	-	-
Total consumer	470	-	470	-	470
Total	\$ 67,822	\$ 710	\$ 68,532	\$ 2,912	\$ 71,444

Colonial American Bank

Notes to Financial Statements December 31, 2012 and 2011

	December 31, 2011				
	Performing (Accruing) Loans			Non-Performing Loans	Total Loans Receivable, net
	0-29 Days Past Due	30-89 Days Past Due	Total		
Residential mortgages					
Pass	\$ 12,363	\$ -	\$ 12,363	\$ -	\$ 12,363
Special mention	-	-	-	-	-
Substandard	-	-	-	-	-
Total residential mortgages	12,363	-	12,363	-	12,363
Commercial real estate					
Pass	11,748	242	11,990	-	11,990
Special mention	98	222	320	-	320
Substandard	559	-	559	1,082	1,641
Total commercial real estate	12,405	464	12,869	1,082	13,951
Home equity and lines of credit					
Pass	2,397	-	2,397	-	2,397
Special mention	97	490	587	-	587
Substandard	-	-	-	64	64
Total home equity and lines of credit	2,494	490	2,984	64	3,048
Commercial and industrial					
Pass	3,026	-	3,026	-	3,026
Special mention	97	-	97	-	97
Substandard	-	-	-	-	-
Total commercial and industrial	3,123	-	3,123	-	3,123
Consumer					
Pass	17	-	17	-	17
Special mention	-	-	-	-	-
Substandard	-	-	-	6	6
Total consumer	17	-	17	6	23
Total	\$ 30,402	\$ 954	\$ 31,356	\$ 1,152	\$ 32,508

Colonial American Bank

Notes to Financial Statements December 31, 2012 and 2011

The following tables summarize impaired loans as of December 31, 2012 and 2011 (in thousands):

	December 31, 2012		
	Recorded Investment	Unpaid Principal Balance	Related Allowance
With No Allowance Recorded:			
Commercial mortgage			
Substandard	\$ 617	\$ 703	\$ -
Home equity and lines of credit			
Special mention	94	94	-
Substandard	547	590	-
Consumer			
Substandard	-	122	-
Total			
Commercial mortgage	617	703	-
Home equity and lines of credit	641	684	-
Consumer	-	122	-
	<u>\$ 1,258</u>	<u>\$ 1,509</u>	<u>\$ -</u>

With a Related Allowance Recorded:			
Commercial mortgage			
Substandard	\$ 1,604	\$ 1,716	\$ 249
Commercial and industrial			
Substandard	144	144	23
Total			
Commercial mortgage	1,604	1,716	249
Commercial and industrial	144	144	23
	<u>\$ 1,748</u>	<u>\$ 1,860</u>	<u>\$ 272</u>

	December 31, 2011		
	Recorded Investment	Unpaid Principal Balance	Related Allowance
With No Allowance Recorded:			
Commercial mortgage			
Substandard	\$ 1,641	\$ 1,728	\$ -
Home equity and lines of credit			
Substandard	64	73	-
Consumer			
Substandard	6	128	-
Total			
Commercial mortgage	1,641	1,728	-
Home equity and lines of credit	64	73	-
Consumer	6	128	-
	<u>\$ 1,711</u>	<u>\$ 1,929</u>	<u>\$ -</u>

Colonial American Bank

Notes to Financial Statements
December 31, 2012 and 2011

Included in the table above at December 31, 2012 are impaired loans with carrying balances of \$1.0 million that were not written down by either charge-offs or specific reserves in the Bank's allowance for loan losses. At December 31, 2011, impaired loans with carrying balances of \$1.5 million were not written down either by charge-offs or specific reserves in the Bank's allowance for loan losses. Loans not written down by charge-offs or specific reserves at December 31, 2012 and 2011, have sufficient collateral values, less costs to sell, supporting the carrying balances of the loans.

The average recorded balance of impaired loans for the years ended December 31, 2012 and 2011 was approximately \$2.0 million and \$1.0 million, respectively. The Bank recorded interest income of \$82,000 and \$32,000 on impaired loans during the years ended December 31, 2012 and 2011, respectively. The Bank would have recorded additional interest income of \$173,000 and \$60,000 on impaired loans during the years ended December 31, 2012 and 2011, respectively, were the loans not classified as non-accrual.

At December 31, 2012, the Bank had \$1.0 million of loans that were modified in a troubled debt restructuring, of which, \$912,000 were classified as non-accrual. At December 31, 2011, the Bank had one loan amounting to \$559,000 that was modified in a troubled debt restructuring, and was classified as accruing.

The following tables summarize loans that were modified in a troubled debt restructuring during the years ended December 31, 2012 and 2011 (in thousands).

	Number of Relationships	December 31, 2012	
		Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Troubled Debt Restructurings			
Commercial real estate			
Substandard	1	\$ 216	\$ 216
Home equity and lines of credit			
Special mention	1	96	96
Commercial and industrial			
Substandard	1	149	126
Total troubled debt restructurings	3	\$ 461	\$ 438

	Number of Relationships	December 31, 2011	
		Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Troubled Debt Restructurings			
Residential mortgage			
Substandard	1	\$ 574	\$ 450
Commercial real estate			
Substandard	1	559	559
Consumer			
Substandard	1	149	149
Total troubled debt restructurings	3	\$ 1,282	\$ 1,158

Colonial American Bank

Notes to Financial Statements
December 31, 2012 and 2011

The commercial real estate loan that was restructured during the year ended December 31, 2012, was restructured to receive a lower interest rate. The home equity and commercial and industrial loans that were restructured during the year ended December 31, 2012 were granted extended maturities. All three loans restructured during the year ended December 31, 2012 are performing in accordance with their restructured terms at December 31, 2012.

During the year ended December 31, 2011, the residential mortgage loan amounting to \$574,000 (pre-modification) was supported by a one- to four-family residential home and was restructured by extending the maturity. This loan was charged-down by \$124,000 as part of the restructuring. This loan subsequently defaulted after the restructuring. This loan was subsequently paid off during the year ended December 31, 2011 as a result of the sale of the underlying collateral. An additional charge-off of \$83,000 was recorded prior to the sale of the collateral. Also during the year ended December 31, 2011, a commercial real estate loan amounting to \$559,000 (pre-modification) was restructured to receive an extension of interest-only payments, when the loan was set to begin principal amortization as well as interest payments. This loan has subsequently defaulted during the year ended December 31, 2012.

The consumer loan amounting to \$149,000 (pre-modification) was an unsecured line of credit. The maturity date of this loan was extended for two years during the year ended December 31, 2011. Subsequent to restructuring, the Bank received a \$20,000 pay-down on the loan. Also subsequent to the restructuring, the Bank recorded a charge-off of \$123,000 during the year ended December 31, 2011 as discussions with the borrower indicated that the outstanding principal balance of the loan would not be fully collectible upon maturity of the loan. This charge-off was recorded based on a change in circumstances regarding this credit, not as a result of a subsequent default after restructuring. The outstanding principal balance of this loan is \$0 at December 31, 2012.

Management 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 fair value of the collateral (less costs 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 values 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. Determining the estimated fair value of underlying collateral (and related costs to sell) can be difficult in illiquid real estate markets and is subject to significant assumptions and estimates. Management employs an independent third party expert in appraisal preparation and review to ascertain the reasonableness of updated appraisals. Projecting the expected cash flows under troubled debt restructurings is inherently subjective and requires, among other things, an evaluation of the borrower's current and projected financial condition. Actual results may be significantly different than our projections and our established allowance for loan losses on these loans, which could have a material effect on our financial results.

Colonial American Bank

Notes to Financial Statements
December 31, 2012 and 2011

7. Premises and Equipment, Net

A summary of the cost and accumulated depreciation of bank premises and equipment as of December 31, 2012 and 2011 is as follows:

	December 31,	
	2012	2011
	(amounts in thousands)	
Leasehold improvements	\$ 1,456	\$ 285
Furniture and equipment	1,281	584
Construction-in-process	576	479
	3,313	1,348
Less: accumulated depreciation and amortization	(1,016)	(785)
Premises and equipment, net	<u>\$ 2,297</u>	<u>\$ 563</u>

Depreciation expense for the years ended December 31, 2012 and 2011 was \$231,000 and \$117,000, respectively.

8. Deposits

Deposits at December 31, 2012 and 2011 consisted of the following:

	December 31,	
	2012	2011
	(in thousands)	
Non-interest bearing demand	\$ 5,015	\$ 1,265
Interest-bearing demand	2,144	1,202
Money market	31,179	9,092
Savings	2,903	7,001
Time (under \$100,000)	20,842	5,796
Time (\$100,000 or more)	43,464	5,006
	<u>\$ 105,547</u>	<u>\$ 29,362</u>

Colonial American Bank

Notes to Financial Statements
December 31, 2012 and 2011

Scheduled maturities of time deposits at December 31, 2012 are summarized as follows:

	December 31, 2012	
	(in thousands)	
2013	\$	56,923
2014		3,856
2015		1,748
2016		30
2017		1,749
	\$	<u>64,306</u>

Interest expense on deposits for the years ended December 31, 2012 and 2011 is summarized as follows:

	Years Ended December 31,	
	2012	2011
	(in thousands)	
Interest-bearing demand	\$ 3	\$ 5
Money market	216	30
Savings	21	55
Time	701	230
	<u>\$ 941</u>	<u>\$ 320</u>

9. Borrowings

Borrowings consisted of FHLB advances, and are summarized as follows (in thousands):

	December 31,	
	2012	2011
FHLB advances	\$ 14,000	\$ -
	<u>\$ 14,000</u>	<u>\$ -</u>

FHLB advances are secured by a blanket lien on unencumbered securities and residential mortgage loans, and the Bank's FHLB capital stock.

All of the Bank's FHLB advances outstanding at December 31, 2012 have contractual maturities during 2013, and have a weighted average rate of 0.19%.

The Bank maintains a \$2.5 million line of credit with Atlantic Central Bankers Bank. The Bank also has additional borrowing capacity of \$21.1 million with the Federal Home Loan Bank of Pittsburgh at December 31, 2012.

Interest expense on borrowings amounted to \$5,000 and \$0 for the years ended December 31, 2012 and 2011, respectively.

Colonial American Bank

Notes to Financial Statements
December 31, 2012 and 2011

10. Income Taxes

The Bank, during its pre-opening period and subsequent to commencement of banking operations, has incurred cumulative net losses which has caused there to be no provision for income taxes, net deferred taxes and income taxes payable as of and for the years ended December 31, 2012 and 2011 because of related valuation allowances.

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities at December 31, 2012 and 2011, are as follows (in thousands):

	December 31,	
	2012	2011
Deferred tax assets:		
Allowance for loan losses	\$ 279	\$ 133
Organizational and Start-up Costs	256	284
Premises and equipment	144	89
Stock Compensation expense	286	253
Other	116	58
Net operating loss carryforwards	1,716	934
	<u>2,797</u>	<u>1,751</u>
Valuation allowance	<u>(2,615)</u>	<u>(1,689)</u>
Total Deferred Tax Assets, Net of Valuation Allowance	182	62
Deferred tax liabilities:		
Unrealized Gains on AFS securities	(165)	(49)
Deferred Loan Costs	(17)	(13)
	<u>(182)</u>	<u>(62)</u>
Net Deferred Tax Asset	<u>\$ -</u>	<u>\$ -</u>

At December 31, 2012, the Bank has federal net operating losses available to offset future income in the amount of approximately \$4.9 million. Net operating losses generated prior to the recapitalization that occurred on April 15, 2011 are currently subject to limitation under Code Section 382. The annual limitation is approximately \$21,000 per year. These federal net operating losses will expire between 2027 and 2032. The Bank also has New Jersey net operating losses available to offset future New Jersey state income in the amount of approximately \$1.0 million that will expire in 2032.

11. Fair Value Measurement

The following table presents the assets reported on the balance sheet at their estimated fair value as of December 31, 2012 and 2011, by level within the Fair Value Measurements and Disclosures Topic of the FASB Accounting Standards Codification – ASC 820. Financial assets and liabilities are classified in their entirety based on the level of input that is significant to the fair value measurement. The fair value hierarchy is as follows:

- Level 1 Inputs – Unadjusted quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date.
- Level 2 Inputs – Inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. These include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability (for example, interest rates, volatilities, prepayment speeds, loss severities, credit risks and default rates) or inputs that are derived principally from or corroborated by observable market data by correlations or other means.
- Level 3 Inputs – Significant unobservable inputs that reflect the Bank’s own assumptions about assumptions that market participants would use in pricing the assets or liabilities.

Colonial American Bank

Notes to Financial Statements

December 31, 2012 and 2011

The following table summarizes financial assets and liabilities measured at fair value on a recurring and non-recurring basis as of December 31, 2012 and 2011, segregated by the level of the valuation inputs within the fair value hierarchy utilized to measure fair value.

	December 31, 2012	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	(in thousands)			
Measured on a recurring basis:				
Assets:				
Available-for-sale investment securities:				
Mortgage-backed securities				
U.S. government agencies	\$ 12,268	\$ -	\$ 12,268	\$ -
Collateralized loan obligations	38,220	-	38,220	-
Corporate bonds	1,695	-	1,695	-
Equity - SBIC	500	-	-	500
Total	\$ 52,683	\$ -	\$ 52,183	\$ 500
Measured on a non-recurring basis:				
Assets:				
Impaired Loans				
Home equity	4	-	-	4
Commercial real estate (CRE)	1,568	-	-	1,568
Commercial and industrial	121	-	-	121
Total impaired loans	1,693	-	-	1,693
Foreclosed assets (Construction)	189	-	-	189
Total	\$ 1,882	\$ -	\$ -	\$ 1,882
	December 31, 2011	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	(in thousands)			
Measured on a recurring basis:				
Assets:				
Available-for-sale investment securities				
Mortgage-backed securities				
U.S. government agencies	\$ 5,267	-	\$ 5,267	-
Total	\$ 5,267	\$ -	\$ 5,267	\$ -
Measured on a non-recurring basis:				
Assets:				
Impaired Loans				
Home equity	\$ 8	\$ -	\$ -	\$ 8
Commercial real estate (CRE)	227	-	-	227
Consumer	6	-	-	6
Total impaired loans	241	-	-	241
Foreclosed assets (Construction)	189	-	-	189
Total	\$ 430	\$ -	\$ -	\$ 430

Colonial American Bank

Notes to Financial Statements
December 31, 2012 and 2011

Assets Measured on a Recurring Basis

Securities Available-for-Sale: The estimated fair value for mortgage-backed securities and corporate bonds are obtained from a nationally recognized third-party pricing service. The estimated fair values are derived primarily from cash flow models, which include assumptions for interest rates, credit losses, and prepayment speeds. The significant inputs utilized in the cash flow models are based on market data obtained from sources independent of the Bank (observable inputs,) and are therefore classified as Level 2 within the fair value hierarchy.

The estimated fair value for collateralized loan obligations are obtained from a nationally recognized third-party pricing service utilizing matrix pricing (Level 2), which is a mathematical technique used 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, and the utilization of other observable inputs such as trades, bid price spread, discount rates and loan level information.

Investments in Equity-SBIC securities are generally illiquid and are initially valued at cost. These investments are adjusted to fair value to reflect the occurrence of significant developments, i.e. capital transactions or business, economic or market events, or deterioration in the underlying assets. Adjustment to fair value are reported in net gain (loss) from investments on the statement of operations.

The table below presents all assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the year ended December 31, 2012 (in thousands).

	Available-for-Sale Equity-SBIC
Balance, January 1, 2012	\$ -
Purchases	500
Balance, December 31, 2012	<u>\$ 500</u>

There were no transfers of securities between Levels during the years ended December 31, 2012 or 2011. The investment was purchased on December 21, 2012. No fair value adjustments were required as of December 31, 2012.

Assets Measured on a Non-Recurring Basis

The following table presents qualitative information for Level 3 assets measured at fair value on a non-recurring basis at December 31, 2012 (in thousands).

	Fair Value	Valuation Methodology	Unobservable Inputs	Range of Inputs
Impaired loans	\$ 1,693	Appraisals	Discount for costs to sell	10%
Foreclosed assets	\$ 189	Appraisals	Discount for costs to sell	10%

Colonial American Bank

Notes to Financial Statements
December 31, 2012 and 2011

Impaired Loans: At December 31, 2012 and 2011, the Bank had impaired loans with outstanding principal balances of \$2.0 million and \$241,000, respectively, that were recorded at their estimated fair value of \$1.7 million and \$241,000, respectively. The Bank recorded charge-offs of \$145,000 and \$218,000, for the years ended December 31, 2012 and 2011, respectively, and impairment charges of \$272,000 and \$0 for the years ended December 31, 2012 and 2011, utilizing Level 3 inputs. For purposes of estimating fair value of impaired loans, management utilizes independent appraisals, if the loan is collateral dependent, adjusted downward by management, as necessary, for changes in relevant valuation factors subsequent to the appraisal date and 10% for costs to sell, or the present value of expected future cash flows for non-collateral dependent loans and troubled debt restructurings.

Foreclosed Assets: At December 31, 2012 and 2011, the Bank had assets acquired through foreclosure of \$189,000, recorded at estimated fair value, less estimated selling costs when acquired, thus establishing a new cost basis. Fair value is generally based on independent appraisals. These appraisals include adjustments to comparable assets based on the appraisers' market knowledge and experience, and are considered level 3 inputs. When an asset is acquired, the excess of the loan balance over fair value, less estimated selling costs (assumed to be 10%), is charged to the allowance for loan losses. If the estimated fair value of the asset declines, a write down is recorded through expense. The valuation of foreclosed assets is subjective in nature and may be adjusted in the future because of changes in the economic conditions.

During 2011, the Bank transferred a loan with a principal balance of \$265,000 and an estimated fair value, less costs to sell, of \$189,000 to foreclosed assets. During the year ended December 31, 2011, the Bank recorded impairment charges of \$76,000 prior to the transfer of the loan to foreclosed assets utilizing Level 3 inputs. During 2011 the Bank made subsequent valuation adjustments to foreclosed assets totaling \$21,000, reflecting continued deterioration in estimated fair values. The remaining reduction to REO was a result of sales.

Fair Value of Financial Instruments

The FASB Accounting Standards Topic for Financial Instruments requires disclosure of the fair value of financial assets and financial liabilities, including those financial assets and financial liabilities that are not measured and reported at fair value on a recurring or non-recurring basis. The methodologies for estimating the fair value of financial assets and financial liabilities that are measured at fair value on a recurring or non-recurring basis are discussed above. The following methods and assumptions were used to estimate the fair value of other financial assets and financial liabilities not already discussed above:

a) Cash and Cash Equivalents

Cash and cash equivalents are short-term in nature with original maturities of three months or less; the carrying amount approximates fair value. Certificates of deposits having original terms of six-months or less; carrying value generally approximates fair value. Certificates of deposits with an original maturity of six months or greater; the fair value is derived from discounted cash flows.

b) Loans (Held-for-Sale)

Held-for-sale loans are carried at the lower of aggregate cost or estimated fair value, less costs to sell, and therefore fair value is equal to carrying value.

c) Loans (Held-for-Investment)

Fair values are estimated for portfolios of loans with similar financial characteristics. Loans are segregated by type such as residential mortgage, construction, land, multifamily, commercial and consumer. Each loan category is further segmented into amortizing and non-amortizing and fixed and adjustable rate interest terms and by performing and nonperforming categories. The fair value of loans is estimated by discounting the future cash flows using current prepayment assumptions and current rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities. This method of estimating fair value does not incorporate the exit price concept of fair value prescribed by the FASB ASC Topic 820 for Fair Value Measurements and Disclosures.

d) Federal Home Loan Bank of Pittsburgh Stock

The fair value for Federal Home Loan Bank of Pittsburgh stock is its carrying value, since this is the amount for which it could be redeemed and there is no active market for this stock.

e) Deposits

The fair value of deposits with no stated maturity, such as non-interest-bearing demand deposits, savings, NOW and money market accounts, is equal to the amount payable on demand. The fair value of certificates of deposit is based on the discounted value of contractual cash flows. The discount rate is estimated using the rates currently offered for deposits of similar remaining maturities.

f) Borrowings

The fair value of borrowings is estimated by discounting future cash flows based on rates currently available for debt with similar terms and remaining maturity.

g) Commitments to Extend Credit and Letters of Credit

The fair value of commitments to extend credit are estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present creditworthiness of the counterparties. For fixed-rate loan commitments, fair value also considers the difference between current levels of interest rates and the committed rates.

The fair value of off-balance-sheet commitments is insignificant and therefore not included in the following table.

Colonial American Bank

Notes to Financial Statements
December 31, 2012 and 2011

The estimated fair values of the Company's significant financial instruments at December 31, 2012, are presented in the following table (in thousands):

	December 31,	
	2012	
	Carrying Value	Estimated Fair Value
Financial assets:		
Cash and cash equivalents	\$ 5,295	5,295
Securities available-for-sale	52,683	52,683
Net loans held-for-sale	4,015	4,015
Net loans held-for-investment	70,218	69,157
Federal Home Loan Bank of Pittsburgh stock, at cost	726	726
Financial liabilities:		
Deposits	\$ 105,547	\$ 105,832
Borrowings	14,000	14,000

Limitations

Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial instrument. These estimates do not reflect any premium or discount that could result from offering for sale at one time the Bank's entire holdings of a particular financial instrument. Because no market exists for a significant portion of the Bank's financial instruments, fair value estimates are based on judgments regarding future expected loss experience, current economic conditions, risk characteristics of various financial instruments, and other factors. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and, therefore, cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

Fair value estimates are based on existing on- and off-balance-sheet financial instruments without attempting to estimate the value of anticipated future business and the value of assets and liabilities that are not considered financial instruments. In addition, the tax ramifications related to the realization of the unrealized gains and losses can have a significant effect on fair value estimates and have not been considered in the estimates.

Colonial American Bank

Notes to Financial Statements
December 31, 2012 and 2011

12. Employee Benefit Plans

The Bank has a 401(k) Plan whereby, during 2012, eligible employees may contribute up to 90% of their compensation subject to certain limits based on federal tax laws. The Bank makes matching contributions equal to 100% of the first 3% of an employee's compensation contributed to the Plan and 50% for contributions greater than 3% but not more than 5.0% of an employee's compensation contributed to the Plan. During 2011, eligible employees were able to contribute up to 15% of their compensation subject to certain limits based on federal tax laws. The Bank made matching contributions equal to 50% of the first 7% of an employee's compensation contributed to the Plan. Matching contributions vest to the employee equally over a five-year period. The Bank's contribution to this plan amounted to \$48,000 and \$7,000 for the years ended December 31, 2012 and 2011, respectively.

13. Shareholders' Equity

Stock Warrants

In connection with the Bank's initial capital offering, each shareholder was also granted one stock purchase warrant for every five shares of common stock purchased. Each warrant was issued at a price of \$187.50 and expired on March 23, 2012. As such, there were zero and 10,159 warrants outstanding and exercisable at December 31, 2012 and 2011, respectively.

In connection with the recapitalization of the Bank that closed on April 15, 2011, a total of 460,403 warrants were granted to new shareholders. Each warrant was issued at a price of \$10.00 and expires April 14, 2021. There were 460,403 warrants outstanding and exercisable at December 31, 2012 and 2011.

Employee and Director Stock Compensation Plan

The Bank's original Board of Directors had approved the 2008 Colonial American Stock Compensation Plan that will have a term of 10 years. Pursuant to the Plan, 15% of the common stock shares that were issued in the initial offering, or 7,511, were reserved for future issuance. To grant incentive stock options under the Plan, the shareholders must approve the Plan. On December 30, 2008 the shareholders approved the Plan. As of December 31, 2011 and 2010, there were no awards under the Plan.

Subsequent to the recapitalization that closed on April 15, 2011, the Bank's newly appointed Board of Directors approved the Colonial American Bank 2011 Stock Award and Incentive Plan. The Plan provides for the issuance or delivery of up to 900,000 shares of Colonial American Bank common stock. On August 17, 2011, certain officers and employees of the Bank were granted an aggregate of 155,000 stock options, and non-employee directors received an aggregate of 55,000 stock options. On September 12, 2011 an employee was granted 5,000 stock options. On January 1, 2012 non-employee directors were granted 50,000 stock options, and on February 1, 2012, an employee was granted 5,000 stock options. On September 1, 2012, certain officers and employees of the Bank were granted 19,500 stock options. All employee and director options granted to date vest in equal installments over a three year period beginning one year from the date of grant. Three executive officers received stock options that vest in equal installments over a three year period beginning on the date of grant. The vesting of options may accelerate in accordance with the term of the Plan. Stock options were granted with an exercise price equal to \$10.00 per share, and have an expiration period of ten years.

Colonial American Bank

Notes to Financial Statements
December 31, 2012 and 2011

The fair value of the stock options granted on August 17, 2011 and September 12, 2011 was estimated utilizing the Black-Scholes option pricing model using the following assumptions: an expected life of 5.75 years for those options granted to executive officers and 6 years for all other options granted utilizing the simplified method, risk-free rate of return of 1.125%, volatility of 30.06%, and a dividend yield of 0.0%. The fair value of stock options granted on January 1, 2012 and February 1, 2012 was estimated utilizing the Black-Scholes option pricing model using the following assumptions: an expected life of 6 years utilizing the simplified method, risk-free rate of return of 1.11%, volatility of 30.06%, and a dividend yield of 0.0%. The fair value of stock options granted on September 30, 2012 was estimated utilizing the Black-Scholes option pricing model using the following assumptions: an expected life of 6 years utilizing the simplified method, risk-free rate of return of 0.925%, volatility of 30.33%, and a dividend yield of 0.0%. The Bank is expensing the grant date fair value of all employee and director share-based compensation over the requisite service periods on a straight-line basis.

During the years ended December 31, 2012 and 2011, the Bank recorded \$231,000 and \$130,000, respectively, of stock-based compensation.

The following table is a summary of the Bank's non-vested stock options as of December 31, 2012, and changes therein during the year then ended:

	Number of Stock Options	Weighted Average Grant Date Fair Value	Weighted Average Exercise Price	Weighted Average Contractual Life (Years)
Outstanding - December 31, 2010	-	\$ -	\$ -	-
Granted	215,000	2.82	10.00	10.00
Outstanding - December 31, 2011	215,000	2.82	10.00	9.63
Granted	74,500	2.63	10.00	10.00
Forfeited	(15,000)	2.94	10.00	10.00
Outstanding - December 31, 2012	274,500	\$ 2.76	\$ 10.00	8.77
Exercisable - December 31, 2012	83,333	\$ 2.81	\$ 10.00	8.63

Expected future stock option expense related to the non-vested options outstanding as of December 31, 2012 is \$405,000 over an average period of 1.6 years.

Preferred Stock

On October 3, 2008 Congress passed the Emergency Economic Stabilization Act of 2008 ("EESA"), which provided the U.S. Secretary of the Treasury with broad authority to implement certain actions to help restore stability and liquidity to the U.S. markets. One of the provisions resulting from the Act was the Treasury Capital Purchase Program ("CPP") which provided direct equity investment of preferred stock by the U.S. Treasury in qualified financial institutions. This program was voluntary and required an institution to comply with several restrictions and provisions, including limits on executive compensation, stock redemptions, and declaration of dividends. The CPP provided for a minimum investment of 1 percent of Risk-Weighted-Assets, with a maximum investment of the lesser of 3 percent of Risk-Weighted Assets or \$25 Billion. On March 27, 2009, the Bank received an investment in preferred stock of \$574,000. The non-cumulative perpetual preferred stock, Series A has a dividend rate of 5 percent per year until the fifth anniversary of the Treasury investment and a dividend of 9 percent, thereafter.

Colonial American Bank

Notes to Financial Statements
December 31, 2012 and 2011

The CPP also requires the Treasury to receive warrants for the purchase of fixed rate non-cumulative perpetual preferred stock, Series B with liquidation value equal to 5 percent of the capital invested by the Treasury. On March 27, 2009, the warrants issued to Treasury for the non-cumulative perpetual preferred stock, Series B were exercised. The exercise price of the warrants was \$1.00. The Series B preferred stock has a dividend rate of 9 percent per year.

The proceeds for the preferred stock were allocated between the Series A and Series B preferred stock based on their relative fair value, using a discount rate of 12%. The original net discount was being accreted over the expected term of five years using the effective interest method. In accordance with state law, because the Bank is in an accumulated deficit position, the preferred stock dividends were declared from additional paid-in capital.

On October 24, 2011, after obtaining the appropriate approvals from the its banking regulators, the Bank redeemed all of the 603 shares of Series A and Series B preferred stock originally issued to the U.S. Department of Treasury.

14. Commitments and Contingencies

The Bank, in the normal course of business, is party to commitments that involve, to varying degrees, elements of risk in excess of the amounts recognized in the financial statements. These commitments include unused lines of credit and commitments to extend credit.

At December 31, 2012, the following commitment and contingent liabilities existed that are not reflected in the accompanying financial statements (in thousands):

	<u>December 31, 2012</u>
Commitments to extend credit	\$ 6,869
Unused lines of credit	7,147

The Bank's maximum exposure to credit losses in the event of nonperformance by the other party to these commitments is represented by the contractual amount. The Bank uses the same credit policies in granting commitments and conditional obligations as it does for amounts recorded in the balance sheets. These commitments and obligations do not necessarily represent future cash flow requirements. The Bank evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary, is based on management's assessment of risk. The Bank maintains an allowance for estimated losses on commitments to extend credit. At December 31, 2012 and 2011, the allowance was \$24,000 and \$10,000, respectively, and is recorded as a component of other non-interest expense.

At December 31, 2012, the Bank was obligated under non-cancellable operating leases on property used for banking purposes. Most leases contain escalation clauses and renewal options which provide for increases in certain property costs including real estate taxes, common area maintenance, and insurance.

Colonial American Bank

Notes to Financial Statements
December 31, 2012 and 2011

The projected minimum annual rental payments under operating leases, are as follows (in thousands):

Year ending December 31,	Rental Payments Operating Leases
2013	\$ 290
2014	267
2015	274
2016	281
2017	289
Thereafter	<u>2,773</u>
Total minimum lease payments	<u>\$ 4,174</u>

Net rental expense included in occupancy expense was approximately \$289,000 and \$137,000 for the years ended December 31, 2012 and 2011, respectively.

In the normal course of business, the Bank may be a party to various outstanding legal proceedings and claims. In the opinion of management, the financial statements will not be materially affected by the outcome of such legal proceedings and claims.

The Bank has entered into employment agreements with its Chief Executive Officer and certain other executive officers of the Bank to ensure the continuity of executive leadership, to clarify roles and responsibilities of executives, and to make explicit the terms and conditions of executive employment. These agreements were for an initial term of three-years, and have a remaining term of two years. The agreements provide for certain level of base annual salary and in the event of a change in control, as defined, or in the event of termination, as defined, certain levels of base salary, and bonus payments.

15. Regulatory Matters

Capital Ratios

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

Colonial American Bank

Notes to Financial Statements
December 31, 2012 and 2011

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the following table) of total and Tier I capital (as defined in the regulations) to risk-weighted assets (as defined), and of Tier I capital (as defined) to average assets (as defined). During 2011, while operating under the Consent Order dated August 11, 2010 (see Note 3), the Bank could not be considered "well-capitalized" and was required to maintain the following capital levels as of December 31, 2011: Tier I capital greater than or equal to 8% of total assets and total risk-based capital greater than or equal to 12% of total risk-weighted assets. At December 31, 2012, subsequent to the termination of the Consent Order, the Bank was required to maintain the following capital levels to be considered "adequately capitalized": Tier I capital greater than or equal to 4% of total assets and total risk-based capital greater than or equal to 8% of total risk-weighted assets. At December 31, 2012 and 2011, the Bank's capital ratios complied with all regulatory requirements.

The following is a summary of the Bank's actual capital amounts and ratios compared to the regulatory requirements as of December 31, 2012 and 2011 (in thousands):

	Actual		Adequacy Purposes		Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2012						
Total Risk Based Capital (to Risk Weighted Assets)	\$ 12,112	15.0%	\$ 6,459	8.0%	\$ 8,074	10.0%
Tier I Capital (to Risk Weighted Assets)	11,100	13.7%	3,230	4.0%	4,037	5.0%
Tier I Capital (to Average Assets)	11,100	8.8%	5,020	4.0%	6,275	5.0%
	Actual		Adequacy Purposes		Under Terms of Consent Order	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2011						
Total Risk Based Capital (to Risk Weighted Assets)	\$ 14,311	43.3%	\$ 2,646	8.0%	\$ 3,969	12.0%
Tier I Capital (to Risk Weighted Assets)	13,897	42.0%	1,323	4.0%	2,646	8.0%
Tier I Capital (to Average Assets)	13,897	33.5%	1,659	4.0%	3,317	8.0%

Banking regulations limit the amount of dividends that may be paid without prior regulatory agency approval. Dividends paid by the Bank would be prohibited if the effect thereof would cause the Bank's capital to be reduced below applicable minimum capital requirements.

16. Related Parties

The Bank had previously entered into consulting agreements with two of its directors that have expired on December 31, 2012. One director has extensive experience in banking, finance and capital markets. This director advised the Bank on business strategy, capital raising plans, and potential investment opportunities. The Bank has recognized consulting expenses totaling \$58,000 and \$97,000 during the years ended December 31, 2012 and 2011, respectively, for this director. The second director also has extensive experience in banking and real estate markets. This director advised the Bank on business strategy, capital raising plans, and loan portfolio reviews. The Bank has recognized consulting expenses of \$60,000 and \$120,000 during the years ended December 31, 2012 and 2011, respectively, for this director.

The Bank also utilized the services of a board member's consulting firm to review the Bank's loan portfolio subsequent to the recapitalization that closed on April 15, 2011. Consulting expenses recognized during the year ended December 31, 2011 related to this board member amounted to \$63,000. In addition, the Bank has its directors and officers liability insurance with an insurance firm at which another board of director is employed. The annual policy amounts to approximately \$50,000.