

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM  
Washington, DC 20551

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2011

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

**FDIC Certificate Number 57690**

**THE CONNECTICUT BANK AND TRUST COMPANY**  
(Exact Name of Registrant as Specified in Its Charter)

CONNECTICUT  
(State or Other Jurisdiction of  
Incorporation or Organization)

90-0115348  
(I.R.S. Employer  
Identification No.)

58 STATE HOUSE SQUARE  
(Address of Principal Executive Offices)

06103  
(Zip Code)

**(860) 246-5200**

(Registrant's Telephone Number, Including Area Code)

Not Applicable

(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)

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

Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes  No

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

Large accelerated filer

Accelerated filer

Non-accelerated filer  (do not check if a smaller reporting company) Smaller reporting company

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

Indicate the number of shares outstanding of each of the issuer’s classes of common stock, as of the latest practicable date.

COMMON STOCK, \$1 par value per share

3,620,950 shares as of November 1, 2011

**THE CONNECTICUT BANK AND TRUST COMPANY  
FORM 10-Q**

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## PART I. FINANCIAL INFORMATION

### Item 1. Financial Statements

#### THE CONNECTICUT BANK AND TRUST COMPANY BALANCE SHEETS (Unaudited)

(In thousands, except share data)	September 30, 2011	December 31, 2010
<b>ASSETS</b>		
Cash and cash equivalents	\$ 13,192	\$ 8,725
Interest-bearing deposits in banks	429	79
Securities available for sale	42,576	35,349
Federal Reserve Bank stock, at cost	780	762
Federal Home Loan Bank stock, at cost	2,057	2,057
Loans held for sale	-	386
Loans	221,376	223,723
Allowance for loan losses	(3,099)	(3,381)
Loans, net	218,277	220,342
Premises and equipment, net	1,744	1,898
Other real estate owned	1,710	682
Deferred tax asset	700	-
Other assets	2,718	3,951
	<u>\$ 284,183</u>	<u>\$ 274,231</u>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Non-interest-bearing deposits	\$ 47,907	\$ 35,972
Interest-bearing deposits	174,637	177,822
Total deposits	222,544	213,794
Secured borrowings	1,098	577
Securities sold under agreements to repurchase	3,987	3,392
Federal Home Loan Bank advances	29,450	30,450
Other borrowings	176	-
Other liabilities	1,141	1,151
Total liabilities	258,396	249,364
Commitments and contingencies (Notes 7 and 10)		
Stockholders' equity:		
Preferred stock, no par value; 1,000,000 shares authorized; issued and outstanding: 5,448 shares; aggregate liquidation preference of \$5,448	5,448	5,448
Discount on preferred stock	(287)	(374)
Common stock, \$1.00 par value; 10,000,000 shares authorized; 3,620,950 shares issued and outstanding	3,621	3,621
Common stock warrants	1,405	1,405
Additional paid-in capital	30,115	30,088
Restricted stock unearned compensation	(118)	(163)
Accumulated deficit	(14,476)	(15,272)
Accumulated other comprehensive income	79	114
Total stockholders' equity	25,787	24,867
	<u>\$ 284,183</u>	<u>\$ 274,231</u>

The accompanying notes are an integral part of these unaudited financial statements.

**THE CONNECTICUT BANK AND TRUST COMPANY**

**Statements of Operations**

(Unaudited)

(In thousands, except per share data)	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2011	2010	2011	2010
Interest and dividend income:				
Loans, including fees	\$ 2,974	\$ 3,159	\$ 8,926	\$ 9,269
Debt securities	239	237	683	728
Other	24	23	60	70
Total interest and dividend income	3,237	3,419	9,669	10,067
Interest expense:				
Deposits	461	559	1,392	1,731
Securities sold under agreements to repurchase	4	4	10	10
Federal Home Loan Bank advances	267	273	791	806
Total interest expense	732	836	2,193	2,547
Net interest income	2,505	2,583	7,476	7,520
Provision for loan losses	398	587	662	896
Net interest income, after provision for loan losses	2,107	1,996	6,814	6,624
Noninterest income:				
Customer service fees	130	103	360	249
Brokerage commissions	88	63	251	206
Net gain on sales of available-for-sale securities	310	-	448	60
Loss on sale of other real estate owned	-	(4)	-	(4)
Net gain on sales of loans	24	24	66	33
Total noninterest income	552	186	1,125	544
Noninterest expenses:				
Salaries and benefits	1,165	1,131	3,586	3,394
Occupancy and equipment	454	452	1,350	1,323
Data processing	88	90	258	248
Marketing	106	100	244	286
Professional services	262	165	742	497
FDIC insurance	101	99	368	289
Other general and administrative	318	280	1,004	759
Total noninterest expenses	2,494	2,317	7,552	6,796
Income (loss) before income tax benefit	165	(135)	387	372
Income tax benefit	-	-	700	-
Net income (loss)	165	(135)	1,087	372
Less preferred stock dividend and accretion	(97)	(97)	(291)	(291)
Net income (loss) attributable to common shareholders	\$ 68	\$ (232)	\$ 796	\$ 81
Net income (loss) per common share:				
Basic	\$ 0.02	\$ (0.06)	\$ 0.22	\$ 0.02
Diluted	\$ 0.02	\$ (0.06)	\$ 0.22	\$ 0.02
Average basic common shares issued and outstanding	3,621	3,621	3,621	3,615
Average diluted common shares issued and outstanding	3,663	3,621	3,670	3,629

The accompanying notes are an integral part of these unaudited financial statements.

**THE CONNECTICUT BANK AND TRUST COMPANY**  
**STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY**  
**Nine Months Ended September 30, 2011 and 2010**  
**(Unaudited)**

(In thousands)	Preferred Stock	Discount on Preferred Stock	Common Stock	Common Stock Warrants	Additional Paid-in Capital	Restricted Stock Unearned Compensation	Accumulated Deficit	Accumulated Other Comprehensive Income (Loss)	Total
Balance at December 31, 2009	\$ 5,448	\$ (489)	\$ 3,572	\$ 1,405	\$ 29,858	\$ (29)	\$ (15,444)	\$ (268)	<u>\$ 24,053</u>
Comprehensive income:									
Net income	-	-	-	-	-	-	372	-	372
Change in net unrealized gain on securities available for sale, net of reclassification adjustment of \$60	-	-	-	-	-	-	-	563	<u>563</u>
Total comprehensive income									<u>935</u>
Cash dividends declared on preferred stock	-	-	-	-	-	-	(204)	-	(204)
Accretion of discount on preferred stock	-	87	-	-	-	-	(87)	-	-
Share-based compensation - restricted stock grant	-	-	49	-	156	(205)	-	-	-
Share-based compensation - stock options	-	-	-	-	55	-	-	-	55
Share-based compensation - restricted stock awards	-	-	-	-	-	58	-	-	58
Balance at September 30, 2010	<u>\$ 5,448</u>	<u>\$ (402)</u>	<u>\$ 3,621</u>	<u>\$ 1,405</u>	<u>\$ 30,069</u>	<u>\$ (176)</u>	<u>\$ (15,363)</u>	<u>\$ 295</u>	<u>\$ 24,897</u>
Balance at December 31, 2010	\$ 5,448	\$ (374)	\$ 3,621	\$ 1,405	\$ 30,088	\$ (163)	\$ (15,272)	\$ 114	<u>\$ 24,867</u>
Comprehensive income:									
Net income	-	-	-	-	-	-	1,087	-	1,087
Change in net unrealized loss on securities available for sale, net of reclassification adjustment of \$448	-	-	-	-	-	-	-	(35)	<u>(35)</u>
Total comprehensive income									<u>1,052</u>
Cash dividends declared on preferred stock	-	-	-	-	-	-	(204)	-	(204)
Accretion of discount on preferred stock	-	87	-	-	-	-	(87)	-	-
Share-based compensation - stock options	-	-	-	-	27	-	-	-	27
Share-based compensation - restricted stock awards	-	-	-	-	-	45	-	-	45
Balance at September 30, 2011	<u>\$ 5,448</u>	<u>\$ (287)</u>	<u>\$ 3,621</u>	<u>\$ 1,405</u>	<u>\$ 30,115</u>	<u>\$ (118)</u>	<u>\$ (14,476)</u>	<u>\$ 79</u>	<u>\$ 25,787</u>

The accompanying notes are an integral part of these unaudited financial statements.

**THE CONNECTICUT BANK AND TRUST COMPANY**  
**Statements of Cash Flows**  
**(Unaudited)**

(In thousands)	Nine Months Ended September 30,	
	2011	2010
Cash flows from operating activities:		
Net income	\$ 1,087	\$ 372
Adjustments to reconcile net income to net cash (used) provided by operating activities:		
Provision for loan losses	662	896
Net gains on sales of available-for-sale securities	(448)	(60)
Depreciation and amortization	364	381
Net amortization of premiums on available-for-sale securities	286	383
Net amortization of deferred loan costs and fees	166	80
Share-based compensation plans	72	113
Deferred income tax benefit	(700)	-
Decrease in loans held for sale	386	-
Decrease (increase) in accrued interest receivable	112	(215)
Increase in other assets	(2,232)	(205)
(Decrease) increase in other liabilities	(10)	10
Net cash (used) provided by operating activities	(255)	1,755
Cash flows from investing activities:		
Activity in available-for-sale securities:		
Sales	15,569	6,902
Maturities and calls	13,446	3,000
Purchases	(38,061)	(19,319)
Principal payments	2,946	5,534
Purchases of certificates of deposit	(350)	(1)
Purchases of FRB stock	(18)	(38)
Net loan principal repayments (originations and purchases)	2,738	(18,654)
Purchases of premises and equipment	(210)	(215)
Net cash used by investing activities	(3,940)	(22,791)
Cash flows from financing activities:		
Net increase in deposits	8,750	12,183
Net increase in secured borrowings	521	-
Increase (decrease) in securities sold under agreement to repurchase	595	(999)
Repayments of FHLB advances	(1,000)	-
Preferred cash dividends paid	(204)	(204)
Net cash provided by financing activities	8,662	10,980
Net change in cash and cash equivalents	4,467	(10,056)
Cash and cash equivalents at beginning of period	8,725	27,117
Cash and cash equivalents at end of period	\$ 13,192	\$ 17,061
Supplemental disclosures of cash flow information:		
Interest paid	\$ 2,277	\$ 2,577
Loans transferred to other real estate owned	\$ 1,501	\$ 226
Liability assumed on other real estate owned	\$ 176	\$ -

The accompanying notes are an integral part of these unaudited financial statements.

**THE CONNECTICUT BANK AND TRUST COMPANY**  
**Notes to Unaudited Financial Statements**  
**September 30, 2011**

**(1) Organization**

The Connecticut Bank and Trust Company (“CBT” or the “Bank”) is a state chartered bank and trust company operating primarily in North Central Connecticut. CBT operates out of its main office at 58 State House Square, Hartford, Connecticut and branch offices at 7 Sycamore Street, Glastonbury, Connecticut; 66 Cedar Street, Newington, Connecticut; 435 Hartford Turnpike, Vernon, Connecticut; 68 South Main Street, West Hartford, Connecticut; 396 Cromwell Avenue, Rocky Hill, Connecticut; 148 Broad Street, Windsor, Connecticut; and St. Francis Hospital, Hartford, Connecticut. CBT is subject to competition from other financial institutions, including but not limited to commercial banks, savings banks, credit unions and mortgage banking companies. CBT is also subject to the regulations of, and periodic examinations by, the Connecticut Department of Banking (“DOB”) and the Board of Governors of the Federal Reserve System (“Fed”) through the Federal Reserve Bank of Boston (“FRBB”). CBT’s deposits are insured up to the limits specified by the Federal Deposit Insurance Corporation (“FDIC”).

**(2) Use of Estimates**

In preparing financial statements in conformity with accounting principles generally accepted in the United States of America, CBT’s management (“Management”) is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the balance sheet and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses, other-than-temporary impairment of securities and the valuation of deferred tax assets.

**(3) Basis of Presentation**

In the opinion of Management, the accompanying unaudited financial statements contain all adjustments necessary to present fairly the financial position at September 30, 2011, the results of operations for the three and nine month periods ended September 30, 2011 and 2010 and changes in stockholders’ equity and cash flows for the nine month periods ended September 30, 2011 and 2010. These adjustments consist only of normal recurring adjustments. Certain amounts in prior periods have been reclassified to conform to the current presentation. The results of operations for the three and nine month periods are not necessarily indicative of the results to be expected for the full year. The statements should be read in conjunction with the financial statements and accompanying notes found on pages 49-81 of CBT’s Annual Report on Form 10-K for the year ended December 31, 2010 filed with the Board of Governors of the Federal Reserve System on March 31, 2011.

**(4) Net Income (Loss) Per Common Share**

Basic net income (loss) per common share represents net income (loss) attributable to common stockholders divided by the weighted-average number of common shares outstanding during the period. Diluted net income per common share reflects additional common shares that would have been outstanding if dilutive potential common shares had been issued. Potential common shares that may be issued by CBT are primarily associated with outstanding warrants and stock options and are determined using the treasury stock method.

Net income (loss) per common share for the three and nine months ended September 30, 2011 and 2010 have been computed based upon the following:

(Dollars in thousands, except per share data)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2011	2010	2011	2010
Net income (loss)	\$ 165	\$ (135)	\$ 1,087	\$ 372
Preferred stock dividend and accretion	(97)	(97)	(291)	(291)
Net income (loss) attributable to common shareholders	<u>\$ 68</u>	<u>\$ (232)</u>	<u>\$ 796</u>	<u>\$ 81</u>
Average number of common shares outstanding	3,620,950	3,620,950	3,620,950	3,612,643
Add: dilutive effect of warrants	<u>42,213</u>	<u>-</u>	<u>48,603</u>	<u>20,997</u>
Average number of common shares outstanding used to calculate diluted net income per common share	<u>3,663,163</u>	<u>3,620,950</u>	<u>3,669,553</u>	<u>3,633,640</u>
Net income (loss) per common share:				
Basic	<u>\$ 0.02</u>	<u>\$ (0.06)</u>	<u>\$ 0.22</u>	<u>\$ 0.02</u>
Diluted	<u>\$ 0.02</u>	<u>\$ (0.06)</u>	<u>\$ 0.22</u>	<u>\$ 0.02</u>
Anti-dilutive common stock equivalents not included in the above computation:				
Stock options	141,900	141,900	141,900	141,900
Warrants	170,500	346,242	170,500	170,500

## (5) Securities Available for Sale

The following table sets forth information regarding the amortized cost and market values of CBT's securities at the dates indicated.

(In thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
<u>September 30, 2011</u>				
Government-sponsored enterprises	\$ 6,518	\$ 10	\$ (1)	\$ 6,527
U.S. Government guaranteed residential mortgage-backed securities	20,784	158	(162)	20,780
Government-sponsored residential mortgage-backed securities	12,394	158	(79)	12,473
U.S. Government guaranteed commercial mortgage-backed securities	1,802	123	-	1,925
Corporate bonds	999	-	(128)	871
	<u>\$ 42,497</u>	<u>\$ 449</u>	<u>\$ (370)</u>	<u>\$ 42,576</u>
<u>December 31, 2010</u>				
Government-sponsored enterprises	\$ 6,540	\$ -	\$ (196)	\$ 6,344
U.S. Government guaranteed residential mortgage-backed securities	5,935	195	(2)	6,128
Government-sponsored residential mortgage-backed securities	12,803	297	(37)	13,063
U.S. Government guaranteed commercial mortgage-backed securities	8,958	70	(40)	8,988
Corporate bonds	999	-	(173)	826
	<u>\$ 35,235</u>	<u>\$ 562</u>	<u>\$ (448)</u>	<u>\$ 35,349</u>

Proceeds from the sales of securities amounted to \$11.6 million and \$15.6 million, respectively, for the three and nine months ended September 30, 2011 with the Bank realizing gross gains of \$310,000 and \$448,000, respectively, and no losses on the sale of such securities. For the three and nine months ended September 30, 2010, proceeds from the sales of securities amounted to \$7.3 million and \$6.9 million, respectively, with the Bank realizing gross gains of \$0 and \$60,000, respectively, and no losses on the sale of such securities.

Information pertaining to securities available for sale with gross unrealized losses at September 30, 2011 and December 31, 2010, aggregated by investment category and length of time that individual securities have been in a loss position, is as follows:

(In thousands)	Less Than Twelve Months		Over Twelve Months	
	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value
<u>September 30, 2011</u>				
Government-sponsored enterprises	\$ 1	\$ 1,010	\$ -	\$ -
U.S. Government guaranteed residential mortgage-backed securities	162	9,882	-	-
Government-sponsored residential mortgage-backed securities	79	7,445	-	-
U.S. Government guaranteed commercial mortgage-backed securities	-	-	-	-
Corporate bonds	-	-	128	871
	<u>\$ 242</u>	<u>\$ 18,337</u>	<u>\$ 128</u>	<u>\$ 871</u>
<u>December 31, 2010</u>				
Government-sponsored enterprises	\$ 196	\$ 6,344	\$ -	\$ -
U.S. Government guaranteed residential mortgage-backed securities	2	919	-	-
Government-sponsored residential mortgage-backed securities	37	6,894	-	-
U.S. Government guaranteed commercial mortgage-backed securities	40	6,883	-	-
Corporate bonds	-	-	173	826
	<u>\$ 275</u>	<u>\$ 21,040</u>	<u>\$ 173</u>	<u>\$ 826</u>

Each reporting period, the Bank evaluates all securities with a decline in fair value below the amortized cost of the investment to determine whether or not the impairment is deemed to be other-than-temporary (“OTTI”). OTTI is required to be recognized if (1) the Bank intends to sell the security; (2) it is “more likely than not” that the Bank will be required to sell the security before the recovery of its amortized cost basis; or (3) the present value of expected cash flows is not sufficient to recover the entire amortized cost basis. For all impaired securities that the Bank intends to sell, or that are more likely than not that the Bank will be required to sell, the full amount of the depreciation is recognized as OTTI through earnings. Credit-related OTTI for all impaired debt securities is recognized through earnings. Non-credit related OTTI for such debt securities is recognized in other comprehensive income, net of applicable taxes.

At September 30, 2011, the Bank had 1 government-sponsored enterprise security with an unrealized loss totaling \$1 thousand. This represented 0.10% of the amortized cost of the securities. The Bank also had 8 U.S. government-guaranteed residential mortgage-backed securities and 5 government-sponsored residential mortgage-backed securities with unrealized losses totaling \$162 thousand and \$79 thousand, respectively. This represented 0.78% and 0.64%, respectively, of the amortized cost of the securities.

Management currently believes that none of the unrealized losses are other than temporary because the debt and mortgage-backed securities are issued and guaranteed by government agencies or government sponsored enterprises. Because the decline in market value is attributable to changes in interest rates and not to credit quality, and because the Bank does not intend to sell the investments and it is more likely than not that the Bank will not be required to sell the investments before recovery of their amortized cost basis, which may be maturity, the Bank does not consider these investments to be other-than-temporarily impaired at September 30, 2011.

The Bank's unrealized loss on the corporate bond segment of the portfolio relates to a senior unsecured obligation from Sallie Mae ("SLM Corp" or "SLM"). SLM provides funding and servicing for student loans. At September 30, 2011, the SLM bond has depreciation totaling 12.8% of its amortized cost and the unrealized losses have existed for more than twelve months. Management believes that the cause of such a decline is driven by the thin trading volume of this bond and the overall illiquidity in the bond market. The value of the bond has declined since June 30, 2011. Because the decline in market value is attributable to illiquidity and to changes in interest rates and not to credit quality, and because the Bank does not intend to sell the investment and it is more likely than not that the Bank will not be required to sell the investment before recovery of the amortized cost basis, which may be maturity, the Bank does not consider the investment to be other-than-temporarily impaired at September 30, 2011.

The amortized cost and fair value of debt securities by contractual maturity as of September 30, 2011 are as follows:

(In thousands)	Amortized Cost	Fair Value
Government-sponsored enterprises:		
Over 1 year to 5 years	\$ 2,011	\$ 2,010
Over 5 years to 10 years	-	-
Over 10 years	4,507	4,517
	<u>6,518</u>	<u>6,527</u>
Corporate bonds:		
Over 1 year to 5 years	999	871
	<u>7,517</u>	<u>7,398</u>
Mortgage-backed securities	34,980	35,178
	<u>\$ 42,497</u>	<u>\$ 42,576</u>

**(6) Loans and Allowance for Loan Losses:**

A summary of the balances of loans is as follows:

(In thousands)	<u>September 30, 2011</u>	<u>December 31, 2010</u>
Commercial real estate:		
Owner occupied	\$ 63,721	\$ 66,020
Non-owner occupied	57,293	50,122
Residential real estate:		
Residential 1-4 family	11,265	9,726
Second mortgages	473	478
Equity lines of credit	8,084	8,480
Construction	<u>10,814</u>	<u>13,766</u>
Total mortgage loans on real estate	151,650	148,592
Commercial loans	63,171	69,110
Consumer loans	<u>6,196</u>	<u>5,627</u>
Total loans	221,017	223,329
Allowance for loan losses	(3,099)	(3,381)
Net deferred loan costs	<u>359</u>	<u>394</u>
Loans, net	<u>\$ 218,277</u>	<u>\$ 220,342</u>

The following table summarizes the changes in the allowance for loan losses by portfolio segment:

(In thousands)

Three months ended September 30, 2011	Commercial Real Estate	Commercial	Construction	Consumer/ Residential	Unallocated	Total
Balance at beginning of period	\$ 1,686	\$ 1,260	\$ 127	\$ 151	\$ 180	\$ 3,404
Provision (credit) for loan losses	233	362	(9)	(8)	(180)	398
Loans charged-off	-	(702)	-	(2)	-	(704)
Recoveries of loans previously charged-off	-	-	-	1	-	1
Balance at end of period	\$ 1,919	\$ 920	\$ 118	\$ 142	\$ -	\$ 3,099

Nine months ended September 30, 2011	Commercial Real Estate	Commercial	Construction	Consumer/ Residential	Unallocated	Total
Balance at beginning of period	\$ 1,527	\$ 1,301	\$ 420	\$ 133	\$ -	\$ 3,381
Provision (credit) for loan losses	392	519	(302)	53	-	662
Loans charged-off	-	(905)	-	(45)	-	(950)
Recoveries of loans previously charged-off	-	5	-	1	-	6
Balance at end of period	\$ 1,919	\$ 920	\$ 118	\$ 142	\$ -	\$ 3,099

Three months ended September 30, 2010	Commercial Real Estate	Commercial	Construction	Consumer/ Residential	Unallocated	Total
Balance at beginning of period	\$ 1,541	\$ 1,225	\$ 36	\$ 124	\$ -	\$ 2,926
Provision (credit) for loan losses	(250)	400	435	2	-	587
Loans charged-off	-	(287)	-	(1)	-	(288)
Recoveries of loans previously charged-off	-	22	-	-	-	22
Balance at end of period	\$ 1,291	\$ 1,360	\$ 471	\$ 125	\$ -	\$ 3,247

Nine months ended September 30, 2010	Commercial Real Estate	Commercial	Construction	Consumer/ Residential	Unallocated	Total
Balance at beginning of period	\$ 1,351	\$ 1,037	\$ 237	\$ 77	\$ -	\$ 2,702
Provision (credit) for loan losses	(60)	625	234	97	-	896
Loans charged-off	-	(324)	-	(49)	-	(373)
Recoveries of loans previously charged-off	-	22	-	-	-	22
Balance at end of period	\$ 1,291	\$ 1,360	\$ 471	\$ 125	\$ -	\$ 3,247

Further information pertaining to the allowance for loan losses and impaired loans at September 30, 2011 and December 31, 2010 is as follows:

(In thousands)	<u>Commercial Real Estate</u>	<u>Commercial</u>	<u>Construction</u>	<u>Consumer/ Residential</u>	<u>Unallocated</u>	<u>Total</u>
<u>September 30, 2011</u>						
Amount of allowance for loan losses related to loans individually evaluated for impairment	<u>\$ 78</u>	<u>\$ 42</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 120</u>
Amount of allowance for loan losses related to loans collectively evaluated for impairment	<u>\$ 1,841</u>	<u>\$ 878</u>	<u>\$ 118</u>	<u>\$ 142</u>	<u>\$ -</u>	<u>\$ 2,979</u>
Loans individually evaluated for impairment	<u>\$ 10,729</u>	<u>\$ 3,278</u>	<u>\$ 2,427</u>	<u>\$ 32</u>	<u>\$ -</u>	<u>\$ 16,466</u>
Loans collectively evaluated for impairment	<u>\$ 110,285</u>	<u>\$ 59,893</u>	<u>\$ 8,387</u>	<u>\$ 25,986</u>	<u>\$ -</u>	<u>\$ 204,551</u>
<u>December 31, 2010</u>						
Amount of allowance for loan losses related to loans individually evaluated for impairment	<u>\$ 50</u>	<u>\$ 344</u>	<u>\$ 224</u>	<u>\$ 18</u>	<u>\$ -</u>	<u>\$ 636</u>
Amount of allowance for loan losses related to loans collectively evaluated for impairment	<u>\$ 1,509</u>	<u>\$ 961</u>	<u>\$ 164</u>	<u>\$ 110</u>	<u>\$ 1</u>	<u>\$ 2,745</u>
Loans individually evaluated for impairment	<u>\$ 9,700</u>	<u>\$ 2,320</u>	<u>\$ 2,854</u>	<u>\$ 50</u>	<u>\$ -</u>	<u>\$ 14,924</u>
Loans collectively evaluated for impairment	<u>\$ 106,442</u>	<u>\$ 66,790</u>	<u>\$ 10,912</u>	<u>\$ 24,261</u>	<u>\$ -</u>	<u>\$ 208,405</u>

The following is a summary of past due and nonaccrual loans:

(In thousands)	30-89 Days Past Due and Still Accruing	Past Due 90 Days or More and Still Accruing	Total Past Due and Still Accruing	Non accrual Loans	Total Past Due incl Non accruals
<u>September 30, 2011</u>					
Commercial real estate owner-occupied	\$ -	\$ -	\$ -	\$ 5,799	\$ 5,799
Commercial real estate non-owner occupied	3,834	-	3,834	2,614	6,448
Commercial	269	-	269	2,862	3,131
Construction	-	-	-	1,572	1,572
Residential real estate	-	-	-	32	32
Consumer	89	-	89	-	89
Total	<u>\$ 4,192</u>	<u>\$ -</u>	<u>\$ 4,192</u>	<u>\$ 12,879</u>	<u>\$ 17,071</u>
<u>December 31, 2010</u>					
Commercial real estate owner-occupied	\$ 3,388	\$ -	\$ 3,388	\$ 2,576	\$ 5,964
Commercial real estate non-owner occupied	809	1,103	1,912	2,890	4,802
Commercial	298	-	298	3,246	3,544
Construction	2,266	-	2,266	-	2,266
Residential real estate	71	-	71	50	121
Consumer	215	46	261	23	284
Total	<u>\$ 7,047</u>	<u>\$ 1,149</u>	<u>\$ 8,196</u>	<u>\$ 8,785</u>	<u>\$ 16,981</u>

The following is a summary of impaired loans at September 30, 2011 and December 31, 2010:

(In thousands)	Recorded Investment	Unpaid Principal Balance	Related Allowance
<u>September 30, 2011</u>			
Impaired loans without a valuation allowance:			
Commercial real estate owner-occupied	\$ 3,186	\$ 3,186	\$ -
Commercial real estate non-owner occupied	4,565	4,565	-
Commercial	3,223	3,874	-
Construction	2,427	2,427	-
Consumer/residential	32	82	-
Total	<u>13,433</u>	<u>14,134</u>	<u>-</u>
Impaired loans with a valuation allowance:			
Commercial real estate owner-occupied	2,060	2,060	20
Commercial real estate non-owner occupied	918	918	58
Commercial	55	55	42
Construction	-	-	-
Consumer/residential	-	-	-
Total	<u>3,033</u>	<u>3,033</u>	<u>120</u>
Total impaired loans	<u>\$ 16,466</u>	<u>\$ 17,167</u>	<u>\$ 120</u>

(In thousands)	Recorded Investment	Unpaid Principal Balance	Related Allowance
<u>December 31, 2010</u>			
Impaired loans without a valuation allowance:			
Commercial real estate owner-occupied	\$ 3,429	\$ 3,429	\$ -
Commercial real estate non-owner occupied	2,870	2,870	-
Commercial	1,266	1,266	-
Construction	1,298	1,298	-
Total	<u>8,863</u>	<u>8,863</u>	<u>-</u>
Impaired loans with a valuation allowance:			
Commercial real estate non-owner occupied	3,401	3,464	50
Commercial	1,054	1,054	344
Construction	1,556	1,556	224
Consumer/residential	50	50	18
Total	<u>6,061</u>	<u>6,124</u>	<u>636</u>
Total impaired loans	<u>\$ 14,924</u>	<u>\$ 14,987</u>	<u>\$ 636</u>

(In thousands)	Three Months Ended September 30, 2011		Nine Months Ended September 30, 2011	
	Average Recorded Investment	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized
Average investment in impaired loans:				
Commercial real estate owner-occupied	\$ 5,823	\$ -	\$ 5,940	\$ 70
Commercial real estate non-owner occupied	8,868	55	9,717	153
Commercial	2,492	5	2,558	24
Construction	2,456	15	2,867	54
Consumer/residential	102	-	109	1
Total	<u>\$ 19,741</u>	<u>\$ 75</u>	<u>\$ 21,191</u>	<u>\$ 302</u>

Interest income recognized for impaired loans on a cash-basis method during the three and nine months ended September 30, 2011 totaled \$75,000 and \$302,000, respectively.

## Allowance for Loan Losses

The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when Management believes the uncollectability of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

The allowance for loan losses is evaluated on a regular basis by Management and is based upon Management's periodic review of the collectability of the loans. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available. The allowance consists of general and allocated and unallocated components, as further described below.

**General component.** The general component of the allowance for loan losses is based on historical loss experience adjusted for qualitative factors stratified by the following loan segments: commercial, commercial real estate, construction and consumer and residential real estate. There were no changes in the Bank's policies or methodology pertaining to the general component of the allowance for loan losses during 2011. The qualitative factors are determined based on the various risk characteristics of each loan segment. Risk characteristics relevant to each portfolio segment are as follows:

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

Commercial real estate – Loans in this segment are primarily income-producing properties in the Greater Hartford area. The underlying cash flows generated by properties are adversely impacted by a downturn in the economy as evidenced by increased vacancy rates, which in turn, will have an effect on the credit quality in this segment. Management obtains rent rolls annually and continually monitors the cash flows of these loans.

Construction loans – Loans in this segment primarily include speculative real estate development loans for which payment is derived from the sale of the property. Credit risk is affected by cost overruns, time to sell at an adequate price and market conditions.

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

**Allocated component.** The allocated component relates to loans that are classified as impaired. Impairment is measured on a loan by loan basis for commercial, commercial real estate and construction loans by either the present value of expected future cash flows discounted at the loan's effective interest rate or the fair value of the collateral if the loan is collateral dependant. An allowance is established when the discounted cash flows or collateral value of the impaired loan is lower than the carrying value of that loan. Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. Accordingly, the Bank does not separately identify individual consumer and residential loans for impairment disclosures, unless such loans are subject to a troubled debt restructuring ("TDR") agreement.

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

The Bank may periodically agree to modify the contractual terms of loans. When a loan is modified and a concession is made to a borrower experiencing financial difficulty, the modification is considered a TDR. All TDRs are initially classified as impaired.

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

the underlying assumptions used in the methodologies for estimating allocated and general losses in the portfolio. For the nine months ended September 30, 2011, the Bank had an unallocated reserve of \$1,000 compared to none for the nine months ended September 30, 2010.

No additional funds are committed to be advanced in connection with impaired loans. For the nine months ended September 30, 2011, interest income of \$29,000 was reversed compared to none for the nine months ended September 30, 2010. All nonaccrual loans are accounted for on the cash basis.

The following is a summary of troubled debt restructurings for the three and nine months ended September 30, 2011:

	Three Months Ended September 30, 2011			Nine Months Ended September 30, 2011		
	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
(In thousands)						
Commercial real estate non-owner occupied	1	\$ 732	\$ 552	1	\$ 732	\$ 552

One non-owner occupied commercial real estate loan was modified during the three and nine months ended September 30, 2011. This loan modification was the foreclosure of a portion of the collateral that partially satisfied this loan in the amount of \$180,000.

At September 30, 2011 and December 31, 2010, there were three loans totaling \$1.9 million and two loans totaling \$1.4 million, respectively, accounted for as troubled debt restructurings. The terms of these loans were modified in the prior year. These loans are considered impaired and on nonaccrual basis.

For the period ended September 30, 2011, there were no payment defaults on troubled debt restructurings.

#### Credit Quality Information

CBT utilizes an eight grade internal loan rating system for its loans as follows:

Loans rated 1-3A: Loans in these categories are considered “pass” rated loans with low to average risk.

Loans rated 4: Loans in this category are considered “special mention.” These loans are starting to show signs of potential weakness and are being closely monitored by Management.

Loans rated 5: Loans in this category are considered “substandard.” Generally, a loan is considered substandard if it is inadequately protected by the current net worth and paying capacity of the obligors and/or the value of the assets pledged as collateral for the loan. There is a distinct possibility that the Bank will sustain some loss if the weakness is not corrected.

Loans rated 6: Loans in this category are considered “doubtful.” Loans classified as doubtful have all the weakness inherent in those loans classified as substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, highly questionable and improbable.

Loans rated 7: Loans in this category are considered uncollectible (“loss”) and of such little value that their continuance as loans is not warranted.

On an annual basis, or more often if needed, Management formally reviews the ratings on all loans. Semi-annually, the Bank engages an independent third party to review a significant portion of loans within these segments. Management uses the results of these reviews as part of its annual review process.

The following table presents the Bank's loans by risk rating at September 30, 2011 and December 31, 2010:

(In thousands)	<u>Commercial Real Estate</u>	<u>Commercial</u>	<u>Construction</u>	<u>Consumer/ Residential</u>	<u>Total Loans</u>
<u>September 30, 2011</u>					
Loans rated 1-3A	\$ 97,964	\$ 54,429	\$ 8,037	\$ 25,275	\$ 185,705
Loans rated 4	7,955	2,430	-	26	10,411
Loans rated 5	15,095	6,282	2,777	685	24,839
Loans rated 6	-	30	-	32	62
Loans rated 7	-	-	-	-	-
Total	<u>\$ 121,014</u>	<u>\$ 63,171</u>	<u>\$ 10,814</u>	<u>\$ 26,018</u>	<u>\$ 221,017</u>
 <u>December 31, 2010</u>					
Loans rated 1-3A	\$ 91,949	\$ 60,159	\$ 8,578	\$ 23,543	\$ 184,229
Loans rated 4	13,271	4,079	2,334	18	19,702
Loans rated 5	10,922	4,872	2,854	700	19,348
Loans rated 6	-	-	-	50	50
Loans rated 7	-	-	-	-	-
Total	<u>\$ 116,142</u>	<u>\$ 69,110</u>	<u>\$ 13,766</u>	<u>\$ 24,311</u>	<u>\$ 223,329</u>

## **(7) Loan Commitments**

CBT is a party to credit related financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit. Such commitments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized on the balance sheets. CBT's commitments to extend credit include unfunded loans and unused lines of credit that comprised an aggregate \$51.1 million at September 30, 2011 and \$43.9 million at December 31, 2010. CBT also had commitments to originate loans and a letter of credit totaling \$7.9 million and \$962,000 at September 30, 2011 compared to \$10.0 million and \$1.1 million at December 31, 2010, respectively.

## **(8) Fair Value of Assets and Liabilities**

### ***Determination of Fair Value***

The Bank uses fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value is best determined based upon quoted market prices. However, in many instances, there are no quoted market prices for the Bank's various assets and liabilities. In cases where quoted market prices are not available, fair value is based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. Accordingly, the fair value estimates may not be realized in an immediate settlement of the asset or liability.

The following methods and assumptions were used by the Bank in estimating fair value disclosures for financial instruments:

Cash and cash equivalents: The carrying amounts of cash and cash equivalents approximate fair value based on the short term nature of the assets.

Interest-bearing deposits in banks: Fair values of interest-bearing deposits in banks are estimated using discounted cash flow analyses based on current market rates for similar types of deposits.

Securities available for sale: Securities measured at fair value in Level 2 are based on pricing models that consider standard input factors such as observable market data, benchmark yields, interest rate volatilities, broker/dealer quotes, credit spreads and new issue data. These securities include government-sponsored enterprise obligations, FHLMC and FNMA bonds, corporate bonds, and other securities. All fair value measurements are obtained from a third party pricing service and are not adjusted by management.

Federal Home Loan Bank and Federal Reserve Bank stock: The carrying amount of FHLB and Federal Reserve Bank stock approximates fair value based on the redemption provisions of the FHLB and FRB.

Loans held for sale: Loans held for sale are accounted for at the lower of cost or market and the fair value of loans held for sale based on quoted market prices of similar loans sold in conjunction with securitization transactions, adjusted as required for changes in loan characteristics.

Loans, net: For variable-rate loans that re-price frequently and with no significant change in credit risk, fair values are based on carrying values. Fair values for other loans are estimated using discounted cash flows analyses, using market interest rates currently being offered for loans with similar terms to borrowers of similar credit quality. Fair values for nonperforming loans are estimated using discounted cash flow analyses or underlying collateral values, where applicable.

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

Secured borrowings: The carrying amounts of secured borrowings approximate fair value.

Short-term borrowings: For short-term borrowings maturing within ninety days, carrying values approximate fair values.

Long-term debt: The fair values of the Bank's long-term borrowings are estimated using discounted cash flow analyses based on the current incremental borrowing rates in the market for similar types of borrowing arrangements.

Other borrowings: The carrying amounts of other borrowings approximate fair value.

Accrued interest: The carrying amounts of accrued interest approximate fair value.

Off-balance-sheet instruments: Fair values for off-balance-sheet credit-related financial instruments are based on fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the counterparties' credit standing. The estimated fair value of off-balance-sheet financial instruments is immaterial.

CBT groups its assets measured at fair value in three levels, based on markets in which the assets are traded and reliability of the assumptions used to determine fair value.

Level 1. Quoted prices in active markets for identical assets. Level 1 assets include debt and equity securities that are traded on an active exchange market. Valuations are obtained from readily available pricing sources for market transactions involving identical assets.

Level 2. Observable inputs other than Level 1 prices, such as quoted prices for similar assets; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets.

Level 3. Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets. Level 3 assets include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

*Assets measured at fair value on a recurring basis are summarized as follows:*

(In thousands)	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total Fair Value</u>
<u>September 30, 2011</u>				
Government-sponsored enterprises	\$ -	\$ 6,527	\$ -	\$ 6,527
U.S. Government guaranteed residential mortgage-backed securities	-	20,780	-	20,780
Government-sponsored residential mortgage-backed securities	-	12,473	-	12,473
U.S. Government guaranteed commercial mortgage-backed securities	-	1,925	-	1,925
Corporate bonds	-	871	-	871
Securities available for sale	<u>\$ -</u>	<u>\$ 42,576</u>	<u>\$ -</u>	<u>\$ 42,576</u>
 <u>December 31, 2010</u>				
Government-sponsored enterprises	\$ -	\$ 6,344	\$ -	\$ 6,344
U.S. Government guaranteed residential mortgage-backed securities	-	6,128	-	6,128
Government-sponsored residential mortgage-backed securities	-	13,063	-	13,063
U.S. Government guaranteed commercial mortgage-backed securities	-	8,988	-	8,988
Corporate bonds	-	826	-	826
Securities available for sale	<u>\$ -</u>	<u>\$ 35,349</u>	<u>\$ -</u>	<u>\$ 35,349</u>

There were no transfers to or from Levels 1 and 2 during the nine months ended September 30, 2011 or 2010.

*Assets measured at fair value on a nonrecurring basis are summarized as follows:*

The Bank may also be required, from time to time, to measure certain other assets on a nonrecurring basis in accordance with generally accepted accounting principles. These adjustments to fair value usually result from application of lower-of-cost-or-market accounting or write-downs of individual assets. The following table summarizes the fair value hierarchy used to determine each adjustment and the carrying value of the related individual assets at the dates indicated.

(In thousands)	Level 1	Level 2	Level 3
<u>September 30, 2011</u>			
Impaired loans	\$ -	\$ -	\$ 2,913
Other real estate owned	-	-	1,710
Total	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 4,623</u>
<u>December 31, 2010</u>			
Impaired loans	\$ -	\$ -	\$ 5,030
Other real estate owned	-	-	682
Total	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 5,712</u>

Gains and losses applicable to impaired loans and other real estate owned are based on appraised values of underlying collateral adjusted for selling costs and for management's assumptions of fair value given current market conditions and portions of loans not guaranteed by the U.S. Government. The Bank recognized losses of \$78,000 and gains of \$49,000, respectively, in the three and nine months ended September 30, 2011 compared to losses of \$375,000 and \$670,000, respectively, for the three and nine months ended September 30, 2010.

The Bank does not measure any liabilities at fair value on a recurring or nonrecurring basis on the balance sheet.

*Summary of Fair Values of Financial Instruments*

The estimated fair values, and related carrying or notional amounts, of the Bank's financial instruments are set forth in the following table. Certain financial instruments and all nonfinancial instruments are exempt from disclosure requirements. Accordingly, the aggregate fair value amounts presented herein may not necessarily represent the underlying fair value of the Bank.

(In thousands)	September 30, 2011		December 31, 2010	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
<b>Financial assets:</b>				
Cash and cash equivalents	\$ 13,192	\$ 13,192	\$ 8,725	\$ 8,725
Interest-bearing deposits in banks	429	429	79	79
Securities available for sale	42,576	42,576	35,349	35,349
Federal Reserve Bank stock, at cost	780	780	762	762
Federal Home Loan Bank stock, at cost	2,057	2,057	2,057	2,057
Loans held for sale	-	-	386	386
Loans, net	218,277	213,424	220,342	217,416
Accrued interest receivable	1,019	1,019	1,100	1,100
<b>Financial liabilities:</b>				
Deposits	222,544	221,027	213,794	211,266
Secured borrowings	1,098	1,098	577	577
Securities sold under agreements to repurchase	3,987	3,987	3,392	3,392
Federal Home Loan Bank advances	29,450	31,178	30,450	30,762
Other borrowings	176	176	-	-
Accrued interest payable	288	288	293	293

## (9) Income Taxes

The Bank recognized a tax benefit in the amount of \$700,000 for the nine months ended September 30, 2011. Prior to March 31, 2011, the Bank had a full valuation reserve of \$5.2 million against the net deferred tax asset which related to prior years' federal and state operating losses as well as other timing differences. In the first quarter of 2011, management determined that based on recent earnings history and near-term earnings projections, it was more likely than not that a portion of the deferred tax asset would be realized and that it was appropriate to decrease the valuation reserve against the deferred tax asset by \$700,000. At September 30, 2011, management continues to believe it is more likely than not that this portion of the deferred tax asset will be realized.

## (10) Subsequent Event

On October 25, 2011, the Bank entered into an agreement and plan of merger with Berkshire Hills Bancorp, Inc. ("BHLB") and Berkshire Bank, BHLB's wholly owned subsidiary, pursuant to which CBT will merge into Berkshire Bank, with Berkshire Bank being the surviving bank.

Subject to the terms and conditions of the agreement and plan of merger, upon consummation of the merger, each outstanding share of common stock of CBT will be converted into the right to receive, at the election of the holder of such share of CBT common stock, (i) cash consideration of \$8.25 or (ii) stock consideration equal to 0.3810 shares of BHLB common stock, subject to the payment of cash in lieu of fractional shares and customary proration and allocation procedures, if necessary, to assure that 70% of the outstanding shares of CBT common stock are exchanged for BHLB common stock and 30% of the outstanding shares of CBT common stock are exchanged for cash. In addition, each outstanding option and warrant to acquire shares of CBT common stock, other than the warrant issued to the United States Department of the Treasury (the "Treasury"), will be terminated and converted to the right to receive cash equal to the product of (i) the greater of (a) \$1.00 or (b) the value of the merger consideration on the day prior to closing in excess of the exercise price multiplied by (ii) the number of shares underlying such outstanding option or warrant.

The agreement and plan of merger also provides that, prior to the consummation of the merger, BHLB will fund the purchase from the Treasury of each share of Fixed Rate Non-Cumulative Perpetual Preferred Stock, Series A, of CBT (the "TARP Preferred Stock") issued and outstanding on that date. In addition, BHLB may, but is not required to, purchase

the outstanding warrant issued to the Treasury (the “TARP Warrant”) to purchase CBT common stock. If BHLB does not purchase the TARP Warrant, such warrant will be converted at the effective time of the merger into a warrant to purchase BHLB common stock, subject to appropriate adjustments in accordance with its terms.

The agreement and plan of merger has been unanimously approved by the Board of Directors of both Berkshire and CBT. Consummation of the merger is subject to the approval of CBT’s shareholders, as well as state and federal bank regulatory agencies. The merger is expected to be completed early in the second quarter of 2012.

## **(11) Recent Accounting Pronouncements**

*Receivables, Topic 310:* In July 2010, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2010-20, Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses. The objective of this update is for an entity to provide disclosures that facilitate financial statement users’ evaluation of (1) the nature of credit risk inherent in the entity’s portfolio of financing receivables, (2) how that risk is analyzed and assessed in arriving at the allowance for credit losses, and (3) the changes and reasons for those changes in the allowance for credit losses. The disclosures as of the end of a reporting period were effective for interim and annual reporting periods ending on or after December 15, 2010 and the disclosures about activity that occurs during a reporting period are effective for interim and annual reporting periods beginning on or after December 15, 2010. The Bank incorporated the end of reporting period disclosures in the December 31, 2010 financial statements. The disclosures about activity are incorporated into the September 30, 2011 financial statements and have significantly increased the Bank’s loan disclosures.

*Receivables, Topic 310:* In April 2011, the FASB issued ASU No. 2011-02, Receivables (Topic 310), A Creditor’s Determination of Whether a Restructuring Is a Troubled Debt Restructuring. This update provides additional guidance and clarification to help creditors in determining whether a creditor has granted a concession and whether a debtor is experiencing financial difficulties for purposes of determining whether a restructuring constitutes a troubled debt restructuring (“TDR”). This update is effective for the first interim or annual period beginning on or after June 15, 2011, with retrospective application to the beginning of the annual period of adoption. The measurement of impairment should be applied prospectively in the period of adoption for loans that are newly identified as TDRs upon adoption of this update. In addition, the TDR disclosures required by ASU 2010-20, should be provided beginning in the period of adoption of this update. The Bank adopted this update on July 1, 2011 and did not have a material impact on its financial statements.

*Reconsideration of Effective Control for Repurchase Agreements:* In April 2011, the FASB issued ASU No. 2011-03, Transfers and Servicing (Topic 860), Reconsideration of Effective Control for Repurchase Agreements. This update provides additional guidance which affects all entities that enter into agreements to transfer financial assets that both entitle and obligate the transferor to repurchase or redeem financial assets before their maturity. The amendment removes from the assessment of effective control (1) the criterion requiring the transferor to have the ability to repurchase or redeem financial assets on substantially the agreed terms, even in the event of default by the transferee, and (2) the collateral maintenance implementation guidance relate to that criterion. The amendment is effective for the first interim or annual period beginning on or after December 15, 2011 and should be applied prospectively to transactions or modifications of existing transactions that occur on or after the effective date. This amendment is not expected to have a significant impact on the Bank’s financial statements.

*Comprehensive Income, Topic 220:* In June 2011, the FASB issued ASU 2011-05, Comprehensive Income (Topic 220), Presentation of Comprehensive Income. This ASU amends the disclosure requirements for the presentation of comprehensive income. The amended guidance eliminates the option to present components of other comprehensive income (OCI) as part of the statement of changes in stockholder’s equity. Under the amended guidance, all changes in OCI are to be presented either in a single continuous statement of comprehensive income or in two separate but consecutive financial statements. The changes are effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. Early application is permitted. There will be no impact to the Bank’s consolidated financial results as the amendments relate only to changes in financial statement presentation.

## **Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations.**

The following discussion and analysis is designed to assist you in better understanding the financial condition, results of operations, liquidity and capital resources of CBT, as well as any significant changes and trends related thereto. This discussion should be read in conjunction with the accompanying unaudited financial statements and the notes appearing in Item 1 of this Form 10-Q and the audited financial statements and accompanying notes found on pages 49 through 81 of CBT’s Annual Report on Form 10-K for the year ended December 31, 2010, filed with the Board of Governors of the Federal Reserve System on March 31, 2011.

### **General**

CBT provides a broad range of banking services to business enterprises and business sponsors as well as individual consumers in its market areas from its eight banking centers and through its website, [www.thecbt.com](http://www.thecbt.com). CBT is a full service commercial bank providing a comprehensive set of loans and deposit services to local businesses, business owners, professionals, and other individuals. CBT actively seeks to finance the credit needs of local businesses and actively markets deposit and loan products to businesses and individuals. CBT also offers certain investment management products to its customers. An important dimension of CBT’s strategy is to provide customers with access to well-trained and experienced bank personnel, including the senior management team.

### **Forward-Looking Statements Safe-harbor Statement**

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 relating to, without limitation, the Bank’s future economic performance, plans and objectives for future operations, and projections of revenues and other financial items that are based on Management’s beliefs, as well as assumptions made by, and information currently available to, Management. The words “may,” “will,” “anticipate,” “should,” “would,” “believe,” “contemplate,” “could,” “project,” “predict,” “expect,” “estimate,” “continue,” and “intend,” as well as other similar words and expressions of the future, are intended to identify forward-looking statements.

These forward-looking statements generally relate to the Bank’s plans, objectives and expectations for future events and include statements about the Bank’s expectations, beliefs, plans, objectives, intentions, assumptions and other statements that are not historical facts. These statements are based on Management’s opinions and estimates as of the date they are made. Although the Bank believes that the expectations reflected in these forward-looking statements are reasonable, such forward-looking statements are subject to known and unknown risks and uncertainties that may be beyond the Bank’s control, which could cause actual results, performance, and achievements to differ materially from results, performance and achievements projected, expected, expressed or implied by the forward-looking statements.

Examples of events that could cause actual results to differ materially from historical results or those anticipated, expressed or implied include, without limitation, changes in overall economy and the interest rate environment; the Bank’s ability to manage growth; the loss of significant borrowers and depositors; the ability of customers to repay their obligations; changes in loan delinquency rates or in the Bank’s levels of nonperforming asset; the adequacy of the allowance for loan losses; changes in returns on the Bank’s investment portfolio; competition; changes in deposit flows, loan demand, or real estate values; changes in economic climate in market areas in which the Bank operates; the departure of key personnel; legislation or regulatory changes; significant changes in accounting, tax, regulatory practices and requirements; technological changes; theft of customer information and security breaches; and claims or litigation related to breaches of fiduciary responsibility to the Bank’s customers. Although Management has taken certain steps to mitigate any negative effect of the aforementioned items, significant unfavorable changes could severely impact the assumptions used and have an adverse effect on profitability.

Because of the risks and uncertainties inherent in forward-looking statements, readers are cautioned not to place undue reliance on them, whether included in this Quarterly Report on Form 10-Q or made elsewhere from time to time by the Bank in its other filings with the Federal Reserve Bank. The Bank undertakes no obligation to publicly revise any forward-looking statements or cautionary factors, except as required by law.

## **Critical Accounting Policies**

In the ordinary course of business, Management makes a number of estimates and assumptions relating to reporting results of operations and financial condition in preparing its financial statements in conformity with accounting principles generally accepted in the United States of America. Actual results could differ significantly from those estimates under different assumptions and conditions. Management believes that the critical accounting policies which rely on material estimates that are susceptible to significant differences between actual results and estimates are the determination of allowance for loan losses, other-than-temporary impairment of securities, and valuation of deferred tax assets. Management believes its accounting policy and estimates relating to the provision and allowance for loan losses is very important to the portrayal of CBT's results of operations and financial condition and requires its most difficult, subjective and complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain. A description of the estimation process and methodology related to the allowance for loan losses, other-than-temporary impairment of securities and the valuation of deferred tax assets is included in CBT's financial statements and accompanying notes included in CBT's Annual Report on Form 10-K for the year ended December 31, 2010, filed with the Board of Governors of the Federal Reserve on March 31, 2011.

## **Financial Regulatory Reform Legislation**

On July 21, 2010, President Obama signed into law the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ( the "Dodd-Frank Act"). The Dodd-Frank Act has a broad impact on the financial services industry, including significant regulatory and compliance changes including, among other things, (i) enhanced resolution authority of troubled and failing banks and their holding companies; (ii) increased capital and liquidity requirements; (iii) increased regulatory examination fees; (iv) changes to assessments to be paid to the FDIC for federal deposit insurance; and (v) numerous other provisions designed to improve supervision and oversight of, and strengthening safety and soundness for, the financial services sector. Additionally, the Dodd-Frank Act establishes a new framework for systemic risk oversight within the financial system to be distributed among new and existing federal regulatory agencies, including the Financial Stability Oversight Council, the Federal Reserve, the Office of the Comptroller of the Currency, and the FDIC.

Effective July 21, 2011, the Dodd-Frank Act provided for the elimination of the federal prohibitions on paying interest on demand deposits, thus allowing businesses to have interest-bearing checking accounts. Depending on competitive responses, this significant change to existing law could have an adverse impact on our net interest margin by potentially increasing our interest expense.

The Dodd-Frank Act also changes the base for FDIC deposit insurance assessments. Assessments are now based on the average consolidated total assets less tangible equity capital of a financial institution, rather than on deposits. The Dodd-Frank Act also permanently increases the maximum amount of deposit insurance for banks, savings institutions and credit unions to \$250,000 per account, retroactive to January 1, 2008, and non-interest bearing transaction accounts have unlimited deposit insurance through December 31, 2013. The legislation also increases the required minimum reserve ratio for the Deposit Insurance Fund, from 1.15% to 1.35% of insured deposits, and directs the FDIC to offset the effects of increased assessments on depository institutions with less than \$10 billion in assets, including the Bank.

The Dodd-Frank Act requires publicly traded companies, like the Bank, to give their stockholders a non-binding vote on executive compensation and so-called "golden parachute" payments, and authorizes the Securities and Exchange Commission to promulgate rules that would allow stockholders to nominate their own candidates using a company's proxy materials. It also provides that the listing standards of the national securities exchanges shall require listed companies to implement and disclose "clawback" policies mandating the recovery of incentive compensation paid to executive officers in connection with accounting restatements. The legislation also directs the Federal Reserve Board to promulgate rules prohibiting excessive compensation paid to bank holding company executives, regardless of whether the company is publicly traded or not.

The Dodd-Frank Act creates a new Consumer Financial Protection Bureau with broad powers to supervise and enforce consumer protection laws. The Consumer Financial Protection Bureau has broad rule-making authority for a wide range of consumer protection laws that apply to all banks and savings institutions, including the authority to prohibit "unfair, deceptive or abusive" acts and practices. The Dodd-Frank Act also weakens the federal preemption rules that have been applicable for national banks and federal savings associations, and gives state attorneys general the ability to enforce

federal consumer protection laws. The Dodd-Frank Act requires minimum leverage (Tier 1) and risk based capital requirements for bank and savings and loan holding companies that are no less than those applicable to banks.

It is difficult to predict at this time what specific impact the Dodd-Frank Act and the yet to be written implementing rules and regulations will have on community banks. However, it is expected that at a minimum they will increase our operating and compliance costs and could increase our interest expense.

### **Comparison of Financial Condition at September 30, 2011 and December 31, 2010**

Total assets were \$284.2 million at September 30, 2011, an increase of \$10.1 million or 3.6%, compared to \$274.2 million at December 31, 2010. Total loans decreased by \$2.3 million to \$221.4 million at September 30, 2011 compared to \$223.7 million at December 31, 2010. The Bank originated loans totaling \$26.4 million during the nine months ended September 30, 2011 and had repayments totaling \$29.1 million. The securities portfolio totaled \$42.6 million at September 30, 2011 compared to \$35.3 million at December 31, 2010. The increase in the securities portfolio was due to purchases of eleven (11) government sponsored and government guaranteed residential mortgage-backed securities and nine (9) government guaranteed commercial-mortgage backed securities which was offset by the sale of eighteen (18) bonds, along with calls made on thirteen (13) other bonds prior to their maturities and the continuous prepayments of mortgage-backed securities. Cash and cash equivalents totaled \$13.2 million at September 30, 2011 compared to \$8.7 million at December 31, 2010 and represented CBT's primary source of liquidity. Other assets decreased by \$1.2 million. This decrease was due to the Bank receiving \$1.0 million in January 2011 that was due from a broker for a security called in December 2010. The Bank recorded a \$700,000 deferred tax asset at September 30, 2011 as a result of a reduction in the valuation allowance. The deferred tax asset was fully reserved for as of December 31, 2010.

Total deposits increased \$8.8 million to \$222.5 million at September 30, 2011 compared to \$213.8 million at December 31, 2010. Management employed a variety of strategies to increase funds from a diverse set of depositors. Checking accounts, including both non-interest bearing and NOW accounts, increased \$18.5 million to \$69.6 million at September 30, 2011 through additional new accounts. Money market funds decreased \$2.6 million to \$70.1 million at September 30, 2011 from \$72.7 million at December 31, 2010. Certificates of deposit declined \$7.7 million to \$80.2 million at September 30, 2011 due to customer migration away from time deposits and planned runoff of brokered deposits. Long-term FHLB advances were \$29.5 million at September 30, 2011, down \$1.0 million from December 31, 2010. Secured borrowings increased \$521,000 to \$1.1 million at September 30, 2011 from \$577,000 at December 31, 2010. Other borrowings were \$176,000 at September 30, 2011 compared to none at December 31, 2010. Other borrowings represents a first lien mortgage to another financial institution for one of the Bank's other real estate owned properties.

### **Securities**

At September 30, 2011, CBT's securities portfolio, all of which are classified as available-for-sale, amounted to \$42.6 million, or 15.0% of total assets. The following table sets forth information regarding the amortized cost and fair values of CBT's securities as of the dates indicated.

(In thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
<u>September 30, 2011</u>				
Government-sponsored enterprises	\$ 6,518	\$ 10	\$ (1)	\$ 6,527
U.S. Government guaranteed residential mortgage-backed securities	20,784	158	(162)	20,780
Government-sponsored residential mortgage-backed securities	12,394	158	(79)	12,473
U.S. Government guaranteed commercial mortgage-backed securities	1,802	123	-	1,925
Corporate bonds	999	-	(128)	871
	<u>\$ 42,497</u>	<u>\$ 449</u>	<u>\$ (370)</u>	<u>\$ 42,576</u>
<u>December 31, 2010</u>				
Government-sponsored enterprises	\$ 6,540	\$ -	\$ (196)	\$ 6,344
U.S. Government guaranteed residential mortgage-backed securities	5,935	195	(2)	6,128
Government-sponsored residential mortgage-backed securities	12,803	297	(37)	13,063
U.S. Government guaranteed commercial mortgage-backed securities	8,958	70	(40)	8,988
Corporate bonds	999	-	(173)	826
	<u>\$ 35,235</u>	<u>\$ 562</u>	<u>\$ (448)</u>	<u>\$ 35,349</u>

Securities available for sale experienced a net increase of \$7.2 million. Purchases of securities available for sale for the nine months ended September 30, 2011 totaled \$38.1 million and consisted of twenty (20) government-guaranteed residential and commercial mortgage-backed securities. For the nine months ended September 30, 2011, proceeds from sales of available for sale securities totaled \$15.6 million and from matured and called securities amounted to \$13.4 million. Principal payments totaled \$2.9 million for the nine months ended September 30, 2011. The portfolio included a net unrealized gain of \$79,000 as of September 30, 2011, a decrease of \$35,000 compared to December 31, 2010. The Bank recognized a net gain of \$448,000 on the sale of securities for the nine months ended September 30, 2011.

## Loans

CBT is a traditional commercial bank with 83.4% of its loan portfolio advanced to commercial and commercial real estate (CRE) borrowers. Because loans generally produce higher yields than securities and other interest-earning assets, it is CBT's strategy to use deposit balances to fund loans within its market area as soon as practicable. At September 30, 2011, CBT's net loan portfolio totaled \$218.3 million, or 76.9% of total assets, compared to \$220.3 million or 80.3% at December 31, 2010. There were no significant changes in the composition of the loan portfolio at September 30, 2011 compared to December 31, 2010. The following table sets forth the composition of CBT's loan portfolio in dollar amounts at the respective dates indicated.

(In thousands)	<u>September 30, 2011</u>	<u>December 31, 2010</u>
Commercial real estate:		
Owner occupied	\$ 63,721	\$ 66,020
Non-owner occupied	57,293	50,122
Residential real estate:		
Residential 1-4 family	11,265	9,726
Second mortgages	473	478
Equity lines of credit	8,084	8,480
Construction	<u>10,814</u>	<u>13,766</u>
Total mortgage loans on real estate	151,650	148,592
Commercial loans	63,171	69,110
Consumer loans	<u>6,196</u>	<u>5,627</u>
Total loans	221,017	223,329
Allowance for loan losses	(3,099)	(3,381)
Net deferred loan costs	<u>359</u>	<u>394</u>
Loans, net	<u>\$ 218,277</u>	<u>\$ 220,342</u>

Management evaluated the loan portfolio and identified 34 loans totaling \$16.5 million which were considered impaired as of September 30, 2011 compared to 31 loans totaling \$14.9 million as of December 31, 2010. Nonaccrual loans of \$12.9 million and \$8.8 million at September 30, 2011 and December 31, 2010, respectively, are impaired loans.

Fourteen loans totaling \$8.3 million were placed on nonaccrual basis during the nine months ended September 30, 2011. Three nonaccrual commercial loans totaling \$128,000 were charged-off as they were deemed uncollectible. Nine nonaccrual commercial loans had partial charge-offs in the amount of \$794,000. A residential mortgage loan had a partial charge-off of \$18,000 and seven consumer loans totaling \$10,000 were also charged off in the nine months ended September 30, 2011. Nonaccrual loans represented 5.8% of the gross loan portfolio at September 30, 2011 compared to 3.9% at December 31, 2010.

In continuing efforts to protect against loan losses, the Bank strives to acquire personal guarantees from borrowers, and when available, guarantees from government agencies to protect against loan losses. In addition to the valuation allowance set aside for impaired loans detailed in note 6 to the accompanying financial statements, the Bank has government guarantees from the Small Business Association (“SBA”) totaling \$518,000 and the United States Department of Agriculture (“USDA”) totaling \$2.1 million as of September 30, 2011.

Net loan charge-offs totaled \$944,000 for the nine months ended September 30, 2011 compared to \$351,000 for the same period in the prior year. The percentage of the allowance for loan losses to total loans was 1.40% at September 30, 2011 compared to 1.51% at December 31, 2010 and 1.48% at September 30, 2010.

## Deposits

Deposits from our primary market have provided a relatively stable funding source for CBT’s loan portfolio and other earning assets. In addition, CBT is a well-capitalized institution and can accept brokered deposits without limitation. CBT offers a full range of interest-bearing and noninterest-bearing accounts with a range of maturity date options. The primary sources of deposits are local businesses, including owners and employees of businesses and consumers of the North-Central Connecticut market area. The following table sets forth the composition of CBT’s deposits in dollar amounts and as a percentage of total deposits at the dates indicated.

(In thousands)	September 30, 2011		December 31, 2010	
	Balance	Percent of Total	Balance	Percent of Total
Noninterest-bearing	\$ 47,907	21.5 %	\$ 35,972	16.8 %
NOW deposits	21,740	9.8	15,140	7.1
Money market deposits	70,073	31.5	72,721	34.0
Savings deposits	2,632	1.2	2,042	1.0
	<u>142,352</u>		<u>125,875</u>	
Certificates of deposit less than \$100,000	28,804	12.9	30,773	14.4
Certificates of deposit greater than \$100,000	51,388	23.1	57,146	26.7
	<u>\$ 222,544</u>	<u>100.0 %</u>	<u>\$ 213,794</u>	<u>100.0 %</u>

Total deposits increased by \$8.8 million to \$222.5 million at September 30, 2011 from \$213.8 million at December 31, 2010. Noninterest-bearing checking accounts totaled \$47.9 million at September 30, 2011, fluctuating within normal deposit ranges. NOW accounts increased \$6.6 million to \$21.7 million at September 30, 2011 primarily due to core growth of new deposit accounts. Tiered money market deposit accounts decreased by \$2.6 million to \$70.1 million at September 30, 2011. Certificates of deposits declined \$7.7 million to \$80.2 million at September 30, 2011 with the planned redemption of \$8 million in brokered certificates. Brokered deposits, including brokered money market deposit accounts, totaled \$27.8 million and \$44.4 million, respectively, at September 30, 2011 and December 31, 2010.

### Comparison of Operating Results for the Three Months Ended September 30, 2011 and 2010

#### General

CBT reported net income of \$165,000 for the three months ended September 30, 2011 compared to net loss of \$135,000 for the same period in the prior year. For both the three months ended September 30, 2011 and 2010, the Bank accounted for dividends and accretion on preferred stock totaling \$97,000. The Bank had a net gain on sale of securities available for sale in the amount of \$310,000 during the three months ended September 30, 2011 compared to none for the three months ended September 30, 2010. Net income available to common stockholders, after dividend and accretion on preferred stock, was \$68,000 for the three months ended September 30, 2011 compared to a net loss of \$232,000 for the same period in the prior year. Net interest income was \$2.5 million for the three months ended September 30, 2011 compared to \$2.6 million for the three months ended September 30, 2010. The net interest margin was 3.59% for the three months ended September 30, 2011 and 3.89% for the three months ended September 30, 2010. An increase in average interest-earning assets to \$276.6 million for the quarter ended September 30, 2011 from \$263.7 million for the quarter ended September 30, 2010 was due to increases in average loans of \$10.5 million and investment in securities of \$8.1 million, which were partially offset by a decrease in other average interest earning assets of \$5.7 million. Average loans totaled \$224.5 million during the quarter ended September 30, 2011 compared to \$214.0 million for the same period in the prior year. Interest income on earning assets declined \$182,000 to \$3.2 million for the three months ended September 30, 2011 compared to \$3.4 million for the same period a year earlier due to lower yielding products. Interest expense was \$732,000 for the three months ended September 30, 2011, a decrease of \$104,000 from the comparable period a year earlier. The provision for loan losses decreased \$189,000 to \$398,000 for the quarter ended September 30, 2011 from \$587,000 for the same period a year earlier. The provision for the three months ended September 30, 2011 included reserves on specifically identified impaired loans, as well as provisions in response to deterioration in loan characteristics primarily resulting from loans migrating to delinquent or nonperforming status. The decrease in the provision for loan losses is attributable to the decrease in the valuation allowance on impaired loans, offset by an increase in the general allowance for loan losses.

## Net Interest Income

Net interest income is the difference between income on interest-earning assets and expense on interest-bearing liabilities. The following table depicts the condensed averages of the major balance sheet categories that generate interest income or interest expense and the resulting asset yields or cost of funds for the three months ended September 30, 2011 and 2010. The difference between asset yields and the cost of funds equals the net interest spread. The difference between interest income and interest expense equals net interest income, which is divided into the average balance of interest-earning assets to arrive at the net interest margin. The average balances of loans include nonaccrual loans, loans held for sale, and deferred fees and costs. Interest on nonaccrual loans has been included only to the extent reflected in the Statement of Operations. The total dollar amount of interest income from assets and the subsequent yields are calculated on a taxable equivalent basis.

	Three Months Ended September 30,					
	2011			2010		
	Average Balance	Interest Income/ Expense	Average Yield Rate	Average Balance	Interest Income/ Expense	Average Yield Rate
	(Dollars in thousands)					
Interest-earning assets:						
Loans	\$ 224,481	\$ 2,974	5.26 %	\$ 213,959	\$ 3,159	5.86 %
Securities	38,186	239	2.48	30,092	237	3.12
Other	13,921	24	0.68	19,612	23	0.47
Total interest-earning assets	276,588	3,237	4.64	263,663	3,419	5.14
Allowance for loan losses	(3,382)			(2,942)		
Cash and due from banks	5,026			4,678		
Other assets	7,591			5,316		
Total assets	<u>\$ 285,823</u>			<u>\$ 270,715</u>		
Interest-bearing liabilities:						
Savings, NOW and money market deposits	\$ 98,381	187	0.75	\$ 82,734	196	0.94
Time deposits	78,615	274	1.38	95,593	363	1.51
Borrowed funds	33,910	271	3.17	33,504	277	3.28
Total interest-bearing liabilities	210,906	732	1.38	211,831	836	1.57
Demand deposits	47,212			32,378		
Total deposits and borrowed funds	258,118			244,209		
Other liabilities	1,440			1,092		
Stockholders' equity	26,265			25,414		
Total liabilities and stockholders' equity	<u>\$ 285,823</u>			<u>\$ 270,715</u>		
Net interest income		<u>\$ 2,505</u>			<u>\$ 2,583</u>	
Interest rate spread			<u>3.26 %</u>			<u>3.57 %</u>
Net interest margin			<u>3.59 %</u>			<u>3.89 %</u>
Interest-earning assets to interest-bearing liabilities			<u>131.14 %</u>			<u>124.47 %</u>

### Rate/Volume Analysis

The following table presents the extent to which changes in interest rates and changes in the volume of interest-earning assets and interest-bearing liabilities have affected CBT's interest income and interest expense during the periods indicated. Information is provided in each category with respect to: (i) changes attributable to changes in volume (changes in volume multiplied by prior rate); (ii) changes attributable to changes in rate (changes in rate multiplied by prior volume); and (iii) the net change. The changes attributable to the combined impact of volume and rate have been allocated proportionately to the changes due to volume and the changes due to rate.

	Three Months Ended September 30, 2011 compared to 2010		
	Increase (Decrease)		
	Due to		
	Volume	Rate	Net
	(In thousands)		
<b>Interest-earning assets:</b>			
Loans	\$ 150	\$ (335)	\$ (185)
Securities	56	(54)	2
Other	(8)	9	1
Total interest-earning assets	<u>198</u>	<u>(380)</u>	<u>(182)</u>
<b>Interest-bearing liabilities:</b>			
Savings, NOW and money market deposits	34	(43)	(9)
Time deposits	(61)	(28)	(89)
Borrowed funds	3	(9)	(6)
Total interest-bearing liabilities	<u>(24)</u>	<u>(80)</u>	<u>(104)</u>
<b>Change in net interest income</b>	<u>\$ 222</u>	<u>\$ (300)</u>	<u>\$ (78)</u>

Total average interest-earning assets increased \$12.9 million to \$276.6 million for the quarter ended September 30, 2011 compared to the same period in the preceding year. Average loan balances increased by \$10.5 million to \$224.5 million for the quarter ended September 30, 2011 as CBT continued to concentrate on commercial lending, with both new originations and advances on existing lines of credit. Average investments in securities, primarily in government-guaranteed or sponsored securities, increased \$8.1 million to \$38.2 million for the quarter ended September 30, 2011. Other average asset balances, mainly liquid short-term interest bearing funds, decreased by \$5.7 million to \$13.9 million for the quarter ended September 30, 2011. Overall, the yield declined 50 basis points year-over-year as an increase of \$198,000 related to volume changes in average interest-earning assets was more than offset by a decrease of \$380,000 related to rate changes in average interest-earning assets.

Average interest-bearing liabilities declined by \$925,000 to \$210.9 million for the quarter ended September 30, 2011. The decrease in average time deposits of \$17.0 million to \$78.6 million for the quarter ended September 30, 2011 more than offset increases in both average savings, NOW and money market deposits of \$15.6 million to \$98.4 million and borrowed funds of \$406,000 to \$33.9 million for the quarter ended September 30, 2011. The average rate paid on these liabilities decreased to 1.38% for the three month period ended September 30, 2011 from 1.57% for the three month period ended September 30, 2010. The effect of these changes resulted in a decrease of \$24,000 related to volume changes and a decrease of \$80,000 related to rate changes. The net interest margin declined to 3.59% for the three months ended September 30, 2011 from 3.89% for the comparable period in 2010.

### ***Provision for Loan Losses***

The provision for loan losses is estimated based upon quantitative factors affecting both the growth in outstanding loans and composition of the loan portfolio. Management's analysis of the adequacy of the loan loss reserve also includes a regular review of qualitative factors including, but not limited to, individual loans, industry trends and concentrations, and national and local economic conditions. Management's evaluation of the current level of outstanding loans and the risk comprised of the qualitative factors within the portfolio resulted in provisions for losses in the amount of \$398,000 for the three months ended September 30, 2011 compared to \$587,000 for the three months ended September 30, 2010. The provision for the three months ended September 30, 2011 included reserves on specifically identified impaired loans and loan charge-offs, as well as provisions in response to deterioration in loan characteristics resulting primarily from loans migrating to delinquent or nonperforming status. Net loan charge-offs amounted to \$703,000 during the three months ended September 30, 2011 compared to \$266,000 in the corresponding period of the prior year.

### ***Non-interest Income***

Total non-interest income for the quarter ended September 30, 2011 was \$552,000, an increase of \$366,000 from the same period in the preceding year. The Bank reported a net gain on the sale of available-for-sale securities of \$310,000 for the three months ended September 30, 2011 compared to none for the same period in the preceding year. Customer service fees totaled \$130,000 for the quarter ended September 30, 2011 compared to \$103,000 for the corresponding period a year earlier due to increased utilization of fee services. Brokerage commissions totaled \$88,000 compared to \$63,000 for the same period in 2010. The Bank recognized \$24,000 in gains on the sale of loans in the secondary market for each of the three months ended September 30, 2011 and 2010.

### ***Non-interest Expenses***

Non-interest expenses increased \$177,000, or 7.6%, to \$2.5 million for the three months ended September 30, 2011 compared to the same period in 2010. Compensation costs rose \$34,000 to \$1.2 million for the quarter ended September 30, 2011 due to staff additions and higher employee benefit costs. Professional services rose \$97,000 to \$262,000 for the three months ended September 30, 2011 due to rising costs and the increased use of legal, accounting and other consulting services due primarily to merger-related activities. Other general and administrative costs grew \$38,000 to \$318,000 for the quarter ended September 30, 2011 due to costs associated with the collection of problem loans and the maintenance of other real estate owned, as well as general increases in costs for goods and services.

## **Comparison of Operating Results for the Nine Months Ended September 30, 2011 and 2010**

### ***General***

CBT reported net income before income tax benefit of \$387,000 for the nine months ended September 30, 2011, compared to net income of \$372,000 for the same period in the prior year. For the nine months ended September 30, 2011 and 2010, the Bank accounted for dividends and accretion on preferred stock totaling \$291,000. The Bank recognized a tax benefit in the amount of \$700,000 in the nine months ended September 30, 2011 due to the reduction in the valuation allowance for deferred taxes. Net income available to common stockholders, after dividend and accretion on preferred stock and the tax benefit, was \$796,000 and \$81,000, respectively, for the nine months ended September 30, 2011 and 2010. Net interest income had a minimal decrease of \$44,000 to \$7.5 million for the nine months ended September 30, 2011 resulting from decreases of \$398,000 and \$354,000, respectively, on interest income and interest expense compared to the same period in the prior year. Noninterest expense had an increase of \$756,000 to \$7.6 million for the nine months ended September 30, 2011, compared to \$6.8 million for the same period in the prior year. Noninterest income had an increase of \$581,000 to \$1.1 million for the nine months ended September 30, 2011, compared to \$544,000 for the nine months ended September 30, 2010. The provision for loan losses was \$662,000 for the nine months ended September 30, 2011, compared to \$896,000 for the comparable period a year earlier. The provision for the nine months ended September 30, 2011 included reserves on specifically identified impaired loans, as well as provisions in response to deterioration in loan characteristics primarily resulting from loans migrating to delinquent or nonperforming status. The decrease in the provision for loan losses is attributable to the decrease in the valuation allowance on impaired loans offset by an increase in the general allowance for loan losses.

## Net Interest Income

Net interest income is the difference between income on interest-earning assets and expense on interest-bearing liabilities. The following table depicts the condensed averages of the major balance sheet categories that generate interest income or interest expense and the resulting asset yields or cost of funds for the nine months ended September 30, 2011 and 2010. The difference between asset yields and the cost of funds equals the net interest spread. The difference between interest income and interest expense equals net interest income, which is divided into the average balance of interest-earning assets to arrive at the net interest margin. The average balances of loans includes nonaccrual loans, loans held for sale, and deferred fees and costs. Interest on nonaccrual loans has been included only to the extent reflected in the Statement of Income. The total dollar amount of interest income from assets and the subsequent yields are calculated on a taxable equivalent basis.

	Nine Months Ended September 30,					
	2011			2010		
	Average Balance	Interest Income/Expense	Average Yield Rate	Average Balance	Interest Income/Expense	Average Yield Rate
(Dollars in thousands)						
Interest-earning assets:						
Loans	\$ 222,839	\$ 8,926	5.36 %	\$ 208,557	\$ 9,269	5.94 %
Securities	34,404	683	2.65	28,679	728	3.39
Other	10,627	60	0.75	23,026	70	0.41
Total interest-earning assets	267,870	9,669	4.83	260,262	10,067	5.17
Allowance for loan losses	(3,381)			(2,817)		
Cash and due from banks	5,047			4,507		
Other assets	7,713			5,177		
Total assets	<u>\$ 277,249</u>			<u>\$ 267,129</u>		
Interest-bearing liabilities:						
Savings, NOW and money market deposits	\$ 94,855	\$ 576	0.81	\$ 75,806	\$ 591	1.04
Time deposits	79,969	816	1.36	100,548	1,140	1.52
Borrowed funds	33,642	801	3.18	32,967	816	3.31
Total interest-bearing liabilities	208,466	2,193	1.41	209,321	2,547	1.63
Demand deposits	41,577			31,441		
Total deposits and borrowed funds	250,043			240,762		
Other liabilities	1,454			1,374		
Stockholders' equity	25,752			24,993		
Total liabilities and stockholders' equity	<u>\$ 277,249</u>			<u>\$ 267,129</u>		
Net interest income		<u>\$ 7,476</u>			<u>\$ 7,520</u>	
Interest rate spread			<u>3.42 %</u>			<u>3.54 %</u>
Net interest margin			<u>3.73 %</u>			<u>3.86 %</u>
Interest-earning assets to interest-bearing liabilities			<u>128.50%</u>			<u>124.34%</u>

### **Rate/Volume Analysis**

The following table presents the extent to which changes in interest rates and changes in the volume of interest-earning assets and interest-bearing liabilities have affected CBT's interest income and interest expense during the periods indicated. Information is provided in each category with respect to: (i) changes attributable to changes in volume (changes in volume multiplied by prior rate); (ii) changes attributable to changes in rate (changes in rate multiplied by prior volume); and (iii) the net change. The changes attributable to the combined impact of volume and rate have been allocated proportionately to the changes due to volume and the changes due to rate.

	Nine Months Ended September 30, 2011 compared to 2010		
	Increase (Decrease)		
	Due to		
	Volume	Rate	Net
	(In thousands)		
<b>Interest-earning assets:</b>			
Loans	\$ 609	\$ (952)	\$ (343)
Securities	80	(125)	(45)
Other	(35)	25	(10)
Total interest-earning assets	<u>654</u>	<u>(1,052)</u>	<u>(398)</u>
<b>Interest-bearing liabilities:</b>			
Savings, NOW and money market deposits	131	(146)	(15)
Time deposits	(218)	(106)	(324)
Borrowed funds	17	(32)	(15)
Total interest-bearing liabilities	<u>(70)</u>	<u>(284)</u>	<u>(354)</u>
<b>Change in net interest income</b>	<u><u>\$ 724</u></u>	<u><u>\$ (768)</u></u>	<u><u>\$ (44)</u></u>

Total average interest-earning assets increased \$7.6 million to \$267.9 million for the nine months ended September 30, 2011 compared to the same period in the preceding year. Average loan balances increased \$14.3 million as CBT continued to concentrate on commercial lending, including new originations of commercial loans and advances on existing lines of credit. Average investments in government-guaranteed securities increased \$5.7 million resulting from purchases of \$38.1 million less sales and maturities and calls of \$15.6 million and \$13.4 million and principal repayments and amortization of \$2.9 million. Overall, the yield in interest-earning assets declined 34 basis points year-over-year with an increase of \$654,000 related to volume changes in average interest-earning assets and a decrease of \$1.1 million related to rate changes in average interest-earning assets.

Average interest-bearing liabilities decreased slightly by \$855,000 to \$208.5 million for the nine months ended September 30, 2011 as the decrease in time deposits of \$20.6 million to \$80.0 million was offset by increases in savings, NOW and money market deposits of \$19.0 million to \$94.9 million and borrowed funds of \$675,000 to \$33.6 million. The average rate paid on liabilities dropped to 1.41% for the nine months ended September 30, 2011 from 1.63% for the comparable period in 2010. The effect of these changes resulted in a decrease of \$70,000 related to volume changes and a decrease of \$284,000 related to rate changes. The net interest margin declined to 3.73% for the nine months ended September 30, 2011 from 3.86% for the comparable period in 2010.

### ***Provision for Loan Losses***

The provision for loan losses is estimated based upon quantitative factors affecting both the growth in outstanding loans and composition of the loan portfolio. Management's analysis of the adequacy of the loan loss reserve also includes a regular review of qualitative factors including but not limited to individual loans, industry trends and concentrations, and national and local economic conditions. Management's evaluation of the current level of outstanding loans and the risk comprised of the qualitative factors within the portfolio resulted in provisions for losses in the amount of \$662,000 for the nine months ended September 30, 2011 compared to \$896,000 for the nine months ended September 30, 2010. The provision for the nine months ended September 30, 2011 included reserves on specifically identified impaired loans and loan charge-offs, as well as provisions in response to deterioration in loan characteristics resulting primarily from loans migrating to delinquent or nonperforming status. Net loan charge-offs amounted to \$944,000 of loans during the nine months ended September 30, 2011 compared to \$351,000 in the corresponding period of the prior year.

### ***Non-interest Income***

Total non-interest income for the nine months ended September 30, 2011 was \$1.1 million, an increase of \$581,000 from the same period in the preceding year. The Bank reported a net gain on the sale of available-for-sale securities of \$448,000 for the nine months ended September 30, 2011 compared to \$60,000 for the same period in the preceding year. Customer service fees totaled \$360,000 for the nine months ended September 30, 2011 compared to \$249,000 for the corresponding period a year earlier due to increased utilization of fee services. Brokerage commissions totaled \$251,000 compared to \$206,000 for the same period in 2010. The Bank recognized \$66,000 in gains on the sale of loans in the secondary market for the nine months ended September 30, 2011 compared to \$33,000 on the sale of loans in the same period a year earlier.

### ***Non-interest Expenses***

Non-interest expenses increased \$756,000, or 11.1%, to \$7.6 million for the nine months ended September 30, 2011 compared to the same period in 2010. Compensation costs rose \$192,000 to \$3.6 million for the nine months ended September 30, 2011 due to staff additions and higher employee benefit costs. Professional services rose \$245,000 to \$742,000 for the nine months ended September 30, 2011 due to rising costs and the increased use of legal, accounting and other consulting services due primarily from merger-related activities. FDIC assessments increased \$79,000 to \$368,000 for the nine months ended September 30, 2011 primarily as a result of higher deposit balances and increased assessment rates imposed by the FDIC. Other general and administrative costs grew \$245,000 to \$1.0 million for the nine months ended September 30, 2011 due to costs associated with the collection of problem loans and the maintenance of other real estate owned, as well as general increases in costs for goods and services.

### ***Income Tax Benefit***

The Bank recognized a tax benefit in the amount of \$700,000 for the nine months ended September 30, 2011. Prior to March 31, 2011, the Bank had a valuation reserve of \$5.2 million against the entire net deferred tax asset which related to prior years' federal and state operating losses as well as other timing differences. Management determined that based on recent earnings history and near term earnings projections, it was more likely than not that a portion of the deferred tax asset would be realized and that it was appropriate to decrease the valuation reserve against the deferred tax asset as by \$700,000.

### ***Liquidity***

CBT closely monitors its liquidity position. Consistent with the requirements of prudent banking practices necessary to maintain liquidity, Management seeks to match maturities and interest rates of loans and the securities portfolio with those of deposits, although exact matching is not always possible. Our primary sources of liquidity are cash and cash equivalents and our securities portfolio. Our securities portfolio consists primarily of marketable securities of government-sponsored enterprises and mortgage-backed securities, generally with varied maturities. Additional off-balance sheet liquidity is provided by a federal funds line of credit, the authority to borrow from the Federal Home Loan Bank of Boston ("FHLB"), and the discount window at the Federal Reserve.

The primary investing activities of CBT are the origination of commercial loans and commercial mortgages. To a lesser extent, CBT invests in the origination of consumer loans, primarily home equity loans and lines of credit, and other types of loans as well as investments in mortgage-backed and government-sponsored enterprise securities. To support the growth in lending and investment activities, CBT uses deposit balances and additional funding sources as well as principal and interest payments on outstanding loans and investment securities. CBT experienced a \$8.8 million increase in total deposits to \$222.5 million for the nine month period ending September 30, 2011. Deposit flows are affected by the overall level of interest rates and products offered by CBT and its local competitors as well as other factors. CBT utilizes these cash flows to fund a large portion of its balance sheet growth.

While maturities and scheduled amortization of loans and securities are predictable sources of funds, deposit outflows and mortgage prepayments are greatly influenced by market interest rates and general economic conditions. When CBT requires funds beyond its ability to generate them internally, additional sources of funds are available through FHLB advances and a \$2.0 million federal funds borrowing line of credit from Bankers' Bank Northeast. At September 30, 2011, CBT had \$29.5 million of borrowings outstanding with the FHLB, which represented a \$1.0 million decrease from December 31, 2010, and had not drawn on the federal funds line of credit with Bankers' Bank Northeast.

The table below indicates the various types of commitments outstanding as of each of the respective dates.

(In thousands)	September 30, 2011	December 31, 2010
Unfunded commitments under commercial lines of credit	\$ 41,563	\$ 34,797
Unfunded commitments under commercial construction loans	2,778	2,534
Unfunded commitments under home equity lines of credit	6,757	6,558
Commitments to originate loans	7,906	9,996
Commercial letter of credit	962	1,054

Management anticipates that it will have sufficient funds available to meet its current loan commitments. Management believes that, although it is not possible to predict future deposit account levels, a significant portion of the Bank's deposits will remain with CBT. Management believes that CBT's short-term assets, combined with access to alternative funding sources such as the FHLB and other short-term borrowing lines, provide sufficient liquidity to cover potential fluctuations in deposit accounts and loan demand and to meet other anticipated operating cash and investment requirements.

### **Interest Rate Sensitivity Management**

Interest rate risk ("IRR") represents CBT's primary market risk exposure. Since the Bank's earnings are to a great extent dependent on its net interest income ("NII"), IRR can adversely affect the Bank's earnings. To manage interest rate risk, the Bank has an Asset/Liability Committee ("ALCO"), whose goal is to mitigate interest rate risk and to maximize net interest income under changing interest rate environments. To serve its purpose, ALCO utilizes an Asset/Liability Management ("ALM") process. ALM employs techniques to quantify, analyze, and control interest rate risk. The principal objective of ALM is to maximize NII while operating within acceptable limits established for interest rate risk and maintaining adequate levels of liquidity.

Net interest income is susceptible to IRR to the degree that interest-earning assets mature or re-price on a different basis and timing than interest-bearing liabilities. This timing difference represents a potential risk to CBT's future earnings. When interest-bearing liabilities mature or re-price more quickly than interest-earning assets in a given period, a significant increase in market rates of interest could adversely affect CBT's NII. Similarly, when interest-earning assets mature or re-price more quickly than interest-bearing liabilities, falling interest rates could result in a decrease in CBT's NII. Hence, interest rate fluctuations can put the Bank's future earnings at risk.

ALCO directs Management to produce a stable net interest margin ("NIM") in periods of interest rate fluctuations. ALCO sets a range of guidelines to ensure a balance sheet composition that enhances both long-term and short-term performance

of the Bank. By adjusting the asset/liability position, the Board and Management attempt to minimize the adverse effects of interest rate fluctuation while maximizing NIM. At times, depending on the general level of interest rates, the relationship between long-term and short-term interest rates, market conditions and competitive factors, CBT's Board of Directors and Management may establish and implement strategies that could add to the level of IRR in order to increase the Bank's NIM. Notwithstanding CBT's IRR management activities, the potential for rising or falling interest rates is an uncertainty that can have an adverse effect on net earnings.

To better mitigate IRR, Management and ALCO adopted ALM processes. Through the use of a discounted cash flow technique, ALM predicts the Bank's performance under various interest rate levels. Management makes a range of assumptions that include behavior of the Bank's interest-earning assets and interest-bearing liabilities during periods of rising and declining interest rates. It is also assumed that the interest rate movement will be parallel – both short-term and long-term rates will change by the same number of basis points. ALM allows Management to analyze the behavior of CBT's balance sheet components under various rate levels and compare it to the base case – the scenario in which interest rates are assumed to remain unchanged.

NII at-risk measures the risk of a decline in earnings due to potential short-term and long-term changes in interest rates. The following table summarizes the estimated impact on net interest income of increases of 100, 200, 300 and 400 basis points in interest rates over a twelve month period commencing September 30, 2011. Interest rates are assumed to change in parallel fashion and NII results are compared to the flat rate scenario as a base.

#### Net Interest Income At-Risk

	Base Case	Estimated Change in Net Interest Income			
	(000's)	+100 BP	+200 BP	+300 BP	+400 BP
September 30, 2011	\$ 9,536	0.74%	0.29%	-2.29%	-4.73%

#### Off-Balance Sheet Arrangements

Information relating to Off-Balance Sheet Arrangements is presented in CBT's Annual Report on Form 10-K for the year ended December 31, 2010 (see Note 10 to the Financial Statements). There have been no material changes in CBT's off-balance sheet arrangements since December 31, 2010.

## Regulatory Capital

Federal law defines specific capital categories for depository institutions. The capital categories, in declining order, are: (i) well capitalized; (ii) adequately capitalized; (iii) undercapitalized; (iv) significantly undercapitalized; and (v) critically undercapitalized. To be considered “adequately capitalized,” an institution must generally have a leverage ratio of at least 4%, a Tier 1 capital to risk-weighted assets ratio of at least 4% and total Tier 1 and Tier 2 capital to risk-weighted assets ratio of at least 8%. To be considered “well capitalized,” an institution must generally have a leverage ratio of at least 5%, a Tier 1 capital to risk-weighted assets ratio of at least 6% and total Tier 1 and Tier 2 capital to risk-weighted assets ratio of at least 10%. As of September 30, 2011, the most recent notification from the FDIC categorized CBT as “well capitalized.” To be categorized as “well capitalized,” CBT must maintain minimum total risk-based, Tier 1 risk-based and Tier 1 leverage ratios as set forth in the table below.

As indicated in the following table, the actual regulatory capital ratios of CBT at September 30, 2011 exceeded the minimum required ratios. Management believes there are no conditions that have changed CBT’s category since its most recent notification from regulators that it is “well capitalized.” CBT’s actual capital amounts and ratios as of September 30, 2011 and December 31, 2010 are presented in the table.

	Actual		Minimum Capital Requirement		Minimum To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
(Dollars in thousands)						
<u>September 30, 2011</u>						
Total capital (to risk weighted assets)	\$ 28,392	12.7 %	\$ 17,821	8.0 %	\$ 22,276	10.0 %
Tier 1 capital (to risk weighted assets)	25,603	11.5	8,910	4.0	13,366	6.0
Tier 1 capital (to average assets)	25,603	9.0	11,426	4.0	14,282	5.0
<u>December 31, 2010</u>						
Total capital (to risk weighted assets)	\$ 27,511	12.3 %	\$ 17,924	8.0 %	\$ 22,406	10.0 %
Tier 1 capital (to risk weighted assets)	24,703	11.0	8,962	4.0	13,443	6.0
Tier 1 capital (to average assets)	24,703	8.9	11,146	4.0	13,933	5.0

A reconciliation of total Bank capital to total regulatory capital is as follows:

(In thousands)	<u>September 30, 2011</u>	<u>December 31, 2010</u>
Total capital per financial statements	\$ 25,787	\$ 24,867
Accumulated net unrealized gains on available-for-sale securities	(79)	(114)
Disallowed deferred tax asset	(55)	-
Intangible assets	<u>(50)</u>	<u>(50)</u>
Total Tier 1 capital	25,603	24,703
<i>Adjustments for total capital</i>		
Allowance for loan losses includible in Tier 2 Capital	<u>2,789</u>	<u>2,808</u>
Total capital per regulatory reporting	<u><u>\$ 28,392</u></u>	<u><u>\$ 27,511</u></u>

### ***Payment of Dividends***

State and federal statutory and regulatory limitations apply to CBT's payment of dividends to stockholders. The prior approval of the DOB is required if the total of all dividends declared by a bank in any calendar year exceeds such bank's net profits, as defined, for that year combined with its retained net profits for the preceding two calendar years. The payment of dividends by CBT may also be affected by other factors, such as the requirement to maintain adequate capital above regulatory guidelines.

If, in the opinion of the FRBB, CBT was engaged in or about to engage in an unsafe or unsound practice, the FRBB could require, after notice and a hearing, CBT to cease and desist from the practice. The federal banking agencies have indicated that paying dividends that deplete a depository institution's capital base to an inadequate level would be an unsafe and unsound banking practice. Under the Federal Reserve's Regulation H, CBT must obtain prior approval of the FRBB in order to declare and pay a dividend if the total of all dividends declared during the calendar year, including the proposed dividend, exceeds the sum of the Bank's net income during the current calendar year and its retained net income for the prior two calendar years. Furthermore, Regulation H prohibits CBT from declaring or paying a dividend if the dividend would exceed the Bank's undivided profits, unless the FRBB and the holders of two-thirds of the share of each class of the Bank's outstanding stock previously approve the dividend.

CBT is required to obtain approval of the DOB, the FRBB and the holders of two-thirds of the shares of each of its common stock and preferred stock in order to pay dividends on the shares of senior preferred stock (the "Preferred Stock") that were issued to the United States Department of the Treasury ("Treasury") on December 19, 2008. In addition, under the terms and conditions of the Bank's Letter Agreement with the Treasury, CBT may not pay any dividends on its common stock without obtaining the prior consent of the Treasury until the earlier of (i) December 19, 2011 or (ii) the date the Treasury no longer owns any shares of Preferred Stock.

From March 2004 (when the Bank commenced operations) through June 30, 2009, the Bank posted net losses that resulted from anticipated start-up costs associated with developing the Bank's operating infrastructure, an initially low volume of earning assets, increases to the provisions for loan losses, and the incurrence of other noninterest expenses. These early losses are typical in a new bank. As a result, the Bank has no undivided profits or net profits (i.e. negative retained earnings) and any dividend payment would be considered a reduction of permanent capital. Accordingly, the Bank would need the approval of the holders of at least two-thirds of the shares of each of its common stock and its Preferred Stock, the FRBB and the DOB in order to declare and pay dividends on its Preferred Stock. Under previous Connecticut law, the DOB had no authority to approve a dividend unless a bank had net profits. On June 3, 2009, a bill was passed by the Connecticut legislature and signed by the Governor to permit the Connecticut Banking Commissioner to approve a dividend even absent any net profits. The effective date of this revision to Connecticut law was October 1, 2009.

At the Bank's annual meeting in May 2009, the Bank's common stockholders approved the dividend payment on its Preferred Stock with 73.8% of the shares of common stock voted in favor of the proposal. The Bank also requested and received the written consent of the Treasury as the sole holder of the Preferred Stock to pay dividends on the Preferred stock to the Treasury. In addition, on a quarterly basis, the Bank has been requesting written approval from the FRBB and the DOB to pay dividends on the Preferred Stock to the Treasury. After the Bank requested and received such written approval from the FRBB and the DOB, the Bank paid all scheduled dividends on the Preferred Stock to Treasury commencing on November 15, 2009 through the second quarter of 2011. Future quarterly dividends will be paid subject to the Bank's receipt of written approvals from the FRBB and the DOB.

The Board of Directors has declared and authorized the payment of a quarterly dividend at a rate of 5% per annum of the liquidation preference (\$1,000 per share) of the Preferred Stock on each of the outstanding 5,448 shares of Preferred Stock. The Bank has requested approval from the FRBB and the DOB to pay such quarterly dividend on November 15, 2011.

### **Item 3. Quantitative and Qualitative Disclosures About Market Risk**

Not required.

### **Item 4. Controls and Procedures**

#### **(a) Evaluation of Disclosure Controls and Procedures**

Management, including CBT's principal executive officer and principal financial officer, have evaluated the effectiveness of CBT's "disclosure controls and procedures," as such term is defined in Rule 13a-15(e) promulgated under the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Based upon their evaluation, the principal executive officer and principal financial officer concluded that, as of the end of the period covered by this report, CBT's disclosure controls and procedures were effective for the purpose of ensuring that the information required to be disclosed in the reports that CBT files or submits under the Exchange Act with the FRBB (1) is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and (2) is accumulated and communicated to Management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure.

As used herein, "disclosure controls and procedures" means controls and other procedures of CBT that are designed to ensure that information required to be disclosed by CBT in the reports that it files or submits pursuant to the Exchange Act is recorded, processed, summarized and reported within the relevant time periods. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by CBT in the reports that it files or submits under the Exchange Act is accumulated and communicated to Management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decision regarding required disclosures.

#### **(b) Changes in Internal Controls over Financial Reporting**

There have been no significant changes in CBT's internal controls over financial reporting or in other factors identified in connection with the evaluation required by Rule 13a-15 that occurred during CBT's quarter ended September 30, 2011 that have materially affected, or are reasonably likely to materially affect, CBT's internal controls over financial reporting.

## **PART II. OTHER INFORMATION**

### **Item 1. Legal Proceedings.**

See Note 10 to the financial statements. CBT is not involved in any other pending legal proceedings other than routine legal proceedings occurring in the ordinary course of business. Such routine legal proceedings, in the aggregate, are believed by Management to be immaterial to the financial condition and results of operations of CBT.

**Item 1A. Risk Factors.**

There have been no material changes from the risk factors previously disclosed in the Bank's Annual Report on Form 10-K for the year ended December 31, 2010.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.**

None.

**Item 3. Defaults Upon Senior Securities.**

None.

**Item 4. [Removed and Reserved.]**

**Item 5. Other Information.**

None

**Item 6. Exhibits.**

<u>No.</u>	<u>Description</u>
2.1	Agreement and Plan of Merger, dated as of October 25, 2011, by and between Berkshire Hills Bancorp, Inc., Berkshire Bank and The Connecticut Bank and Trust Company (incorporated by reference to Exhibit 2.1 to The Connecticut Bank and Trust Company's Form 8-K dated October 25, 2011).
3(i)	Restated and Amended Certificate of Incorporation of The Connecticut Bank and Trust Company (incorporated by reference to Exhibit 3(i) to The Connecticut Bank and Trust Company's Registration Statement on Form S-3 dated January 14, 2009)
3(ii)	Amended Bylaws of The Connecticut Bank and Trust Company (incorporated by reference to Exhibit 3.2 to The Connecticut Bank and Trust Company's Registration Statement on Form 10-SB dated April 28, 2005)
31.1	Rule 13a-14(a)/15d-14(a) Certification by Chief Executive Officer
31.2	Rule 13a-14(a)/15d-14(a) Certification by Chief Financial Officer
32.1	Section 1350 Certification by Chief Executive Officer
32.2	Section 1350 Certification by Chief Financial Officer

## **SIGNATURES**

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

### THE CONNECTICUT BANK AND TRUST COMPANY

Dated: November 14, 2011

By: /s/ David A. Lentini  
David A. Lentini  
Chairman of the Board and  
Chief Executive Officer

Dated: November 14, 2011

By: /s/ Paul Granato  
Paul Granato  
Treasurer and  
Chief Financial Officer

## EXHIBIT INDEX

No.	Description
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31.1	Rule 13a-14(a)/15d-14(a) Certification by Chief Executive Officer
31.2	Rule 13a-14(a)/15d-14(a) Certification by Chief Financial Officer
32.1	Section 1350 Certification by Chief Executive Officer
32.2	Section 1350 Certification by Chief Financial Officer

## EXHIBIT 31.1

### CERTIFICATIONS

I, David A. Lentini, Chairman of the Board and Chief Executive Officer of The Connecticut Bank and Trust Company, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of The Connecticut Bank and Trust Company;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 14, 2011

/s/ David A. Lentini  
David A. Lentini  
Chief Executive Officer

## EXHIBIT 31.2

### CERTIFICATIONS

I, Paul Granato, Treasurer and Chief Financial Officer of The Connecticut Bank and Trust Company, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of The Connecticut Bank and Trust Company;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 14, 2011

/s/ Paul Granato  
Paul Granato  
Chief Financial Officer

**EXHIBIT 32.1**

**CERTIFICATION PURSUANT TO  
18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of The Connecticut Bank and Trust Company (“CBT”) on Form 10-Q for the period ended September 30, 2011 as filed with the Federal Reserve Bank of Boston (the “Report”), I, David A. Lentini, Chief Executive Officer of CBT, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of CBT as of and for the period covered by the Report.

/s/ David A. Lentini  
David A. Lentini  
Chief Executive Officer  
November 14, 2011

**EXHIBIT 32.2**

**CERTIFICATION PURSUANT TO  
18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of The Connecticut Bank and Trust Company (“CBT”) on Form 10-Q for the period ended September 30, 2011 as filed with the Federal Reserve Bank of Boston (the “Report”), I, Paul Granato, Chief Financial Officer of CBT, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of CBT as of and for the period covered by the Report.

/s/ Paul Granato  
Paul Granato  
Chief Financial Officer  
November 14, 2011