ENTERPRISE BANCORP INC /MA/
Form 10-Q
November 09, 2011
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

x 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

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

For the transition period from to

Commission File Number: 001-33912

Enterprise Bancorp, Inc.

(Exact name of registrant as specified in its charter)

Massachusetts (State or other jurisdiction of incorporation or organization)	**04-3308902** (I.R.S. Employer Identification No.)
222 Merrimack Street, Lowell, Massachusetts (Address of principal executive offices)	**01852** (Zip code)

(978) 459-9000

(Registrant s telephone number, including area code)

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. **x** Yes o 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) **x** Yes o 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 definition for large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act (Check one):

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

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

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date: **November 2, 2011** Common Stock - Par Value **$0.01: 9,445,490** shares outstanding.

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ENTERPRISE BANCORP, INC.

Consolidated Balance Sheets

(Dollars in thousands)	September 30, 2011 (unaudited)	December 31, 2010
Assets		
Cash and cash equivalents:		
Cash and due from banks	$ 33,763	$ 30,541
Short-term investments	48,419	24,465
Total cash and cash equivalents	82,182	55,006
Investment securities at fair value	128,922	142,060
Federal Home Loan Bank Stock	4,740	4,740
Loans, less allowance for loan losses of $22,569 at September 30, 2011 and $19,415 at December 31, 2010 respectively	1,206,989	1,123,931
Premises and equipment	25,893	24,924
Accrued interest receivable	5,418	5,532
Deferred income taxes, net	12,129	11,039
Bank-owned life insurance	14,801	14,397
Prepaid income taxes	377	379
Prepaid expenses and other assets	9,693	9,657
Goodwill	5,656	5,656
Total assets	$ 1,496,800	$ 1,397,321
Liabilities and Stockholders Equity		
Liabilities		
Deposits	$ 1,345,488	$ 1,244,071
Borrowed funds	4,494	15,541
Junior subordinated debentures	10,825	10,825
Accrued expenses and other liabilities	11,080	9,297
Accrued interest payable	366	914
Total liabilities	1,372,253	1,280,648
Commitments and Contingencies		
Stockholders Equity		
Preferred stock, $0.01 par value per share; 1,000,000 shares authorized; no shares issued		
Common stock $0.01 par value per share; 20,000,000 shares authorized; 9,444,428, and 9,290,465 shares issued and outstanding at September 30, 2011 and December 31, 2010	94	93
Additional paid-in-capital	44,577	42,590
Retained earnings	77,133	72,000
Accumulated other comprehensive income	2,743	1,990
Total stockholders equity	124,547	116,673
Total liabilities and stockholders equity	$ 1,496,800	$ 1,397,321

See the accompanying notes to the unaudited consolidated financial statements.

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ENTERPRISE BANCORP, INC.

Consolidated Statements of Income

(unaudited)

(Dollars in thousands, except per share data)	Three Months Ended September 30, 2011	Three Months Ended September 30, 2010	Nine Months Ended September 30, 2011	Nine Months Ended September 30, 2010
Interest and dividend income:				
Loans	$ 16,078	$ 15,334	$ 46,915	$ 45,457
Investment securities	827	996	2,693	3,143
Short-term investments	8	23	35	43
Total interest and dividend income	16,913	16,353	49,643	48,643
Interest expense:				
Deposits	1,858	2,125	5,676	6,680
Borrowed funds	22	37	66	144
Junior subordinated debentures	294	294	883	883
Total interest expense	2,174	2,456	6,625	7,707
Net interest income	14,739	13,897	43,018	40,936
Provision for loan losses	1,840	1,275	3,954	3,187
Net interest income after provision for loan losses	12,899	12,622	39,064	37,749
Non-interest income:				
Investment advisory fees	919	880	2,844	2,613
Deposit service fees	1,157	1,040	3,313	3,046
Income on bank-owned life insurance	162	170	484	492
Other than temporary impairment on investment securities				(8)
Net gains on sales of investment securities	486		747	777
Gains on sales of loans	119	208	403	392
Other income	397	362	1,275	1,296
Total non-interest income	3,240	2,660	9,066	8,608
Non-interest expense:				
Salaries and employee benefits	7,177	6,703	21,275	19,825
Occupancy and equipment expenses	1,346	1,302	4,147	3,941
Technology and telecommunications expenses	959	839	2,893	2,761
Advertising and public relations expenses	471	477	1,717	1,758
Deposit insurance premiums	276	469	1,049	1,378
Audit, legal and other professional fees	331	280	1,003	875
Supplies and postage expenses	212	194	636	591
Investment advisory and custodial expenses	97	107	327	353
Other operating expenses	1,009	837	3,125	2,631
Total non-interest expense	11,878	11,208	36,172	34,113
Income before income taxes	4,261	4,074	11,958	12,244
Provision for income taxes	1,324	1,345	3,872	4,026

Net income	$ 2,937	$ 2,729	$ 8,086	$ 8,218
Basic earnings per share	$ 0.31	$ 0.30	$ 0.86	$ 0.89
Diluted earnings per share	$ 0.31	$ 0.30	$ 0.86	$ 0.89
Basic weighted average common shares outstanding	9,429,360	9,246,601	9,383,678	9,197,269
Diluted weighted average common shares outstanding	9,463,664	9,250,665	9,435,506	9,201,468

See the accompanying notes to the unaudited consolidated financial statements.

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ENTERPRISE BANCORP, INC.

Consolidated Statement of Changes in Stockholders Equity

(Unaudited)

Nine months ended September 30, 2011

(Dollars in thousands)	Common Stock	Additional Paid-in Capital	Retained Earnings	Comprehensive Income	Accumulated Other Comprehensive Income	Total Stockholders Equity
Balance at December 31, 2010	$ 93	$ 42,590	$ 72,000		$ 1,990	$ 116,673
Comprehensive income						
Net income			8,086	$ 8,086		8,086
Other comprehensive income, net				753	753	753
Total comprehensive income				$ 8,839		
Tax benefit from exercise of stock options		4				4
Common stock dividend paid ($0.315 per share)			(2,953)			(2,953)
Common stock issued under dividend reinvestment plan		942				942
Stock-based compensation	1	802				803
Stock options exercised		239				239
Balance at September 30, 2011	$ 94	$ 44,577	$ 77,133		$ 2,743	$ 124,547

See the accompanying notes to the unaudited consolidated financial statements.

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ENTERPRISE BANCORP, INC.

Consolidated Statements of Cash Flows

(Unaudited)

(Dollars in thousands)	**Nine months ended September 30, 2011**	**2010**
Cash flows from operating activities:		
Net income	$ 8,086	$ 8,218
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	3,954	3,187
Depreciation and amortization	3,081	2,826
Amortization of intangible assets		76
Stock-based compensation expense	796	664
Mortgage loans originated for sale	(19,338)	(31,673)
Proceeds from mortgage loans sold	22,549	28,878
Gains on sales of loans	(403)	(392)
Gains on sales of OREO		(120)
Net gains on sales of investment securities	(747)	(777)
Other-than-temporary-impairment on investment securities		8
Income on bank-owned life insurance, net of costs	(404)	(422)
Changes in:		
Accrued interest receivable	114	(159)
Prepaid expenses and other assets	423	(1,569)
Deferred income taxes	(1,524)	
Accrued expenses and other liabilities	327	3,468
Accrued interest payable	(548)	(655)
Net cash provided by operating activities	16,366	11,558
Cash flows from investing activities:		
Proceeds from sales of investment securities available for sale	10,935	5,330
Proceeds from maturities, calls and pay-downs of investment securities	39,000	38,435
Purchase of investment securities	(33,611)	(41,286)
Net increase in loans	(90,645)	(32,331)
Additions to premises and equipment, net	(3,796)	(4,097)
Proceeds from OREO sales and payments	325	1,556
Net cash used in investing activities	(77,792)	(32,393)
Cash flows from financing activities:		
Net increase in deposits	101,417	120,556
Net decrease in borrowed funds	(11,047)	(9,854)
Cash dividends paid	(2,953)	(2,755)
Proceeds from issuance of common stock	942	902
Proceeds from the exercise of common stock options	239	
Tax benefit from the exercise of common stock option	4	
Net cash provided by financing activities	88,602	108,849
Net increase in cash and cash equivalents	27,176	88,014
Cash and cash equivalents at beginning of period	55,006	32,610
Cash and cash equivalents at end of period	$ 82,182	$ 120,624
Supplemental financial data:		
Cash Paid For: Interest	$ 7,173	$ 8,362
Income taxes	5,391	5,105
Supplemental schedule of non-cash investing activity:		

Purchase of investment securities not yet settled	1,463	
Transfer from loans to other real estate owned	825	1,350

See accompanying notes to the unaudited consolidated financial statements.

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ENTERPRISE BANCORP, INC.

Notes to the Unaudited Consolidated Financial Statements

(1) Organization of Holding Company

The consolidated interim financial statements of Enterprise Bancorp, Inc. (the Company or Enterprise) include the accounts of the Company and its wholly owned subsidiary Enterprise Bank and Trust Company (the Bank). The Bank is a Massachusetts trust company organized in 1989. Substantially all of the Company s operations are conducted through the Bank.

The Bank has five wholly owned subsidiaries. The Bank s subsidiaries include Enterprise Insurance Services, LLC and Enterprise Investment Services, LLC, organized for the purposes of engaging in insurance sales activities and offering non-deposit investment products and services, respectively. In addition, the Bank has three subsidiary security corporations (Enterprise Security Corporation, Enterprise Security Corporation II, and Enterprise Security Corporation III), which hold various types of qualifying securities. The security corporations are limited to conducting securities investment activities that the Bank itself would be allowed to conduct under applicable laws.

Through the Bank and its subsidiaries, the Company offers a range of commercial and consumer loan products, deposit and cash management products, investment advisory and management, trust and insurance services. The services offered through the Bank and subsidiaries are managed as one strategic unit and represent the Company s only reportable operating segment.

The Federal Deposit Insurance Corporation (the FDIC) and the Massachusetts Commissioner of Banks (the Commissioner) have regulatory authority over the Bank. The Bank is also subject to certain regulatory requirements of the Board of Governors of the Federal Reserve System (the Federal Reserve Board) and, with respect to its New Hampshire branch operations, the New Hampshire Banking Department. The business and operations of the Company are subject to the regulatory oversight of the Federal Reserve Board. The Commissioner also retains supervisory jurisdiction over the Company.

(2) Basis of Presentation

The accompanying unaudited consolidated financial statements and these notes should be read in conjunction with the Company s December 31, 2010 audited consolidated financial statements and notes thereto contained in the Company s 2010 Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 15, 2011. Interim results are not necessarily indicative of results to be expected for the entire year.

The Company has not changed its significant accounting and reporting policies from those disclosed in its 2010 Annual Report on Form 10-K.

The accompanying unaudited consolidated financial statements have been prepared in accordance with generally accepted accounting principles (GAAP) for interim financial information and the instructions for Form 10-Q and Article 10 of Regulation S-X. In the opinion of management, the accompanying consolidated financial statements reflect all necessary adjustments consisting of normal recurring accruals for a fair presentation. All significant intercompany balances and transactions have been eliminated in the accompanying consolidated financial statements.

Certain previous year amounts in the footnotes to the consolidated financial statements have been reclassified to conform to the current year s presentation.

(3) Critical Accounting Estimates

In preparing the consolidated financial statements in conformity with U.S. generally accepted accounting principles, management is required to exercise judgment in determining many of the methodologies, assumptions and estimates to be utilized. These estimates and assumptions affect the reported amounts of assets and liabilities as of the balance sheet date and revenues and expenses for the period then ended. As future events and their effects cannot be determined with precision, actual results could differ significantly from these estimates should the assumptions and estimates used change over time due to changes in circumstances. Changes in those estimates resulting from continuing changes in the economic environment and other factors will be reflected in the financial statements and results of operations in future periods.

As discussed in the Company s 2010 Annual Report on Form 10-K, the three most significant areas in which management applies critical assumptions and estimates that are particularly susceptible to change relate to the determination of the allowance for loan losses, impairment review of investment securities and the impairment review of goodwill. Refer to note 1 to the Company s

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Notes to the Unaudited Consolidated Financial Statements

consolidated financial statements included in the Company s 2010 Annual Report on Form 10-K for significant accounting policies.

(4) Reporting Comprehensive Income

Comprehensive income is defined as all changes to equity except investments by and distributions to stockholders. Net income is one component of comprehensive income, with other components referred to in the aggregate as other comprehensive income. The Company s only other comprehensive income component is the net unrealized holding gains or losses on investments available for sale, net of deferred income taxes.

The following table summarizes the components of other comprehensive income for the nine month periods ended September 30, 2011 and 2010.

(Dollars in thousands)	**2011**	**2010**
Gross unrealized holding gains on investments arising during the period	$ 1,933	$ 3,421
Income tax expense	(697)	(1,235)
Net unrealized holding gains, net of tax	1,236	2,186
Less: Reclassification adjustment for impairment included in net income:		
Other than temporary impairment loss arising during the period		(8)
Income tax benefit		3
Reclassification adjustment for impairment realized, net of tax		(5)
Less: Reclassification adjustment for net gains included in net income		
Net realized gains on sales of securities during the period	747	777
Income tax expense	(264)	(271)
Reclassification adjustment for gains realized, net of tax	483	506
Other comprehensive income, net of reclassifications	$ 753	$ 1,685

(5) Earnings per share

Basic earnings per share are calculated by dividing net income by the weighted average number of common shares outstanding during the period. Diluted earnings per share reflects the effect on weighted average shares outstanding of the number of additional shares outstanding if dilutive stock options were converted into common stock using the treasury stock method.

The table below presents the increase in average shares outstanding, using the treasury stock method, for the diluted earnings per share calculation and the effect of those shares on earnings, for the periods indicated:

	Three months ended September 30,				Nine months ended September 30,			
	2011		2010		2011		2010	
Basic weighted average common shares outstanding		9,429,360		9,246,601		9,383,678		9,197,269
Dilutive shares		34,304		4,064		51,828		4,199
Diluted weighted average common shares outstanding		9,463,664		9,250,665		9,435,506		9,201,468
Basic earnings per share	$	0.31	$	0.30	$	0.86	$	0.89
Effect of dilutive shares								
Diluted earnings per share	$	0.31	$	0.30	$	0.86	$	0.89

For the nine months ended September 30, 2011, there was an additional 133,535 average stock options outstanding, which were excluded from the year-to-date calculation of diluted earnings per share due to the exercise price of these options exceeding the

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average market price of the Company s common stock for the period. These options, which were not dilutive at that date, may potentially dilute earnings per share in the future.

(6) Investments

The amortized cost and carrying values of investment securities at the dates specified are summarized as follows:

	September 30, 2011			
(Dollars in thousands)	**Amortized cost**	**Unrealized gains**	**Unrealized losses**	**Carrying Amount**
Federal agency obligations (1)	$ 37,541	$ 186	$	$ 37,727
Federal agency mortgage backed securities (MBS) (1)	35,852	1,577		37,429
Municipal securities	45,603	2,428		48,031
Total fixed income securities	118,996	4,191		123,187
Equity investments	5,645	584	494	5,735
Total available for sale securities, at fair value	$ 124,641	$ 4,775	$ 494	$ 128,922

	December 31, 2010			
(Dollars in thousands)	**Amortized cost**	**Unrealized gains**	**Unrealized losses**	**Carrying Amount**
Federal agency obligations(1)	$ 41,149	$ 55	$ 264	$ 40,940
MBS(1)	41,581	1,056	112	42,525
Non-agency collateralized mortgage obligation (CMO)	2,386	53		2,439
Municipal securities	50,576	1,109	96	51,589
Total fixed income securities	135,692	2,273	472	137,493
Equity investments	3,273	1,300	6	4,567
Total available for sale securities, at fair value	$ 138,965	$ 3,573	$ 478	$ 142,060

(1) These categories may include investments issued or guaranteed by government sponsored enterprises such as Fannie Mae (FNMA), Freddie Mac (FHLMC), Ginnie Mae (GNMA), Federal Farm Credit Bank (FFCB), or one of several Federal Home Loan Banks (FHLBs). All agency MBS/CMO investments owned by the Company are backed by residential mortgages.

Included in the carrying amount of federal agency MBS category were CMOs totaling $23.0 million and $26.0 million at September 30, 2011 and December 31, 2010, respectively.

See Note 13, Fair Value Measurements below for further information regarding the Company s fair value measurements for available-for-sale securities.

The contractual maturity distribution as of September 30, 2011, of the fixed income securities is set forth in the table below:

	Within One Year		After One, But Within Five Years		After Five, But within Ten Years		After Ten Years	
	Amortized Cost	**Carrying Amount**	**Amortized Cost**	**Carrying Amount**	**Amortized Cost**	**Carry Amount**	**Amortized Cost**	**Carry Amount**
Federal agency obligations	$	$	$ 37,541	$ 37,727	$	$	$	$
MBS			181	181	15,001	15,549	20,670	21,699
Municipal securities	4,696	4,754	10,633	11,003	16,711	17,707	13,563	14,567
Total Fixed Income	$ 4,696	$ 4,754	$ 48,355	$ 48,911	$ 31,712	$ 33,256	$ 34,233	$ 36,266

Scheduled contractual maturities may not reflect the actual maturities of the investments. MBS/CMO s are shown at their final maturity. However, due to prepayments and amortization the actual MBS/CMO cash flows may be faster than presented above. Similarly, included in the carrying value of municipal and federal agency obligations categories are $47.1 million in securities which can be called before maturity. Actual maturity of these callable securities could be shorter if market interest rates decline further. Management considers these factors when evaluating the net interest margin in the Company s asset-liability management program.

Net unrealized appreciation and depreciation on investments available for sale, net of applicable income taxes, are reflected as a component of accumulated other comprehensive income.

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The net unrealized gain or loss in the Company s fixed income portfolio fluctuates as market interest rates rise and fall. Due to the fixed rate nature of this portfolio, as market rates fall the value of the portfolio rises, and as market rates rise, the value of the portfolio declines. The unrealized gains or losses on fixed income investments will also decline as the securities approach maturity. Unrealized gains or losses will be recognized in the statements of income if the securities are sold. However, if an unrealized loss on the fixed income portfolio is deemed to be other than temporary, the credit loss portion is charged to earnings and the noncredit portion is recognized in accumulated other comprehensive income. At September 30, 2011, the Company did not have any unrealized losses on the fixed income portfolio.

The net unrealized gain or loss on equity securities will fluctuate based on changes in the market value of the funds and individual securities held in the portfolio. Unrealized gains or losses will be recognized in the statements of income if the securities are sold. However, if an unrealized loss on an equity security is deemed to be other than temporary prior to a sale, the loss is charged to earnings.

At September 30, 2011, the equity portfolio consisted primarily of investments in a diversified group of mutual funds, with a small portion of the portfolio (approximately 16%) invested in funds or individual common stock of entities in the financial services industry. At September 30, 2011, the Company had seventeen investments in equity mutual funds or individual stocks having combined unrealized losses of $494 thousand which were short term in nature. Management regularly reviews the portfolio for securities with unrealized losses that are other than temporarily impaired. Management s assessment includes evaluating if any equity security or fund exhibits fundamental deterioration and whether it is unlikely that the security or fund will completely recover its unrealized loss within a reasonable time period. In determining the amount of the other than temporary impairment charge, management considers the severity of the declines and the uncertainty of recovery in the short-term for these equities. Based upon this review, the Company did not consider those equity funds to be other-than-temporarily impaired at September 30, 2011.

During the nine months ended September 30, 2011, the Company did not record any fair value impairment charges on equity investments; during that period, the Company sold $388 thousand of previously impaired equity funds and recognized book gains of $207 thousand. In addition, the Company sold $9.8 million in other investment securities, primarily municipal securities, and recognized book gains of $540 thousand.

During the nine months ended September 30, 2010, the Company recorded fair value impairment charges of $8 thousand, on a previously impaired equity investment; also during that period, the Company sold $1.6 million of previously impaired equity funds and recognized book gains of $752 thousand, in addition to gains of $25 thousand on other investment securities over the period.

From time to time the Company may pledge securities from its investment portfolio as collateral for various municipal deposit accounts and repurchase agreements. The fair value of securities pledged as collateral for these purposes was $42.8 million at September 30, 2011. In addition, securities designated as qualified collateral for FHLB borrowing capacity amounted to $27.2 million at September 30, 2011. Securities designated as qualified collateral for borrowing from the Federal Reserve Bank of Boston (the FRB) through its discount window amounted to $42.6 million at September 30, 2011.

(7) Restricted Investments

As a member of the Federal Home Loan Bank of Boston (FHLB), the Company is required to purchase certain levels of FHLB capital stock in association with the Company s borrowing relationship from the FHLB. This stock is classified as a restricted investment and carried at cost, which management believes approximates fair value. FHLB stock represents the only restricted investment held by the Company.

In February 2009, the FHLB began implementing a number of measures in order to strengthen its financial position and to increase its capital levels, including the indefinite suspension of its quarterly dividends and a moratorium on the repurchase of excess capital stock from member banks, among other programs. However, in the first quarter of 2011, the FHLB announced the reinstitution of quarterly dividends on capital stock balances based on improved profitability and capital levels. The FHLB noted that the board of directors anticipates continuing to declare modest cash dividends through 2011, but cautioned that negative events such as further credit losses, a decline in income or regulatory disapproval could lead them to reconsider this plan. The FHLB continues to take steps to protect members capital and improve its profitability, including amendments to its capital plan and a joint capital enhancement agreement with the other eleven FHLBs, and a continuation of the moratorium on excess capital stock repurchases. Although recent financial results of the FHLB have improved, if further deterioration in the FHLB financial condition or capital levels occurs, the Company s investment in FHLB capital stock may become other than temporarily impaired to some degree. At September 30, 2011, the Company s investment in FHLB capital stock amounted to $4.7 million. Based on management s review of this investment, FHLB stock was not other than temporarily impaired as of September 30, 2011.

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Notes to the Unaudited Consolidated Financial Statements

(8) Loans

Major classifications of loans and loans held for sale at the periods indicated, are as follows:

(Dollars in thousands)	September 30, 2011	December 31, 2010
Real estate:		
Commercial real estate	$ 634,229	$ 595,075
Commercial construction	120,753	111,681
Residential mortgages	89,900	86,560
Residential construction	2,429	2,874
Loans held for sale	3,600	6,408
Total real estate	850,911	802,598
Commercial and industrial	305,015	274,829
Home equity	71,547	63,108
Consumer	3,541	4,228
Gross loans	1,231,014	1,144,763
Deferred loan origination fees, net	(1,456)	(1,417)
Total loans	1,229,558	1,143,346
Allowance for loan losses	(22,569)	(19,415)
Net loans and loans held for sale	$ 1,206,989	$ 1,123,931

The Company manages its loan portfolio to avoid concentration by industry and loan size to minimize its credit risk exposure. In addition, the Company does not have a sub-prime mortgage program. However, inherent in the lending process is the risk of loss due to customer non-payment, or credit risk.

Loan Categories

Commercial loans:

Commercial real estate loans include loans secured by both owner-use and non-owner occupied real estate. These loans are typically secured by a variety of commercial and industrial property types including apartment buildings, office or mixed-use facilities, strip shopping centers, or other commercial property and are generally guaranteed by the principals of the borrower. Commercial real estate loans generally have repayment periods of approximately fifteen to twenty-five years. Variable interest rate commercial real estate loans have a variety of adjustment terms and indices, and are generally fixed for the first one to five years before periodic rate adjustments begin.

Commercial and industrial loans include seasonal revolving lines of credit, working capital loans, equipment financing (including equipment leases), and term loans. Also included in commercial and industrial loans are loans partially guaranteed by the Small Business Administration (SBA), loans under various programs issued in conjunction with the Massachusetts Development Finance Agency and other agencies. Commercial and industrial credits may be unsecured loans and lines to financially strong borrowers, secured in whole or in part by real estate unrelated to the principal purpose of the loan or secured by inventories, equipment, or receivables, and are generally guaranteed by the principals of the borrower. Variable rate loans and lines in this portfolio have interest rates that are periodically adjusted, with loans generally having fixed initial periods of one to three years. Commercial and industrial loans have average repayment periods of one to seven years.

Commercial construction loans include the development of residential housing and condominium projects, the development of commercial and industrial use property and loans for the purchase and improvement of raw land. These loans are secured in whole or in part by the underlying real estate collateral and are generally guaranteed by the principals of the borrowers. Construction lenders work to cultivate long-term relationships with established developers. The Company limits the amount of financing provided to any single developer for the construction of properties built on a speculative basis. Funds for construction projects are disbursed as pre-specified stages of construction are completed. Regular site inspections are performed, either by experienced construction lenders on staff or by independent outside inspection companies, at each construction phase, prior to advancing additional funds. Commercial construction loans generally are variable rate loans and lines with interest rates that are periodically adjusted and generally have terms of one to three years.

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From time to time, the Company participates with other banks in the financing of certain commercial projects. In some cases, the Company may act as the lead lender, originating and servicing the loans, but participating out a portion of the funding to other banks. In other cases, the Company may participate in loans originated by other institutions. In each case, the participating bank funds a percentage of the loan commitment and takes on the related risk. In each case in which the Company participates in a loan, the rights and obligations of each participating bank are divided proportionately among the participating banks in an amount equal to their share of ownership and with equal priority among all banks. The balances participated out to other institutions are not carried as assets on the Company s financial statements. Loans originated by other banks in which the Company is the participating institution are carried in the loan portfolio at the Company s pro rata share of ownership. The Company performs an independent credit analysis of each commitment and a review of the participating institution prior to participation in the loan. Loans originated by other banks in which the Company is the participating institution amounted to $35.4 million at September 30, 2011 and $32.7 million at December 31, 2010.

Standby letters of credit are conditional commitments issued by the Company to guarantee the financial obligation or performance by a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. If the letter of credit is drawn upon, a loan is created for the customer, generally a commercial loan, with the same criteria associated with similar commercial loans.

Other loans:

Enterprise originates conventional mortgage loans on one-to-four family residential properties. These properties may serve as the borrower s primary residence, or be vacation homes or investment properties. Loan to value limits vary, generally from 80% for adjustable rate and multi-family, owner occupied properties, up to 97% for fixed rate loans on single family, owner occupied properties, with mortgage insurance coverage required for loan-to-value ratios greater than 80% based on program parameters. In addition, financing is provided for the construction of owner occupied primary residences. Residential mortgage loans may have terms of up to 30 years at either fixed or adjustable rates of interest. Fixed and adjustable rate residential mortgage loans are generally originated using secondary market underwriting and documentation standards.

Depending on the current interest rate environment, management projections of future interest rates and the overall asset-liability management program of the Company, management may elect to sell those fixed and adjustable rate residential mortgage loans which are eligible for sale in the secondary market, or hold some or all of this residential loan production for the Company s portfolio. Mortgage loans are generally not pooled for sale, but instead sold on an individual basis. The Company may retain or sell the servicing when selling the loans. All loans sold are currently sold without recourse, subject to an early payment default period covering the first four payments for certain loan sales.

Home equity loans are originated for one-to-four family residential properties with maximum original loan to value ratios generally up to 80% of the assessed or appraised value of the property securing the loan. Home equity loan payments consist of monthly principal and interest based on amortization ranging from three to fifteen years. The rates may also be fixed for three to fifteen years.

The Company originates home equity lines of credit for one-to-four family residential properties with maximum original loan to value ratios generally up to 80% of the appraised value of the property securing the loan. Home equity lines generally have interest rates that adjust monthly based on changes in the Prime Rate as published in the Wall Street Journal, although minimum rates may be applicable. Some home equity line rates may be fixed for a period of time and then adjusted monthly thereafter. The payment schedule for home equity lines for the first ten years of the lines are interest only payments. Generally at the end of ten years, the line is frozen to future advances, and principal plus interest payments are collected over a fifteen-year amortization schedule.

Consumer loans primarily consist of secured or unsecured personal loans and overdraft protection lines on checking accounts extended to individual customers.

Loans serviced for others

At September 30, 2011 and December 31, 2010, the Company was servicing residential mortgage loans owned by investors amounting to $26.0 million and $27.2 million, respectively. Additionally, the Company was servicing commercial loans participated out to various other institutions amounting to $38.0 million and $36.6 million at September 30, 2011 and December 31, 2010, respectively.

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Loans Serving as Collateral

Loans designated as qualified collateral and pledged to the FHLB for borrowing capacity are summarized below:

	September 30, 2011	December 31, 2010
Commercial real estate	$ 212,999	$ 227,926
Residential mortgages	64,755	63,166
Home equity	19,665	24,417
Total loans pledged to FHLB	$ 297,419	$ 315,509

(9) Allowance for Loan Loss

Credit Quality Indicators

Adversely Classified Loans

The Company s loan risk rating system classifies loans depending on risk of loss characteristics. The classifications range from substantially risk free for the highest quality loans and loans that are secured by cash collateral, to the more severe adverse classifications of substandard , doubtful and loss based on criteria established under banking regulations.

Loans classified as substandard include those loans characterized by the distinct possibility that the Company will sustain some loss if the deficiencies are not corrected. These loans are inadequately protected by the sound net worth and paying capacity of the borrower; repayment has become increasingly reliant on collateral liquidation or reliance on guaranties; credit weaknesses are well-defined; borrower cash flow is insufficient to meet required debt service specified in loan terms and to meet other obligations, such as trade debt and tax payments.

Loans classified as doubtful have all the weaknesses inherent in a substandard rated loan with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable. The probability of loss is extremely high, but because of certain important and reasonably specific pending factors which may work to the advantage and strengthening of the loan, its classification as an estimated loss is deferred until more exact status may be determined.

Loans classified as loss are generally considered uncollectible at present, although long term recovery of part or all of loan proceeds may be possible. These loss loans would require a specific loss reserve or charge-off.

Adversely classified loans may be accruing or in non-accrual status and may be additionally designated as impaired or restructured, or some combination thereof. Loans which are evaluated to be of weaker credit quality are reviewed on a more frequent basis by management.

The following table presents the credit risk profile by internally assigned risk rating category at the periods indicated.

	September 30, 2011				
	Adversely Classified				
(Dollars in thousands)	Substandard	Doubtful	Loss	Not Adversely Classified	Gross Loans
Cmml real estate	$ 23,244	$	$	$ 610,985	$ 634,229
Cmml and industrial	7,908	105		297,002	305,015
Cmml construction	5,101			115,652	120,753
Residential	1,459			90,870	92,329
Home Equity	213			71,334	71,547
Consumer	5	3		3,533	3,541
Loans held for sale				3,600	3,600
Total gross loans	$ 37,930	$ 108	$	$ 1,192,976	$ 1,231,014

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	December 31, 2010				
	Adversely Classified				
(Dollars in thousands)	Substandard	Doubtful	Loss	Not Adversely Classified	Gross Loans
Cmml real estate	$ 12,885	$ 250	$	$ 581,940	$ 595,075
Cmml and industrial	6,765	47		268,017	274,829
Cmml construction	2,890			108,791	111,681
Residential	2,132			87,302	89,434
Home Equity	207			62,901	63,108
Consumer	18	4		4,206	4,228
Loans held for sale				6,408	6,408
Total gross loans	$ 24,897	$ 301	$	$ 1,119,565	$ 1,144,763

The increase in adversely classified loans as of September 30, 2011, as compared to December 2010, was primarily due to the downgrade of twelve commercial real estate relationships totaling approximately $11.4 million and two construction relationships of approximately $3.0 million, partially offset by paydowns and credit upgrades during the period. Management continues to closely monitor these adversely classified relationships.

Past Due and Non-Accrual Loans

Loans on which the accrual of interest has been discontinued are designated as non-accrual loans. Accrual of interest on loans is generally discontinued when a loan becomes contractually past due, with respect to interest or principal, by 90 days, or when reasonable doubt exists as to the full and timely collection of interest or principal. When a loan is placed on non-accrual status, all interest previously accrued but not collected is reversed against current period interest income. Interest accruals are resumed on such loans only when payments are brought current and have remained current for a period of 180 days and when, in the judgment of management, the collectability of both principal and interest is reasonably assured. Interest payments received on loans in a non-accrual status are generally applied to principal.

The following table presents an age analysis of past due loans as of September 30, 2011.

(Dollars in thousands)	Loans 30-59 Days Past Due	Loans 60-89 Days Past Due	Loans 90 or More Days Past Due (non-accrual)	Total Past Due Loans	Current Loans	Gross Loans
Cmml real estate	$ 2,314	$ 987	$ 13,291	$ 16,592	$ 617,637	$ 634,229
Cmml and industrial	1,100	733	9,254	11,087	293,928	305,015
Cmml construction	472		2,107	2,579	118,174	120,753
Residential	420	822	997	2,239	90,090	92,329
Home Equity	147	72	141	360	71,187	71,547
Consumer	50	19	6	75	3,466	3,541

Loans held for sale										3,600		3,600
Total gross loans	$	4,503	$	2,633	$	25,796	$	32,932	$	1,198,082	$	1,231,014

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The following table presents an age analysis of past due loans as of December 31, 2010.

(Dollars in thousands)	Loans 30-59 Days Past Due	Loans 60-89 Days Past Due	Loans 90 or More Days Past Due (non-accrual)	Total Past Due Loans	Current Loans	Gross Loans
Cmml real estate	$ 4,363	$ 2,002	$ 8,065	$ 14,430	$ 580,645	$ 595,075
Cmml and industrial	816	317	7,573	8,706	266,123	274,829
Cmml construction	247		2,890	3,137	108,544	111,681
Residential	622		1,667	2,289	87,145	89,434
Home Equity	40		135	175	62,933	63,108
Consumer	24	5	11	40	4,188	4,228
Loans held for sale					6,408	6,408
Total gross loans	$ 6,112	$ 2,324	$ 20,341	$ 28,777	$ 1,115,986	$ 1,144,763

As of September 30, 2011, loans 30 59 days past due declined compared to December 31, 2010, due primarily to several commercial real estate loans which were 31 days overdue at December 31, 2010 that were subsequently brought current. Total non-accrual loans amounted to $25.8 million at September 30, 2011 and $20.3 million at December 31, 2010. Non-accrual loans which were not adversely classified amounted to $2.7 million at September 30, 2011 and $2.4 million at December 31, 2010. These balances primarily represented the guaranteed portions of non-performing Small Business Administration loans.

The ratio of non-accrual loans to total loans amounted to 2.10%, 1.78% and 1.64% at September 30, 2011, December 31, 2010 and September 30, 2010, respectively.

The level of delinquent and non-performing assets is largely a function of economic conditions and the overall banking environment. Despite prudent loan underwriting, adverse changes within the Company s market area or further deterioration in the local, regional or national economic conditions could negatively impact the Company s level of non-performing assets in the future.

At September 30, 2011, additional funding commitments for loans on non-accrual status totaled $158 thousand. The Company s obligation to fulfill the additional funding commitments on non-accrual loans is generally contingent on the borrower s compliance with the terms of the credit agreement, or if the borrower is not in compliance additional funding commitments may be made at the Company s discretion.

The majority of the non-accrual loan balances were also carried as impaired loans during the periods, and are discussed further below.

Impaired Loans

Impaired loans are individually significant loans for which management considers it probable that not all amounts due (principal and interest) in accordance with original contractual terms will be collected. The majority of impaired loans are included within the non-accrual balances; however, not every loan in non-accrual status has been designated as impaired. Impaired loans include loans that have been modified in a troubled debt restructuring (or TDR , see below). Management does not set any minimum delay of payments as a factor in reviewing for impaired classification. Management considers the payment status, net worth and earnings potential of the borrower, and the value and cash flow of the collateral as factors to determine if a loan will be paid in accordance with its contractual terms.

Impaired loans exclude large groups of smaller-balance homogeneous loans, such as residential mortgage loans and consumer loans, which are collectively evaluated for impairment, loans that are measured at fair value and leases, unless the loan is amended in a TDR. Impaired loans are individually evaluated for credit loss and a specific reserve is assigned for the amount of the estimated credit loss. Refer to heading Allowance for probable loan losses methodology contained in Note 3 Loans and Allowance For Loan Losses , to the Company s consolidated financial statements contained in the Company s 2010 Annual Report on Form 10-K for further discussion of management s methodology used to estimate specific reserves for impaired loans.

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Total impaired loans amounted to $38.6 million and $49.8 million, at September 30, 2011 and December 31, 2010, respectively. Total accruing impaired loans amounted to $13.4 million and $30.7 million at September 30, 2011 and December 31, 2010, respectively, while non accrual impaired loans amounted to $25.2 million and $19.1 million as of September 30, 2011 and December 31, 2010, respectively. During the current year, an accruing commercial real estate relationship of approximately $13.2 million was upgraded and removed from impaired/TDR status, due to the borrower s improved financial condition and sustained performance over time. In addition, the decrease was impacted by paydowns and, in particular, the full payoff of one $3.3 million commercial real estate impaired/TDR relationship during the first quarter of 2011.

The following table sets forth the recorded investment in impaired loans and the related specific allowance allocated as of September 30, 2011.

(Dollars in thousands)	Unpaid contractual principal balance	Total recorded investment in impaired loans	Recorded investment with no allowance	Recorded investment with allowance	Related allowance
Cmml real estate	$ 25,207	$ 23,862	$ 13,551	$ 10,311	$ 1,163
Cmml and industrial	11,789	10,311	5,281	5,030	2,130
Cmml construction	3,879	3,747	1,543	2,204	652
Residential	706	676	288	388	175
Home Equity					
Consumer	17	17		17	17
Total	$ 41,598	$ 38,613	$ 20,663	$ 17,950	$ 4,137

The following table presents the average recorded investment in impaired loans and the related interest recognized during the periods indicated.

	Three months ended September 30, 2011		Nine months ended September 30, 2011	
(Dollars in thousands)	Average recorded investment	Interest income recognized	Average recorded investment	Interest income recognized
Cmml real estate	$ 22,991	$ 130	$ 28,407	$ 574
Cmml and industrial	9,837	18	9,668	47
Cmml construction	3,755	20	4,055	64
Residential	661	1	602	2
Home Equity				1
Consumer	19	1	19	2
Total	$ 37,263	$ 170	$ 42,751	$ 690

The following table sets forth the recorded investment in impaired loans and the related specific allowance allocated as of December 31, 2010.

(Dollars in thousands)	Unpaid contractual principal balance	Total recorded investment in impaired loans	Recorded investment with no allowance	Recorded investment with allowance	Related allowance
Cmml real estate	$ 37,331	$ 36,031	$ 25,405	$ 10,626	$ 853
Cmml and industrial	9,942	8,780	4,824	3,956	1,284
Cmml construction	4,419	4,364	2,135	2,229	414
Residential	646	630	283	347	121
Home Equity					
Consumer	19	19		19	19
Total	$ 52,357	$ 49,824	$ 32,647	$ 17,177	$ 2,691

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Troubled Debt Restructures

Loans are designated as a TDR when a concession is made on a credit as a result of financial difficulties of the borrower. Typically, such concessions consist of a reduction in interest rate to a below market rate, taking into account the credit quality of the note, or a deferment or reduction of payments, principal or interest, which materially alters the Bank s position or significantly extends the note s maturity date, such that the present value of cash flows to be received is materially less than those contractually established at the loan s origination.

Restructured loans are included in the impaired loan category and as such, these loans are individually evaluated and a specific reserve is assigned for the amount of the estimated credit loss. Refer to heading Allowance for probable loan losses methodology contained in Note 3 Loans and Allowance For Loan Losses , to the Company s consolidated financial statements contained in the Company s 2010 Annual Report on Form 10-K for further discussion of management s methodology used to estimate specific reserves for impaired loans.

Total TDR loans, included in the impaired loan figures above as of September 30, 2011 and December 31, 2010 were $27.3 million and $41.6 million, respectively.

TDR loans on accrual status amounted to $12.6 million and $30.2 million at September 30, 2011 and December 31, 2010, respectively. The decrease in accruing TDR loans is primarily due to the upgrade of the accruing commercial real estate relationship referred to above under impaired loans. TDR loans included in non-performing loans amounted to $14.7 million and $11.4 million at September 30, 2011 and December 31, 2010, respectively.

The following tables present certain information regarding loan modifications classified as troubled debt restructures during the periods presented.

Troubled debt restructure agreements entered into during the three months ended September 30, 2011.

(Dollars in thousands)	**Number of restructurings**	**Pre-modification outstanding recorded investment**	**Post-modification outstanding recorded investment**
Cmml real estate	6	$ 1,854	$ 1,841
Cmml and industrial	4	121	118
Cmml construction	1	1,438	1,377
Residential	1	138	136

Home Equity			
Consumer			
Total	12	$ 3,551	3,472

Troubled debt restructures that defaulted during the three months ended September 30, 2011.

(Dollars in thousands)	Number of TDR s that defaulted	Post-modification outstanding recorded investment as of September 30, 2011
Cmml real estate	1	$ 582
Cmml and industrial	3	73
Cmml construction	1	1,377
Residential	1	136
Home Equity		
Consumer		
Total	6	$ 2,168

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Troubled debt restructure agreements entered into during the nine months ended September 30, 2011.

(Dollars in thousands)	Number of restructurings		Pre-modification outstanding recorded investment		Post-modification outstanding recorded investment
Cmml real estate	11	$	3,205	$	3,192
Cmml and industrial	14		1,251		1,228
Cmml construction	2		1,603		1,543
Residential	1		138		136
Home Equity					
Consumer					
Total	28	$	6,197	$	6,099

2011 Troubled debt restructuring that subsequently defaulted during the nine months ended September 30, 2011.

(Dollars in thousands)	Number of TDR s that defaulted		Post-modification outstanding recorded investment as of September 30, 2011
Cmml real estate	2	$	778
Cmml and industrial	8		521
Cmml construction	1		1,378
Residential	1		136
Home Equity			
Consumer			
Total	12	$	2,813

There were no charge-offs associated with TDRs noted in the table above. At September 30, 2011, specific reserves allocated to the 2011 TDRs amounted to $280 thousand, and interest payments received on non-accruing 2011 TDR loans which was applied to principal and not recognized as interest income amounted to $114 thousand.

Allowance for probable loan losses methodology

On a quarterly basis, management prepares an estimate of the allowance necessary to cover estimated credit losses. The Company maintains the allowance at a level that it deems adequate to absorb all reasonably anticipated losses from specifically known and other credit risks associated with the portfolio. The Company uses a systematic methodology to measure the amount of estimated loan loss exposure inherent in the portfolio for purposes of establishing a sufficient allowance for loan losses. The methodology makes use of specific reserves, for loans individually evaluated and deemed impaired and general reserves, for larger groups of homogeneous loans, which rely on a combination of qualitative and quantitative factors that could have an impact on the credit quality of the portfolio.

There have been no material changes in the Company s underwriting practices, credit risk management system, or to the allowance assessment methodology used to estimate loan loss exposure as reported in the Company s Annual Report on Form 10-K for the prior year. Refer to heading Allowance for probable loan losses methodology contained in Note 3 Loans and Allowance For Loan Losses , to the Company s consolidated financial statements contained in the Company s 2010 Annual Report on Form 10-K for further discussion of management s methodology used to estimate the loan loss exposure inherent in the portfolio for purposes of establishing a sufficient allowance.

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Allowance for Loan Loss activity

The allowance for loan losses is established through a provision for loan losses, a direct charge to earnings. Loan losses are charged against the allowance when management believes that the collectability of the loan principal is unlikely. Recoveries on loans previously charged-off are credited to the allowance.

Changes in the allowance for loan losses for the nine months ended September 30, are summarized as follows:

(Dollars in thousands)	2011	2010
Balance at beginning of year	$ 19,415	$ 18,218
Provision charged to operations	3,954	3,187
Loan recoveries	228	49
Less: Loans charged-off	1,028	2,469
Balance at end of year	$ 22,569	$ 18,985

Changes in the allowance for loan losses by segment for the three months ended September 30, 2011, are presented below:

(Dollars in thousands)	Cmml Real Estate	Cmml and Industrial	Cmml Constr	Resid. Mortgage	Home Equity	Consumer	Total
Beginning Balance, 6/30/11	$ 10,473	$ 6,041	$ 3,194	$ 948	$ 557	$ 97	$ 21,310
Provision	839	972	(49)	25	50	3	1,840
Recoveries	28	59				3	90
Less: Charge offs	504	150				17	671
Ending Balance, 09/30/11	$ 10,836	$ 6,922	$ 3,145	$ 973	$ 607	$ 86	$ 22,569

Changes in the allowance for loan losses by segment for the nine months ended September 30, 2011, are presented below:

(Dollars in thousands)	Cmml Real Estate	Cmml and Industrial	Cmml Constr	Resid. Mortgage	Home Equity	Consumer	Total
Beginning Balance, 12/31/10	$ 9,769	$ 5,489	$ 2,609	$ 923	$ 512	$ 113	$ 19,415
Provision	1,529	1,753	532	52	95	(7)	3,954
Recoveries	76	137	4	2		9	228
Less: Charge offs	538	457		4		29	1,028
Ending Balance, 09/30/11	$ 10,836	$ 6,922	$ 3,145	$ 973	$ 607	$ 86	$ 22,569

Ending allowance balance allotted to:							
Loans individually evaluated for impairment	$ 1,163	$ 2,130	$ 652	$ 175	$	$ 17	$ 4,137
Loans collectively evaluated for impairment	9,673	4,792	2,493	798	607	69	$ 18,432

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The balances of loans as of September 30, 2011 by segment and evaluation method are summarized as follows:

(Dollars in thousands)	Loans individually evaluated for impairment	Loans collectively evaluated for impairment	Total Loans
Cmml real estate	$ 23,862	$ 610,367	$ 634,229
Cmml and industrial	10,311	294,704	305,015
Cmml construction	3,747	117,006	120,753
Residential	676	91,653	92,329
Home Equity		71,547	71,547
Consumer	17	3,524	3,541
Loans held for sale		3,600	3,600
Deferred Fees		(1,456)	(1,456)
Total loans	$ 38,613	$ 1,190,945	$ 1,229,558

The balances of loans as of December 31, 2010 by segment and evaluation method are summarized as follows:

(Dollars in thousands)	Loans individually evaluated for impairment	Loans collectively evaluated for impairment	Total Loans
Cmml real estate	$ 36,031	$ 559,044	$ 595,075
Cmml and industrial	8,780	266,049	274,829
Cmml construction	4,364	107,317	111,681
Residential	630	88,804	89,434
Home Equity		63,108	63,108
Consumer	19	4,209	4,228
Loans held for sale		6,408	6,408
Deferred Fees		(1,417)	(1,417)
Total loans	$ 49,824	$ 1,093,522	$ 1,143,346

(10) Stock-Based Compensation

The Company currently has three individual stock incentive plans. The Company has not changed the general terms and conditions of these plans from those disclosed in the Company s 2010 Annual Report on Form 10-K.

The Company s stock-based compensation expense includes restricted stock awards and stock option awards to officers, other employees and directors, and stock compensation in lieu of cash fees to directors. Total stock-based compensation expense was $249 thousand and $796 thousand for the three and nine months ended September 30, 2011, respectively, compared to $223 thousand and $664 thousand for the three and nine months ended September 30, 2010, respectively.

Stock Option Awards

The Company recognized stock-based compensation expense related to stock option awards of $63 thousand and $172 thousand for the three and nine months ended September 30, 2011, respectively, compared to $57 thousand and $182 thousand for the three and nine months ended September 30, 2010.

In the third quarter of 2011, 1,000 stock options awards were granted. There were none granted in the third quarter of 2010. There were a total of 83,075 and 63,775 stock option awards granted to employees in nine months ended September 30, 2011 and 2010, respectively. These options generally become exercisable at the rate of 25% per year on or about the anniversary date of the original grant. The 2011 awards allow for accelerated vesting of unvested options upon the date of retirement, if during the normal vesting period. The 2010 awards provide for accelerated vesting of the entire grant for those who are age 62 on the grant date or

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upon attaining age 62 during the normal vesting period. Vested options are only exercisable while the employee remains employed with the Bank and for a limited period thereafter, and these options expire seven years from the date of grant.

The Company utilizes the Black-Scholes option valuation model in order to determine the per share grant date fair value of option grants. The table below provides a summary of the options granted, fair value, the fair value as a percentage of the market value of the stock at the date of grant and the average assumptions used in the model for the options granted in the nine months ended September 30, 2011 and 2010.

		2011		**2010**
Options granted		83,075		63,775
Average assumptions used in the model:				
Expected volatility		45%		43%
Expected dividend yield		2.91%		2.98%
Expected life in years		5.5		5.5
Risk-free interest rate		2.17%		2.66%
Market price on date of grant	$	14.88	$	12.51
Per share weighted average fair value	$	5.28	$	4.35
Percentage of market value at grant date		35%		35%

Refer to note 9 Stock Based Compensation Plans in the Company s 2010 Annual Report on Form 10-K for a further description of the assumptions used in the valuation model.

Restricted Stock Awards

Stock-based compensation expense recognized in association with restricted stock awards amounted to $156 thousand and $497 thousand for the three and nine months ended September 30, 2011, respectively, compared to $143 thousand and $381 thousand for the three and nine months ended September 30, 2010, respectively.

During the first quarter of 2011, the Company granted 63,765 shares of common stock in the form of restricted stock awards comprised of 53,475 shares awarded to employees, generally vesting over four years, 3,500 shares awarded to an executive officer vesting immediately, and 6,790 shares awarded to directors vesting over two years. The grant date fair value of the restricted stock awarded was $14.85 per share, which reflected the market value of the common stock on the grant date. During the third quarter of 2011, the Company granted 1,000 shares of restricted stock that vest over four years and had a grant date fair value of $17.00 per share, which reflected the market value of the common stock on the grant date. The unvested 2011 awards generally vest, in each case, in equal portions beginning on or about the first anniversary date of the award.

During the first quarter of 2010, the Company granted 77,963 shares of common stock in the form of restricted stock awards comprised of 70,475 shares awarded to employees, vesting over four years, and 7,488 shares awarded to directors vesting over two years. The grant date fair value of the restricted stock awarded was $12.51 per share, which reflects the market value of the common stock on the grant date. The 2010 awards generally vest, in each case, in equal portions beginning on or about the first anniversary date of the award.

The restricted stock awards allow for the receipt of dividends, and the voting of all shares, whether or not vested, throughout the vesting periods.

If a grantee s employment or other service relationship, such as service as a director, is terminated for any reason, then any shares of restricted stock or stock options granted that have not vested as of the time of such termination must be forfeited, unless the Compensation Committee or the Board of Directors, as the case may be, waives such forfeiture requirement, or in the case of the 2011 awards, the employee meets certain retirement criteria.

Stock in Lieu of Directors Fees

In addition to restricted stock awards discussed above, the members of the Company s Board of Directors may opt to receive newly issued shares of the Company s common stock in lieu of cash compensation for attendance at Board and Board Committee meetings. Stock-based compensation expense related to Directors election to receive shares of common stock in lieu of cash fees for attendance at Board and Board committee meetings amounted to $30 thousand and $127 thousand for the three and nine months ended September 30, 2011, respectively, compared to $23 thousand and $101 thousand for the three and nine months

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ended September 30, 2010. In January 2011, 12,046 shares of common stock were issued to directors in lieu of cash fees related to the 2010 annual directors stock-based compensation expense of $134 thousand.

(11) Supplemental Retirement Plan and Other Postretirement Benefit Obligations

Supplemental Retirement Plan (SERPs)

The Company has salary continuation agreements with two of its executive officers, and one former executive officer, who currently works on a part time basis. These salary continuation agreements provide for a predetermined fixed-cash supplemental retirement benefit, the amount subject to vesting requirements, to be provided for a period of 20 years after the individual reaches a defined retirement age. Each officer has attained their individually defined retirement age and all participants are fully vested under the plan.

The following table illustrates the net periodic benefit cost for the SERPs for the periods indicated:

	Three months ended September 30,		Nine months ended September 30,	
(Dollars in thousands)	**2011**	**2010**	**2011**	**2010**
Service Cost	$	$	$	$ 55
Interest Cost	43	46	128	138
Net periodic benefit cost	$ 43	$ 46	$ 128	$ 193

Benefits paid amounted to $69 thousand and $207 thousand for the three and nine months ended September 30, 2011, respectively, compared to $69 thousand and $183 thousand for the three and nine months ended September 30, 2010, respectively. The Company anticipates accruing an additional $43 thousand to the plan during the remainder of 2011.

Bank Owned Life Insurance

The Company has purchased bank-owned life insurance (BOLI) on certain senior and executive officers. The cash surrender value carried on the balance sheet at September 30, 2011 and December 31, 2010 amounted to $14.8 million and $14.4 million, respectively. There are no associated surrender charges under the outstanding policies.

Supplemental Life Insurance

For certain senior and executive officers on whom the Company owns BOLI, the Company has provided supplemental life insurance which provides a death benefit to the officer s designated beneficiaries.

The following table illustrates the net periodic post retirement benefit cost for the supplemental life insurance plans for the periods indicated:

	Three months ended September 30,		Nine months ended September 30,	
(Dollars in thousands)	**2011**	**2010**	**2011**	**2010**
Service Cost	$ 4	$ (11)	$ 11	$ (32)
Interest Cost	18	18	54	52
Actuarial Gain/Loss			(19)	
Net periodic post retirement benefit cost	$ 22	$ 7	$ 46	$ 20

(12) Accounting for Income Taxes

The Company uses the asset and liability method of accounting for income taxes. Under this method, deferred tax assets and liabilities are recognized for the future tax attributable to differences between the financial statement carrying amounts and the tax basis of assets and liabilities. The deferred tax assets and liabilities are reflected at currently enacted income tax rates applicable to the period in which the deferred tax assets or liabilities are expected to be realized or settled. As changes in tax laws or rates are enacted, deferred tax assets and liabilities will be adjusted accordingly through the provision for income taxes.

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ENTERPRISE BANCORP, INC.

Notes to the Unaudited Consolidated Financial Statements

The Company s policy is to classify interest resulting from underpayment of income taxes as income tax expense in the first period the interest would begin accruing according to the provisions of the relevant tax law. The Company classifies penalties resulting from underpayment of income taxes as income tax expense in the period for which the Company claims or expects to claim an uncertain tax position or in the period in which the Company s judgment changes regarding an uncertain tax position.

The Company did not have any unrecognized tax benefits accrued as income tax liabilities or receivables or as deferred tax items at September 30, 2011. The Company s tax years beginning after December 31, 2005 are open to federal and state income tax examinations.

(13) Fair Value Measurements

The Financial Accounting Standard Board (FASB) defines the fair value of an asset or liability to be the price which a seller would receive in an orderly transaction between market participants (an exit price) and also establishes a fair value hierarchy segregating fair value measurements using three levels of inputs: (Level 1) quoted market prices in active markets for identical assets or liabilities; (Level 2) significant other observable inputs, including quoted prices for similar items in active markets, quoted prices for identical or similar items in markets that are not active, inputs such as interest rates and yield curves, volatilities, prepayment speeds, credit risks and default rates which provide a reasonable basis for fair value determination or inputs derived principally from observed market data; (Level 3) significant unobservable inputs for situations in which there is little, if any, market activity for the asset or liability. Unobservable inputs must reflect reasonable assumptions that market participants would use in pricing the asset or liability, which are developed on the basis of the best information available under the circumstances.

The following tables summarize significant assets and liabilities carried at fair value at the dates specified: