

CHICOPEE BANCORP, INC.  
Form 10-K  
March 12, 2015

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-K

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

For the fiscal year ended December 31, 2014

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

Commission File Number: 000-51996

CHICOPEE BANCORP, INC.  
(Exact name of registrant as specified in its charter)

Massachusetts  
(State or other jurisdiction of  
incorporation or organization)

20-4840562  
(I.R.S. Employer  
Identification No.)

70 Center Street, Chicopee, Massachusetts  
(Address of principal executive offices)

01013  
(Zip Code)

Registrant's telephone number: (413) 594-6692

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

| Title of each class        | Name of each exchange on which registered |
|----------------------------|---|
| Common Stock, no par value | NASDAQ Global Market                      |

Securities registered pursuant to Section 12(g) of the Act:  
None

Indicate by check mark whether the registrant is a well known seasoned issuer, as defined in Rule 405 of the Securities Act. YES\_\_\_ NO X

Indicate by check mark whether the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. YES NO X

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

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

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Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. \_\_\_

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 "accelerated filer," "large accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12(b)-2 of the Exchange Act).

YES \_\_\_ NO

On June 30, 2014, the aggregate market value of the voting and non-voting common equity held by non-affiliates was \$85,587,625

The number of shares of Common Stock outstanding as of March 10, 2015 was 5,270,670.

#### DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Proxy Statement for our Annual Meeting of Stockholders, to be held on May 27, 2015, are incorporated by reference in Part III of this Annual Report on Form 10-K.

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## PART I

### Item 1. Business.

#### General

Chicopee Bancorp, Inc. (the “Company” or “Chicopee Bancorp”), a Massachusetts corporation, was formed on March 14, 2006 by Chicopee Savings Bank (the “Bank” or “Chicopee Savings Bank”) to become the holding company for the Bank upon completion of the Bank’s conversion from a mutual savings bank to a stock savings bank. The conversion and the offering were completed on July 19, 2006.

The Bank, a Massachusetts stock savings bank, was organized in 1845 under the name Cabot Savings Bank and adopted its present name in 1854. The Bank is a full-service, community oriented financial institution offering products and services to individuals and businesses through nine offices located in Western Massachusetts. The Bank’s deposits are insured by the Federal Deposit Insurance Corporation (“FDIC”) and Depositor’s Insurance Fund (“DIF”) of Massachusetts. The Bank is also a member of the Federal Home Loan Bank of Boston (“FHLB”) and is regulated by the FDIC and the Massachusetts Division of Banks. Chicopee Savings Bank’s business consists primarily of making loans to its customers, including residential mortgages, commercial real estate loans, commercial loans, consumer loans and home equity loans, and investing in a variety of investment securities. The Bank funds these lending and investment activities with deposits from the general public, funds generated from operations and borrowings. The Bank also sells residential one-to-four family real estate loans to the secondary market to reduce interest rate risk. The Bank’s revenues are derived from the generation of interest and fees on loans, interest and dividends on investment securities, fees from its retail banking operation, and investment management. The Bank’s primary sources of funds are deposits, principal and interest payments on loans and investments, advances from the FHLB and proceeds from loan sales. The Bank also provides access to insurance and investment products through its Financial Services Division.

#### Available Information

The Company’s website is [www.chicopeesavings.com](http://www.chicopeesavings.com). The Company makes available free of charge, on or through its website, its annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and any amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, as soon as reasonably practicable after the Company electronically files such material with, or furnishes it to, the Securities and Exchange Commission. Information on the Company’s website shall not be considered part of this Form 10-K.

#### Market Area

Chicopee Savings Bank is headquartered in Chicopee, Massachusetts. The Bank’s primary lending and deposit market areas include Hampden and Hampshire Counties in Western Massachusetts. Chicopee is located at the “Crossroads of New England”, the intersection of Interstate 91 and the Massachusetts Turnpike. Interstate 91 is the major north-south highway and Interstate 90 is the major east-west highway that crosses Massachusetts. The city is also bisected by several secondary highways, which include Routes 391, 116, 33 and 141. These roadways provide good access to major highways and centers of employment. Chicopee is located approximately 90 miles west of Boston, Massachusetts, 80 miles southeast of Albany, New York and 30 miles north of Hartford, Connecticut.

Chicopee is an urban community, which serves as the home of the Westover Air Force Base, which is the nation’s largest Air Force Reserve Base and is a key part of the local economy. More than 2,700 military and civilian workers are assigned to Westover’s 43<sup>rd</sup> Military Airlift Wing. A diversified mix of industry groups also operate within Hampden and Hampshire County, including manufacturing, health care, higher education, whole sale retail trade and

service. The economy of our primary market area has benefited from the presence of large employers such as Baystate Health, Big Y Supermarkets, University of Massachusetts, Mass Mutual Financial Group, Hasbro Games, Peter Pan Bus Lines, Friendly's Ice Cream Corporation, Sisters of Providence Health Systems, Westover Air Force Base, Smith and Wesson, Yankee Candle and Verizon. Other employment and economic activity is provided by financial institutions, nine other colleges and universities, eight other hospitals, and a variety of wholesale and retail trade business. Our market also enjoys a strong tourism business with attractions such as the Eastern States Exposition called the Big E, the largest fair in the northeast, the Basketball Hall of Fame and Six Flags New England.

#### Competition

We face significant competition in attracting deposits and loans. Our most direct competition for deposits has historically come from the several financial institutions and credit unions operating in our market area and, to a lesser extent, from other financial service companies such as brokerage firms and insurance companies. We also face competition for depositors' funds from money market funds, mutual funds and other corporate and government securities. At June 30, 2014, which is the most recent

date for which data is available from the FDIC, we held approximately 4.87% of the deposits in Hampden County, which was the 8<sup>th</sup> largest market share out of the 19 banks and thrifts with offices in Hampden County. This data does not include deposits held by one of our primary competitors, credit unions, which, as tax-exempt organizations, are able to offer higher rates on deposits than banks. There are 15 credit unions headquartered in Hampden County, some of the larger of which are headquartered in Chicopee, Massachusetts. In addition, banks owned by large super-regional bank holding companies such as Bank of America Corporation, Santander Bank, N.A., Citizens Financial Group, First Niagara Financial Group, Inc., and TD Bank, Inc. also operate in our market area. These institutions are significantly larger than us and, therefore, have greater resources.

Our competition for loans comes primarily from financial institutions in our market areas, and, to a lesser extent, from other financial service providers such as mortgage companies and mortgage brokers. Competition for loans also comes from the increasing number of non-depository financial service companies entering the mortgage market such as insurance companies, securities companies and specialty finance companies.

We expect competition to increase in the future as a result of legislative, regulatory and technological changes and the continuing trend of consolidation in the financial services industry. Technological advances, for example, have lowered the barriers to market entry, allowed banks and other lenders to expand their geographic reach by providing services over the Internet and made it possible for non-depository institutions to offer products and services that traditionally have been provided by banks. Changes in federal laws permit affiliation among banks, securities firms and insurance companies, which promotes a competitive environment in the financial services industry. Competition for deposits and the origination of loans could limit our future growth.

#### Lending Activities

General. The Company's loan portfolio totaled \$523.7 million at December 31, 2014 compared to \$489.3 million at December 31, 2013, representing 81.9% and 83.3% of total assets, respectively. In its lending activity, the Company originates one-to-four family real estate loans, commercial real estate loans, residential and commercial construction loans, commercial and industrial loans, home equity lines-of-credit, fixed rate home equity loans and other consumer loans. The Company does not originate loans that generally target borrowers with weakened credit histories typically characterized by payment delinquencies, previous charge-offs, judgments, bankruptcies, or borrowers with questionable repayment capacity as evidenced by low credit scores or high debt-burden ratios. While the Company makes loans throughout Massachusetts, most of its lending activities are concentrated in Hampden and Hampshire counties. Loans originated totaled \$140.5 million in fiscal year 2014 and \$187.6 million in 2013, including residential mortgage loans sold to the secondary market of \$4.7 million and \$26.4 million, respectively. Servicing rights are retained on all loans originated and sold into the secondary market.

Residential Real Estate Loans. At December 31, 2014 and 2013, the residential real estate loan portfolio totaled \$118.7 million and \$112.5 million, or 22.7% and 23.0% of the total loan portfolio, with an average yield of 3.87% and 4.09%, respectively. Residential real estate loans originated totaled \$36.2 million and \$79.3 million in 2014 and 2013, respectively, which includes loans sold to the secondary market of \$4.7 million and \$26.4 million in 2014 and 2013, respectively. Of the residential real estate loans outstanding at December 31, 2014, \$104.3 million, or 87.9%, were adjustable rate loans. Total loans serviced for others as of December 31, 2014 and 2013 were \$91.3 million and \$97.6 million, respectively. Residential real estate loans enable borrowers to purchase or refinance existing homes, most of which serve as the primary residence of the owner. We offer fixed-rate and adjustable-rate loans with terms up to 30 years. Borrower demand for adjustable-rate loans versus fixed-rate loans is a function of the level of interest rates, the expectations of changes in the level of interest rates, and the difference between the interest rates and loan fees offered for fixed-rate mortgage loans and the initial period interest rates and loan fees for adjustable-rate loans. The relative amount of fixed-rate mortgage loans and adjustable-rate mortgage loans that can be originated at any time is largely determined by the demand for each in a competitive environment. The loan fees, interest rates and other provisions of

mortgage loans are determined by the demand for each in a competitive environment.

We offer fixed-rate residential real estate loans secured by one-to-four family residences with terms between 10 and 30 years. Management establishes the loan interest rates based on market conditions. Interest rates and payments on our adjustable-rate mortgage loans generally adjust annually after an initial fixed period that ranges from one to ten years. Interest rates and payments on our adjustable-rate loans generally are adjusted to a rate typically equal to 3.50 percentage points above the one-year constant maturity Treasury index. The maximum amount by which the interest rate on our adjustable-rate mortgage loans may be increased or decreased is generally 2 percentage points per adjustment period and the lifetime interest rate cap is generally 6 percentage points over the initial interest rate of the loan. We also offer adjustable-rate mortgage loans that adjust every three years after an initial three-year fixed period and adjustable-rate mortgage loans that adjust every five years after an initial six-year fixed period. Interest rates and payments on these adjustable-rate loans generally are adjusted to a rate typically equal to 3.50 percentage points above the three- and five-year constant maturity Treasury index.



The largest owner-occupied residential real estate loan was \$1.7 million and was performing according to its original terms as of December 31, 2014.

All adjustable-rate mortgage loans are underwritten taking the indexed rate into consideration at each adjustment period until the full cap is reached. A Mass Attorney General Important Disclosure (MA Chapter 93A-Determining Affordability of ARM Loans) is completed for each adjustable rate mortgage request, which calculates the overall debt to income based on the initial principal and interest payment along with real estate taxes, insurance, and other monthly payments due from the borrower and also includes the repricing of these payments at each adjustment up to the maximum caps allowed under the note. This process minimizes the risk of qualification at the time the loan reaches the maximum rate for that product.

Adjustable rate mortgage loans help decrease the risk associated with changes in market interest rates by periodically repricing. However, upward adjustment of interest rates is limited by the maximum periodic and lifetime interest rate adjustments permitted by our loan documents. In addition, adjustable rate mortgage loans may increase credit risk because, as interest rates increase, interest payments on adjustable rate loans increase, which increases the potential for defaults by our borrowers. See "Loan Underwriting Risks" below.

While one-to-four-family residential real estate loans are normally originated with up to 30-year terms, such loans typically remain outstanding for substantially shorter periods because borrowers often prepay their loans in full upon sale of the property pledged as security or upon refinancing the original loan. Therefore, average loan maturity is a function of, among other factors, the level of purchase and sale activity in the real estate market, prevailing interest rates and the interest rates payable on outstanding loans.

We generally do not make conventional loans with loan-to-value ratios exceeding 95% at the time the loan is originated. Conventional loans with loan-to-value ratios in excess of 80% generally require private mortgage insurance or additional collateral. We require all properties securing mortgage loans to be appraised by a board-approved independent appraiser. We generally require title insurance on all first mortgage loans. Borrowers must obtain hazard insurance, and flood insurance for loans on properties located in a flood zone, before closing the loan.

In an effort to provide financing for first-time home buyers, we offer 30-year fixed-rate residential mortgage loans and 10/1 adjustable rate mortgage loans with loan-to-value ratios up to 97%. We offer mortgage loans through this program to qualified individuals and originate the loans using underwriting guidelines as set forth by the Company.

**Commercial Real Estate Loans.** At December 31, 2014 and 2013, commercial real estate loans totaled \$249.6 million and \$211.2 million, or 47.7% and 43.1% of the total loan portfolio, with an average yield of 4.75% and 5.24%, respectively. This yield calculation includes commercial construction and residential investment loan balances and interest income. Commercial real estate loans originated totaled \$66.6 million and \$87.4 million in 2014 and 2013, respectively. Our commercial real estate and residential investment loans are generally secured by apartment buildings and properties used for business purposes such as office buildings, industrial facilities and retail facilities. In addition to originating these loans, we also participate in loans with other financial institutions located primarily in Massachusetts.

We originate a variety of fixed- and adjustable-rate commercial real estate and residential investment loans for terms up to 25 years. Interest rates and payments on our adjustable-rate loans adjust every one to ten years and generally are adjusted to a rate equal to 2.0% to 3.0% above the corresponding U.S. Treasury rate or FHLB rate. Most of our adjustable-rate commercial real estate and residential investment loans adjust every five years. There are no adjustment period or lifetime interest rate caps. Loan amounts generally do not exceed 80% of the property's appraised value at the time the loan is originated.

At December 31, 2014, our largest commercial real estate loan was \$9.1 million and was secured by multiple warehouse/industrial buildings in Westfield, Massachusetts. This loan was performing according to the original terms at December 31, 2014.

At December 31, 2014, our exposure to commercial real estate and commercial business loan participations purchased and sold totaled \$18.2 million and \$19.0 million, respectively. The properties securing these loans are located primarily in Massachusetts.

We also originate land loans primarily to local contractors and developers for making improvements on approved building lots. Such loans are generally written with a maximum 75% loan-to-value ratio based upon the appraised value or purchase price, whichever is less, for a term of up to three years. Interest rates on our land loans are fixed for three years. At December 31, 2014, we had eleven land loans totaling \$480,000.

Construction Loans. At December 31, 2014 and 2013, the Company had \$43.9 million and \$44.6 million of construction loans outstanding, representing 8.4% and 9.2% of the total loan portfolio, with an average yield of 4.12% and 4.47%, respectively. We originate fixed-rate and adjustable-rate loans to individuals and builders to finance the construction of residential dwellings.

We also make construction loans for commercial development projects, including apartment buildings, condominiums, small industrial buildings and retail and office buildings. Our construction loans generally provide for the payment of interest only during the construction phase, which is usually 12 to 36 months. At the end of the construction phase, the loan generally converts to a permanent mortgage loan. Loans generally can be made with a maximum loan to value ratio of 80% at the time the loan is originated. Before making a commitment to fund a construction loan, we require an appraisal of the property by an independent licensed appraiser. We also will require an inspection of the property before disbursement of funds during the term of the construction loan.

At December 31, 2014, our largest outstanding residential construction loan was \$1.1 million, of which \$950,000 was outstanding. At December 31, 2014, our largest outstanding commercial construction loan was \$7.9 million, of which \$7.0 million was outstanding for the development of an office building. These loans were performing in accordance with their original terms at December 31, 2014.

**Commercial and Industrial Loans.** The Company originated \$30.4 million and \$38.2 million in commercial and industrial loans in 2014 and 2013, respectively. As of December 31, 2014 and 2013, the Company had \$74.3 million and \$86.5 million in commercial and industrial loans, representing 14.1% and 17.7% of the total loan portfolio, with an average yield of 3.99% and 4.23%, respectively. We make commercial business loans primarily in our market area to a variety of professionals, sole proprietorships and small businesses. Commercial lending products include term loans, revolving lines of credit and letters of credit loans. Commercial loans and lines of credit are made with either variable or fixed rates of interest. Variable rates are based on the prime rate as published in The Wall Street Journal, plus a margin. Fixed-rate business loans are generally indexed to a corresponding U.S. Treasury rate, plus margin, or FHLB, plus margin. The Company generally does not make unsecured commercial and industrial loans.

When making commercial and industrial loans, we consider the financial statements of the borrower, our lending history with the borrower, the debt service capabilities of the borrower, the projected cash flows of the business and the value of the collateral, primarily accounts receivable, inventory and equipment, and are supported by personal guarantees. Depending on the collateral used to secure the loans, commercial loans are made in amounts of up to 80% of the value of the collateral securing the loan. The collateral securing commercial and industrial loans may depreciate over time, may be difficult to appraise and may fluctuate in value. See "-Loan Underwriting Risks" below.

At December 31, 2014, our largest commercial term loan was a \$2.0 million loan secured by real estate located in East Longmeadow, Massachusetts, including all assets of the borrower. The loan was performing according to its original terms at December 31, 2014. Our largest lending exposure was a \$14.4 million commercial lending relationship, of which \$11.7 million was outstanding at December 31, 2014. The relationship consists of three separate entities each providing independent cash flow and were secured by the assets of the borrower, including all assets and commercial real estate. The loans were performing in accordance with their original terms at December 31, 2014.

**Consumer Loans.** The Company originated \$12.1 million and \$8.9 million of consumer loans, including home equity loans, in 2014 and 2013, respectively. At December 31, 2014 and 2013, consumer loans outstanding totaled \$37.2 million and \$34.5 million, or 7.1% and 7.0% of the total loan portfolio, with an average yield of 3.67% and 3.82%, respectively. We offer a variety of consumer loans, primarily home equity loans and lines of credit, and, to a much lesser extent, loans secured by automobiles, recreational vehicles, pools and spas and home improvement loans.

The procedures for underwriting consumer loans include an assessment of the applicant's payment history on other debts and ability to meet existing obligations and payments on the proposed loan. Although the applicant's creditworthiness is a primary consideration, the underwriting process also includes a comparison of the value of the collateral, if any, to the proposed loan amount.

We generally offer home equity loans with a maximum combined loan to value ratio of 80% and home equity lines of credit with a maximum combined loan to value ratio of 80%. Home equity lines of credit have adjustable rates of interest that are indexed to the prime rate as reported in The Wall Street Journal. Home equity loans have fixed interest rates and terms that range from five to twenty years.

We offer automobile and recreational vehicle loans secured by new and used vehicles. These loans have fixed interest rates and generally have terms up to six years for new automobiles, five years for used automobiles and four years for recreational vehicles. We also offer fixed-rate pool and spa loans up to \$10,000 for terms up to five years.

#### Loan Underwriting Risks

Adjustable-Rate Loans. While we anticipate adjustable-rate loans will better offset the potential adverse effects of an increase in interest rates as compared to fixed-rate mortgages, the increased mortgage payments required of adjustable-rate loan

borrowers in a rising interest rate environment could cause an increase in delinquencies and defaults. The marketability of the underlying property also may be adversely affected in a high interest rate environment. In addition, although adjustable-rate mortgage loans help make our loan portfolio more responsive to changes in interest rates, the extent of this interest sensitivity is limited by the annual and lifetime interest rate adjustment limits.

**Residential Real Estate.** The Company's primary residential real estate lending market areas include Hampden and Hampshire Counties in Western Massachusetts. If real estate prices decline, the value of real estate collateral securing our loans will be reduced. Our ability to recover defaulted loans by foreclosing and selling the real estate collateral would then be diminished, and we would be more likely to incur financial losses on defaulted loans. Real estate values and real estate markets are generally affected by changes in national, regional or local economic conditions, fluctuations in interest rates and the availability of loans to potential purchasers, changes in tax laws, regulations and acts of nature. Residential real estate loans are dependent on the borrower's continuing financial stability and, therefore, are more likely to be adversely affected by job loss, divorce, illness or personal bankruptcy. In addition, the application of various federal and state laws, including foreclosure, bankruptcy and insolvency laws may limit the amount that can be recovered on such loans.

**Commercial Real Estate.** Loans secured by commercial real estate and residential investment real estate generally have larger balances and involve a greater degree of risk than one-to four-family residential mortgage loans. Of primary concern in commercial real estate and residential investment lending is the borrower's creditworthiness and the feasibility and cash flow potential of the project. Payments on loans secured by income properties often depend on successful operation and management of the properties. As a result, repayment of such loans may be subject to a greater extent than residential real estate loans to adverse conditions in the real estate market or the economy. To monitor cash flows on income properties, we generally require borrowers and loan guarantors, if any, to provide annual financial statements and/or tax returns on commercial real estate and residential investment loans. In reaching a decision on whether to make a commercial real estate and residential investment loan, we consider the net operating income of the property, the borrower's expertise, credit history and profitability and the value of the underlying property. We have generally required that the properties securing these real estate loans have debt service coverage ratios (the ratio of earnings before debt service to debt service) of at least 1.20x; however, this ratio can be lower depending on the amount and type of collateral. Environmental surveys and inspections are obtained when circumstances suggest the possibility of the presence of hazardous materials.

We underwrite all loan participations to our own underwriting standards. In addition, we also consider the financial strength and reputation of the lead lender. To monitor cash flows on loan participations, we require the lead lender to provide annual financial statements for the borrower. Generally, we also conduct an annual internal loan review for loan participations.

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

**Commercial and Industrial Loans.** Unlike residential mortgage loans, which generally are made on the basis of the borrower's ability to make repayment from his or her employment or other income, and which are secured by real

property the value of which tends to be more easily ascertainable, commercial and industrial loans are of higher risk and typically are made on the basis of the borrower's ability to make repayment from the cash flow of the borrower's business. As a result, the availability of funds for the repayment of commercial and industrial loans may depend substantially on the success of the business itself. Further, any collateral securing such loans may depreciate over time, may be difficult to appraise and may fluctuate in value.

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

**Loan Originations, Purchases, and Sales.** Loan originations come from a number of sources. The primary sources of loan originations are existing customers, walk-in traffic, advertising and referrals from customers. We advertise on television, on

the radio and in newspapers that are widely circulated in Hampden and Hampshire Counties, both in Massachusetts. Accordingly, because our rates are competitive, we attract loans from throughout Hampden and Hampshire Counties. We occasionally purchase participation interests in loans to supplement our origination efforts.

We generally originate loans for our portfolio; however, we generally sell, prior to funding, to the secondary market all newly originated conforming fixed-rate, 10- to 30-year one-to-four-family residential real estate loans. Our decision to sell loans is based on prevailing market interest rate conditions and interest rate risk management. Generally, loans are sold to Freddie Mac with loan servicing retained. In addition, we sell participation interests in commercial real estate loans to local financial institutions, primarily on the portion of loans that exceed our borrowing limits.

**Loan Approval Procedures and Authority.** Our lending activities follow written, non-discriminatory, underwriting standards and loan origination procedures established by our Board of Directors and management. Our Board of Directors has granted loan approval authority to certain officers up to prescribed limits, depending on the officer's experience, the type of loan and whether the loan is secured or unsecured. Loans in excess of the Senior Lending Officer limits (\$500,000 for real estate loans, secured consumer loans, and secured and unsecured commercial loans; and \$100,000 for unsecured consumer loans.) must be authorized by the President and the Executive Vice President of Lending up to 1.5 times the Senior Lending Officer lending limits. All other extensions of credit exceeding such limitations require the approval of the executive committee, a committee of the Board of Directors of the Bank.

**Loans to One Borrower.** The maximum amount that we may lend to one borrower and the borrower's related entities generally is limited, by statute, to 20% of our stated capital and reserves. At December 31, 2014, our general regulatory limit on loans to one borrower was \$15.7 million. At December 31, 2014, our internal lending limit to one borrower was \$8.0 million, unless approved in excess of this amount by the executive committee of the Board of Directors. Our largest lending exposure was a \$14.4 million commercial lending relationship, of which \$11.7 million was outstanding at December 31, 2014. The relationship consists of three separate entities each providing independent cash flow and were secured by the assets of the borrower, including all assets and commercial real estate. The loans were performing in accordance with their original terms at December 31, 2014.

**Loan Commitments.** We issue commitments for fixed- and adjustable-rate mortgage loans conditioned upon the occurrence of certain events. Commitments to originate mortgage loans are legally binding agreements to lend to our customers. Generally, our mortgage loan commitments expire after 30 days.

#### Investment Activities

We have legal authority to invest in various types of liquid assets, including marketable equity securities, U.S. Treasury obligations, securities of various government sponsored enterprises and municipal governments, deposits at the FHLB and certificates of deposit of federally insured institutions. We are also required to maintain an investment in FHLB stock. While we have the authority under applicable law to invest in derivative securities, our investment policy does not permit us to do so and we had no investments in derivative securities at December 31, 2014.

At December 31, 2014, our investment portfolio consisted primarily of tax-exempt industrial revenue bonds, and to a lesser extent, certificates of deposit, collateralized mortgage obligations, and investment-grade marketable equity securities.

Our investment objectives are to provide and maintain liquidity, to establish an acceptable level of interest rate and credit risk, to provide an alternate source of low-risk investments when demand for loans is weak and to generate a favorable return. The Board of Directors of the Bank has the overall responsibility for approval of our investment policy. The Treasurer is responsible for the implementation of the investment policy. Individual investment

transactions are reviewed and approved by our executive committee monthly while portfolio composition and performance are reviewed at least annually by the Board of Directors of the Bank.

Our Chief Financial Officer and Treasurer is responsible for ensuring that the investment policy is followed and that all securities are considered prudent for investment.

#### Deposit Activities and Other Sources of Funds

General. Deposits, borrowings and loan repayments are the major sources of our funds for lending and other investment purposes. Loan repayments are a relatively stable source of funds, while deposit inflows and outflows and loan prepayments are significantly influenced by general interest rates and money market conditions.

Deposits. Substantially all of our depositors are residents of the Commonwealth of Massachusetts. Deposits are attracted, by advertising and through our website, from within our market areas through the offering of a broad selection of deposit instruments, including non-interest-bearing demand accounts (such as checking accounts), interest-bearing accounts (such as NOW and money



market deposit accounts), regular savings accounts (such as passbook accounts) and certificates of deposit. At December 31, 2014, we did not utilize brokered deposits. Deposit account terms vary according to the minimum balance required, the time periods the funds must remain on deposit and the interest rate, among other factors. In determining the terms of our deposit accounts, we consider the rates offered by our competition, our liquidity needs, profitability to us, matching deposit and loan products and customer preferences and concerns. We generally review our deposit mix and pricing weekly. Our current strategy is to offer competitive rates and price the deposit products depending on our needs for funds and rates on borrowings. Deposit accounts at the Bank are insured by the Deposit Insurance Fund of the FDIC, generally up to a maximum of \$250,000 for each separately insured depositor and up to a maximum of \$250,000 for self-directed retirement accounts. In addition, as a Massachusetts-chartered savings bank, Chicopee Savings Bank is required to be a member of DIF, a corporation that insures savings bank deposits in excess of federal deposit insurance coverage. The combination of FDIC and DIF insurance provides customers of Massachusetts-chartered savings banks with full deposit insurance on all their deposits.

**Borrowed Funds.** We may utilize advances from the FHLB to supplement our supply of investable funds. The FHLB functions as a central reserve bank providing credit for its member financial institutions. As a member, we are required to own capital stock in the FHLB and are authorized to apply for advances on the security of such stock and certain of our whole first real estate loans and other assets (principally securities which are obligations of, or guaranteed by, the United States), provided certain standards related to creditworthiness have been met. Advances are made under several different programs, each having its own interest rate and range of maturities. Depending on the program, limitations on the amount of advances are based either on a fixed percentage of an institution's net worth or on the FHLB's assessment of the institution's creditworthiness.

Securities sold under agreements to repurchase are customer deposits that are invested overnight in U.S. Treasury securities. The customers, predominantly commercial customers, set a predetermined balance and deposits in excess of that amount are transferred into the repurchase account from each customer's checking account. These types of accounts are often referred to as sweep accounts.

#### Financial Services

We have a partnership with a third-party registered broker-dealer, Linsco/Private Ledger ("LPL"). Through LPL, we offer customers a range of non-deposit investment products, including mutual funds, debt, equity and government securities, retirement accounts, insurance products and fixed and variable annuities. We receive a portion of the commissions generated by LPL from sales to customers. For the years ended December 31, 2014, 2013 and 2012, we received fees of \$374,000, \$320,000 and \$312,000, respectively, through our relationship with LPL.

#### Subsidiary Activities

Chicopee Bancorp, Inc. conducts its principal business activities through its two wholly-owned subsidiaries: Chicopee Savings Bank and Chicopee Funding Corporation.

**Chicopee Funding Corporation.** Chicopee Funding Corporation was incorporated in Massachusetts in 2006. Chicopee Bancorp, Inc. contributed funds to Chicopee Funding Corporation to enable it to make a 20-year loan to the employee stock ownership plan to allow it to purchase shares of the Company's common stock as part of the initial public offering. The Employee Stock Ownership Plan purchased 595,149 shares in the initial public offering, or 8% of the 7,439,368 shares issued in connection with the Bank's mutual-to-stock conversion.

The following are descriptions of Chicopee Savings Bank's wholly-owned subsidiaries:

CSB Colts, Inc. CSB Colts, Inc. was formed in 2003 as a Massachusetts corporation to engage in buying, selling and holding securities on its own behalf. At December 31, 2014, CSB Colts had total assets of \$33.5 million consisting primarily of tax-exempt industrial revenue bonds. CSB Colts' net income for the year ended December 31, 2014 was \$1.5 million. As a Massachusetts securities corporation, the income earned on CSB Colts' investment securities is subject to a lower state tax rate than that assessed on income earned on investment securities maintained at Chicopee Savings Bank.

CSB Investment Corp. CSB Investment Corp. was formed in 2003 as a Massachusetts corporation to engage in buying, selling and holding securities on its own behalf. At December 31, 2014, CSB Investment had total assets of \$679,000 consisting primarily of collateralized mortgage obligations and marketable equity securities. CSB Investment's net income for the year ended December 31, 2014 was \$59,000. As a Massachusetts securities corporation, the income earned on CSB Investment's investment securities is subject to a lower state tax rate than that assessed on income earned on investment securities maintained at Chicopee Savings Bank.

Cabot Realty L.L.C. Cabot Realty L.L.C. was formed as a Massachusetts limited liability company to hold other real estate owned (“OREO”). At December 31, 2014, Cabot Realty had total assets of \$1.7 million consisting primarily of cash and cash equivalents of \$535,000 and OREO of \$1.1 million. Cabot Realty’s net loss for the year ended December 31, 2014 was \$205,000. Cabot Management Corporation, a wholly owned subsidiary of Chicopee Savings Bank, has a 1% membership interest in, and Chicopee Savings Bank has a 99% membership interest in, Cabot Realty.

Cabot Management Corporation. Cabot Management Corporation was formed in 1979 as a Massachusetts corporation to acquire and manage interests in real property and to acquire, construct, rehabilitate, lease, finance and dispose of housing facilities. Cabot Management is currently inactive and at December 31, 2014 had total assets of \$17,000.

#### Personnel

As of December 31, 2014, we had approximately 108 full-time employees and 22 part-time employees, none of whom is represented by a collective bargaining unit. We believe we have a good relationship with our employees.

#### Regulation and Supervision

##### General

Chicopee Savings Bank is a Massachusetts-chartered savings bank and the wholly-owned subsidiary of Chicopee Bancorp, a Massachusetts corporation. Chicopee Savings Bank’s deposits are insured up to applicable limits by the FDIC, and by the DIF for amounts in excess of the FDIC insurance limits. Chicopee Savings Bank is subject to extensive regulation by the Massachusetts Commissioner of Banks, as its chartering agency, and by the FDIC, its primary federal regulator and deposit insurer. Chicopee Savings Bank is required to file reports with, and is periodically examined by, the FDIC and the Massachusetts Commissioner of Banks concerning its activities and financial condition and must obtain regulatory approvals prior to entering into certain transactions, including, but not limited to, mergers with or acquisitions of other financial institutions. As a registered bank holding company, Chicopee Bancorp is regulated by the Board of Governors of the Federal Reserve System, or the “Federal Reserve Board.”

The regulatory and supervisory structure establishes a comprehensive framework of activities in which an institution can engage and is intended primarily for the protection of depositors and the deposit insurance funds, rather than for the protection of stockholders and creditors. The regulatory structure also gives the regulatory authorities extensive discretion in connection with their supervisory and enforcement activities and examination policies, including policies concerning the establishment of deposit insurance assessment fees, classification of assets and establishment of adequate loan loss reserves for regulatory purposes. Any change in such regulatory requirements and policies, whether by the Massachusetts legislature, the Massachusetts Commissioner of Banks, the FDIC, the Federal Reserve Board or Congress, could have a material adverse impact on the financial condition and results of operations of Chicopee Bancorp and Chicopee Savings Bank. As is further described below, the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act”), has significantly changed the bank regulatory structure and may affect the lending, investment and general operating activities of depository institutions and their holding companies.

Set forth below is a summary of certain material statutory and regulatory requirements that are applicable to Chicopee Savings Bank and Chicopee Bancorp. This description of statutes and regulations is not intended to be a complete description of such statutes and regulations and their effects on Chicopee Savings Bank and Chicopee Bancorp.

##### The Dodd-Frank Act

The Dodd-Frank Act has significantly changed the bank regulatory structure and is affecting the lending and investment activities and general operations of depository institutions and their holding companies.

The Dodd-Frank Act required the Federal Reserve Board to establish minimum consolidated capital requirements for bank holding companies that are as stringent as those required for insured depository institutions; the components of Tier 1 capital will be restricted to capital instruments that are currently considered to be Tier 1 capital for insured depository institutions. In addition, the proceeds of trust preferred securities are excluded from Tier 1 capital unless such securities were issued prior to May 19, 2010 by bank or savings and loan holding companies with less than \$15 billion of assets. The legislation also established a floor for capital of insured depository institutions that cannot be lower than the standards in effect on July 21, 2010, and directed the federal banking regulators to implement new leverage and capital requirements within 18 months of that date. The revised capital regulations are effective January 1, 2015.

The Dodd-Frank Act also created a new Consumer Financial Protection Bureau with extensive powers to implement and enforce consumer protection laws. The Consumer Financial Protection Bureau has broad rulemaking authority for a wide range of consumer protection laws that apply to all banks and savings associations, among other things, including the authority to prohibit “unfair, deceptive or abusive” acts and practices. The Consumer Financial Protection Bureau has examination and enforcement authority over all banks and savings associations with more than \$10 billion in assets. Banks and savings associations with \$10 billion or less in assets will continue to be examined for compliance with federal consumer protection and fair lending laws by their applicable primary federal bank regulators.

The Dodd-Frank Act also broadened the base for FDIC insurance assessments. The FDIC was required to promulgate rules revising its assessment system so that it is based on the average consolidated total assets less tangible equity capital of an insured institution instead of deposits. That rule took effect April 1, 2011. The Dodd-Frank Act also permanently increased the maximum amount of deposit insurance for banks, savings institutions and credit unions to \$250,000 per depositor, retroactive to January 1, 2008, and provided non-interest bearing transaction accounts with unlimited deposit insurance through December 31, 2012.

The Dodd-Frank Act requires companies to give stockholders a non-binding vote on executive compensation and so-called “golden parachute” payments. The legislation also directed the Federal Reserve Board to promulgate rules prohibiting excessive compensation paid to bank holding company executives, regardless of whether the company is publicly traded.

The Dodd-Frank Act made many other changes in banking regulation. These include authorizing depository institutions, for the first time, to pay interest on business checking accounts, mandating that regulation be issued requiring originators of securitized loans to retain a percentage of the risk for transferred loans and establishing regulatory rate-setting for certain debit card interchange fees and establishing a number of reforms for mortgage originations.

In addition, the Consumer Financial Protection Bureau issued a rule implementing the “Ability to Pay” requirements of the Dodd-Frank Act. The regulations generally require lenders to make a reasonable, good faith determination as to a potential borrower’s ability to repay a residential mortgage loan. The final rule establishes a safe harbor for certain “Qualified Mortgages,” which contain certain features and terms deemed to make the loan less risky. The Ability to Repay final rules were effective January 10, 2014.

Many of the provisions of the Dodd-Frank Act were subject to delayed effective dates and the legislation required various federal agencies to promulgate numerous and extensive implementing regulations over a period of years. It is therefore difficult to predict at this time what the full impact the new legislation and implementing regulations will have on community banks such as Chicopee Savings Bank. Although the substance and scope of many of these regulations cannot be determined at this time, it is expected that the legislation and implementing regulations, particularly those provisions relating to the new Consumer Financial Protection Bureau, may increase operating and compliance costs.

#### Massachusetts Banking Laws and Supervision

General. As a Massachusetts-chartered stock savings bank, Chicopee Savings Bank is subject to supervision, regulation and examination by the Massachusetts Commissioner of Banks and to various Massachusetts statutes and regulations which govern, among other things, investment powers, lending and deposit-taking activities, borrowings, maintenance of surplus and reserve accounts, distribution of earnings and payment of dividends. In addition, Chicopee Savings Bank is subject to Massachusetts consumer protection and civil rights laws and regulations. The approval of the Massachusetts Commissioner of Banks and/or the Massachusetts Board of Bank Incorporation is required for a Massachusetts-chartered bank to establish or close branches, merge with other financial institutions, issue stock and undertake certain other activities.

Massachusetts regulations generally allow Massachusetts banks to, with appropriate regulatory approvals, engage in activities permissible for federally chartered banks or banks chartered by another state. The Commissioner also has adopted procedures reducing regulatory burdens and expense and expediting branching by well-capitalized and well-managed banks.

New Massachusetts banking legislation, “An Act Modernizing the Banking Laws and Enhancing the Competitiveness of State-Chartered Banks,” was signed into law in January 2015 and is effective April 2015. Among other things, the legislation attempts to better synchronize Massachusetts laws with federal requirements in the same area, streamlines the process for an institution to engage in activities permissible for federally chartered and out of state institutions, consolidates corporate governance statutes and provides authority for the Commissioner to establish a tiered supervisory system for Massachusetts-chartered institutions based on factors such as asset size, capital level, balance sheet composition, examination rating, compliance and other factors deemed appropriate.

Dividends. A Massachusetts stock bank may declare cash dividends from net profits not more frequently than quarterly. Non-cash dividends may be declared at any time. No dividends may be declared, credited or paid if the bank's capital stock is impaired. The approval of the Massachusetts Commissioner of Banks is required if the total of all dividends declared in any calendar year exceeds the total of its net profits for that year combined with its retained net profits of the preceding two years. Dividends from The Company may depend, in part, upon receipt of dividends from Chicopee Savings Bank. The payment of dividends from Chicopee Savings Bank would be restricted by federal law if the payment of such dividends resulted in Chicopee Savings Bank failing to meet regulatory capital requirements.

For the years ended December 31, 2014, 2013 and 2012, a total of \$5.0 million, \$2.5 million and \$1.6 million, respectively, in dividends were declared from the Bank to the Company. During 2014, 2013 and 2012, a total of \$700,000, \$660,000 and \$2.0 million, respectively, in dividends were declared from Chicopee Funding Corporation ("CFC") to the Company, respectively.

For the years ended December 31, 2014 and 2013, a total of \$1.4 million and \$1.0 million, respectively, in cash dividends were paid to the Company's stockholders. The Company did not pay any dividend to shareholders during the year ended December 31, 2012. The first quarterly dividend declared by the Company was announced on January 24, 2013.

Loans to One Borrower Limitations. Massachusetts banking law grants broad lending authority. However, with certain limited exceptions, total obligations to one borrower may not exceed 20 percent of the total of the bank's capital, surplus and undivided profits.

Loans to a Bank's Insiders. Massachusetts banking laws prohibit any executive officer or director of a savings bank from borrowing or guaranteeing extensions of credit by such savings bank except for any of the following loans or extensions of credit with the approval of a majority of the Board of Directors: (i) loans or extensions of credit, secured or unsecured, to an officer of the savings bank in an amount not exceeding \$100,000; (ii) loans or extensions of credit intended or secured for educational purposes to an officer of the bank in an amount not exceeding \$200,000; (iii) loans or extensions of credit secured by a mortgage on residential real estate to be occupied in whole or in part by the officer to whom the loan or extension of credit is made, in an amount not exceeding \$750,000; and (iv) loans or extensions of credit to a director of the savings bank who is not also an officer of the savings bank in an amount permissible under the savings bank's loan to one borrower limit. No such loan or extension of credit may be granted with an interest rate or other terms that are preferential in comparison to loans granted to persons not affiliated with the savings bank. The recent Massachusetts legislation provides that, beginning in April 2015, Massachusetts law incorporates federal regulations governing extensions of credit to insiders, and the separate Massachusetts requirements are regarding such extensions of credit are repealed.

Investment Activities. In general, Massachusetts-chartered savings banks may invest in preferred and common stock of any corporation organized under the laws of the United States or any state provided such investments do not involve control of any corporation and do not, in the aggregate, exceed 4% of the bank's deposits. Federal law imposes additional restrictions on Chicopee Savings Bank's investment activities. See "-Federal Regulations-Business and Investment Activities."

Regulatory Enforcement Authority. Any Massachusetts savings bank that does not operate in accordance with the regulations, policies and directives of the Massachusetts Commissioner of Banks may be subject to sanctions for non-compliance, including revocation of its charter. The Massachusetts Commissioner of Banks may, under certain circumstances, suspend or remove officers or directors who have violated the law, conducted the bank's business in an unsafe or unsound manner or contrary to the depositors interests or been negligent in the performance of their duties. Upon finding that a bank has engaged in an unfair or deceptive act or practice, the Massachusetts Commissioner of Banks may issue an order to cease and desist and impose a fine on the bank concerned. The Commissioner also has authority to take possession of a bank and appoint a liquidating agent under certain conditions such as an unsafe and

unsound condition to transact business, the conduct of business in an unsafe or unauthorized manner of impaired capital. In addition, Massachusetts consumer protection and civil rights statutes applicable to Chicopee Savings Bank permit private individual and class action law suits and provide for the rescission of consumer transactions, including loans, and the recovery of statutory and punitive damage and attorney's fees in the case of certain violations of those statutes.

**Depositors Insurance Fund.** All Massachusetts-chartered savings banks are required to be members of the DIF, a corporation that insures savings bank deposits in excess of federal deposit insurance coverage. The DIF is authorized to charge savings banks an annual assessment fee on deposit balances in excess of amounts insured by the FDIC.

Assessment rates are based on the institution's risk category, similar to the method currently used to determine assessments by the FDIC discussed below under "-Federal Regulations-Insurance of Deposit Accounts."

**Protection of Personal Information.** Massachusetts has adopted regulatory requirements intended to protect personal information. These requirements, which became effective March 1, 2010, are similar to existing federal laws such as the Gramm-



Leach-Bliley Act, discussed below under “-Federal Regulations-Privacy Regulations”, that require organizations to establish written information security programs to prevent identity theft. The Massachusetts regulation also contains technology system requirements, especially for the encryption of personal information sent over wireless or public networks or stored on portable devices.

Massachusetts has other statutes or regulations that are similar to certain of the federal provisions discussed below.  
Federal Regulations

**Capital Requirements.** Under the FDIC’s regulations, federally insured state-chartered banks that are not members of the Federal Reserve System (“state non-member banks”), such as Chicopee Savings Bank, are required to comply with minimum leverage capital requirements. During 2014, for an institution not anticipating or experiencing significant growth and deemed by the FDIC to be, in general, a strong banking organization rated composite 1 under Uniform Financial Institutions Ranking System, the minimum capital leverage requirement was a ratio of Tier 1 capital to total assets of 3.0%. For all other institutions, the minimum leverage capital ratio was not less than 4.0%. Tier 1 capital is the sum of common stockholder’s equity, noncumulative perpetual preferred stock (including any related surplus) and minority investments in certain subsidiaries, less intangible assets (except for certain servicing rights and credit card relationships) and certain other specified items.

FDIC regulations also require state non-member banks to maintain certain ratios of regulatory capital to regulatory risk-weighted assets, or “risk-based capital ratios.” Risk-based capital ratios are determined by allocating assets and specified off-balance sheet items to four risk-weighted categories ranging from 0.0% to 100.0%. During 2014, state non-member banks were required to maintain a minimum ratio of total capital to risk-weighted assets of at least 8.0%, of which at least one-half must be Tier 1 capital. Total capital consists of Tier 1 capital plus Tier 2 or supplementary capital items, which include allowances for loan losses in an amount of up to 1.25% of risk-weighted assets, cumulative preferred stock, subordinated debentures and certain other capital instruments, and a portion of the net unrealized gain on equity securities. The includable amount of Tier 2 capital cannot exceed the amount of the institution’s Tier 1 capital.

In July 2013, the FDIC and the other federal bank regulatory agencies issued a final rule to revise their leverage and risk-based capital requirements and the method for calculating risk-weighted assets to make them consistent with agreements that were reached by the Basel Committee on Banking Supervision and certain provisions of the Dodd-Frank Act. Among other things, the rule establishes a uniform leverage ratio requirement of 4% of total assets, provides for a new common equity Tier 1 minimum capital requirement (4.5% of risk-weighted assets), increases the minimum Tier 1 capital to risk-based assets requirement (from 4% to 6% of risk-weighted assets) and assigns a higher risk weight (150%) to exposures that are more than 90 days past due or are on nonaccrual status and to certain commercial real estate facilities that finance the acquisition, development or construction of real property. The final rule also requires unrealized gains and losses on certain “available-for-sale” securities holdings to be included for purposes of calculating regulatory capital requirements unless a one-time opt-in or opt-out is exercised. The rule limits a banking organization’s capital distributions and certain discretionary bonus payments to executive officers if the banking organization does not hold a “capital conservation buffer” consisting of 2.5% of common equity Tier 1 capital to risk-weighted assets in addition to the amount necessary to meet its minimum risk-based capital requirements. The final rule also implements the Dodd-Frank Act’s directive to apply to bank and savings and loan holding companies consolidated capital requirements that are not less stringent than those applicable to their subsidiary institutions. The final rule became effective January 1, 2015. The “capital conservation buffer” will be phased in from January 1, 2016 to January 1, 2019, when the full capital conservation buffer will be effective.

**Prompt Corrective Regulatory Action.** Federal law requires, among other things, that federal bank regulatory authorities take “prompt corrective action” with respect to banks that do not meet minimum capital requirements. For these purposes, the law establishes five capital categories: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized and critically undercapitalized.

The FDIC has adopted regulations to implement the prompt corrective action legislation. During 2014, an institution was deemed to be “well capitalized” if it has a total risk-based capital ratio of 10.0% or greater, a Tier 1 risk-based capital ratio of 6.0% or greater and a leverage ratio of 5.0% or greater. An institution was “adequately capitalized” if it

has a total risk-based capital ratio of 8.0% or greater, a Tier 1 risk-based capital ratio of 4.0% or greater, and a leverage ratio of 4.0% or greater. An institution was “undercapitalized” if it has a total risk-based capital ratio of less than 8.0%, a Tier 1 risk-based capital ratio of less than 4.0%, or a leverage ratio of less than 4.0%. An institution was deemed to be “significantly undercapitalized” if it has a total risk-based capital ratio of less than 6.0%, a Tier 1 risk-based capital ratio of less than 3.0%, or a leverage ratio of less than 3.0%. An institution is considered to be “critically undercapitalized” if it has a ratio of tangible equity (as defined in the regulations) to total assets that is equal to or less than 2.0%.

“Undercapitalized” banks must adhere to growth, capital distribution (including dividend) and other limitations and are

required to submit a capital restoration plan. A bank's compliance with such a plan must be guaranteed by any company that controls the undercapitalized institution in an amount equal to the lesser of 5% of the institution's total assets when deemed undercapitalized or the amount necessary to achieve the status of adequately capitalized. If an "undercapitalized" bank fails to submit an acceptable plan, it is treated as if it is "significantly undercapitalized." "Significantly undercapitalized" banks must comply with one or more of a number of additional measures, including, but not limited to, a required sale of sufficient voting stock to become adequately capitalized, a requirement to reduce total assets, cessation of taking deposits from correspondent banks, the dismissal of directors or officers and restrictions on interest rates paid on deposits, compensation of executive officers and capital distributions by the parent holding company. "Critically undercapitalized" institutions are subject to additional measures including, subject to a narrow exception, the appointment of a receiver or conservator within 270 days after it obtains such status. In connection with the final capital rule described earlier, the federal banking agencies have adopted revisions to the prompt corrective action framework, effective January 1, 2015. Under the revised prompt corrective action requirements, insured depository institutions would be required to meet the following in order to qualify as "well capitalized:" (1) a common equity Tier 1 risk-based capital ratio of at least 6.5%; (2) a Tier 1 risk-based capital ratio of at least 8% (increased from 6%); (3) a total risk-based capital ratio of at least 10% (unchanged) and (4) a Tier 1 leverage ratio of 5% or greater (unchanged).

**Standards for Safety and Soundness.** As required by statute, the federal banking agencies adopted final regulations and Interagency Guidelines Establishing Standards for Safety and Soundness to implement safety and soundness standards. The guidelines set forth the safety and soundness standards that the federal banking agencies use to identify and address problems at insured depository institutions before capital becomes impaired. The guidelines address internal controls and information systems, internal audit systems, credit underwriting, loan documentation, interest rate exposure, asset growth, asset quality, earnings, compensation, fees and benefits and, more recently, safeguarding customer information. If the appropriate federal banking agency determines that an institution fails to meet any standard prescribed by the guidelines, the agency may require the institution to submit to the agency an acceptable plan to achieve compliance with the standard.

**Business and Investment Activities.** Under federal law, all state-chartered FDIC-insured banks, including savings banks, have been limited in their activities as principal and in their equity investments to the type and the amount authorized for national banks, notwithstanding state law. Federal law permits exceptions to these limitations. For example, certain state-chartered savings banks may, with FDIC approval, continue to exercise state authority to invest in common or preferred stocks listed on a national securities exchange and in the shares of an investment company registered under the Investment Company Act of 1940, as amended. The maximum permissible investment is the lesser of 100.0% of Tier 1 capital or the maximum amount permitted by Massachusetts law. Chicopee Savings Bank received approval from the FDIC to retain and acquire such equity instruments up to the specified limits. Any such grandfathered authority may be terminated upon the FDIC's determination that such investments pose a safety and soundness risk or upon the occurrence of certain events such as the savings bank's conversion to a different charter. The FDIC is also authorized to permit state banks to engage in state authorized activities or investments not permissible for national banks (other than non-subsidiary equity investments) if they meet all applicable capital requirements and it is determined that such activities or investments do not pose a significant risk to the FDIC insurance fund. The FDIC has adopted regulations governing the procedures for institutions seeking approval to engage in such activities or investments. The Gramm-Leach-Bliley Act of 1999 specified that a state bank may control a subsidiary that engages in activities as principal that would only be permitted for a national bank to conduct in a "financial subsidiary," if a bank meets specified conditions and deducts its investment in the subsidiary for regulatory capital purposes.

**Transactions with Affiliates.** Transactions between a bank (and, generally, its subsidiaries) and its related parties or affiliates are limited by Sections 23A and 23B of the Federal Reserve Act. An affiliate of a bank is any company or entity that controls, is controlled by or is under common control with the bank. In a holding company context, the parent bank holding company and any companies which are controlled by such parent holding company are affiliates of the bank. Generally, Sections 23A and 23B of the Federal Reserve Act limit the extent to which the bank or its subsidiaries may engage in "covered transactions" with any one affiliate to 10% of such institution's capital stock and

surplus and contain an aggregate limit on all such transactions with all affiliates to an amount equal to 20% of such institution's capital stock and surplus. The term "covered transaction" includes the making of loans, purchase of assets, issuance of a guarantee and similar transactions. In addition, loans or other extensions of credit by the institution to the affiliate are required to be collateralized in accordance with specified requirements. The law also requires that affiliate transactions be on terms and conditions that are substantially the same, or at least as favorable to the institution, as those provided to non-affiliates.

The Sarbanes-Oxley Act of 2002 generally prohibits loans by a company to its executive officers and directors. The law contains a specific exception for loans by a depository institution to its executive officers and directors in compliance with federal banking laws, assuming such loans are also permitted under the law of the institution's chartering state. Under such laws, a bank's authority to extend credit to executive officers, directors and 10% shareholders ("insiders"), as well as entities such persons control, is restricted. The law limits both the individual and aggregate amount of loans that may be made to insiders based, in part, on the

bank's capital position and requires certain board approval procedures to be followed. Such loans are required to be made on terms substantially the same as those offered to unaffiliated individuals and not involve more than the normal risk of repayment. There is an exception for loans made pursuant to a benefit or compensation program that is widely available to all employees of the institution and does not give preference to insiders over other employees. Loans to executive officers are further limited to loans of specific types and amounts.

**Enforcement.** The FDIC has extensive enforcement authority over insured state savings banks, including Chicopee Savings Bank. That enforcement authority includes, among other things, the ability to assess civil money penalties, issue cease and desist orders and remove directors and officers. In general, enforcement actions may be initiated in response to violations of laws and regulations and unsafe or unsound practices. The FDIC also has authority under federal law to appoint a conservator or receiver for an insured bank under certain circumstances. The FDIC is required, with certain exceptions, to appoint a receiver or conservator for an insured state non-member bank if that bank was "critically undercapitalized" on average during the calendar quarter beginning 270 days after the date on which the institution became "critically undercapitalized."

**Federal Insurance of Deposit Accounts.** Deposit accounts in Chicopee Savings Bank are insured by the FDIC's Deposit Insurance Fund, generally up to a maximum of \$250,000 per separately insured depositor, pursuant to changes made permanent by the Dodd-Frank Act. The FDIC assesses insured depository institutions to maintain the Deposit Insurance Fund. No institution may pay a dividend if in default of its deposit insurance assessment. Under the FDIC's risk-based assessment system, insured institutions are assigned to a risk category based on supervisory evaluations, regulatory capital levels and other risk-based factors. An institution's assessment rate depends upon the category to which it is assigned and certain adjustments specified by the FDIC, with less risky institutions paying lower assessments. On February 7, 2011, as required by the Dodd-Frank Act, the FDIC published a final rule to revise the deposit insurance assessment system. The rule, which took effect April 1, 2011, changes the assessment base used for calculating deposit insurance assessments from deposits to total assets less tangible (Tier 1) capital. Since the new base is larger than the previous base, the FDIC also lowered assessment rates so that the rule would not significantly alter the total amount of revenue collected from the industry. The range of adjusted assessment rates is now 2.5 to 45 basis points of the new assessment base.

In addition to FDIC assessments, the Financing Corporation ("FICO") is authorized to impose and collect, through the FDIC, assessments for costs related to bonds issued by the FICO in the 1980s to recapitalize the former Federal Savings and Loan Insurance Corporation. The bonds issued by the FICO are due to mature in 2017 through 2019. During the year ended December 31, 2014, Chicopee Savings Bank paid \$31,000 in fees related to the FICO. The Dodd-Frank Act increased the minimum target Deposit Insurance Fund ratio from 1.15% of estimated insured deposits to 1.35% of estimated insured deposits. The FDIC must seek to achieve the 1.35% ratio by September 30, 2020. Insured institutions with assets of \$10 billion or more are supposed to fund the increase. The Dodd-Frank Act eliminated the 1.5% maximum fund ratio, instead leaving it to the discretion of the FDIC. The FDIC has exercised that discretion by establishing a long range fund ratio of 2%.

A material increase in insurance premiums would likely have an adverse effect on the operating expenses and results of operations of Chicopee Savings Bank. Management cannot predict what insurance assessment rates will be in the future.

Insurance of deposits may be terminated by the FDIC upon a finding that an institution has engaged in unsafe or unsound practices, is in an unsafe or unsound condition to continue operations or has violated any applicable law, regulation, rule, order or condition imposed by the FDIC. We do not know of any practice, condition or violation that might lead to termination of Chicopee Savings Bank's deposit insurance.

As a Massachusetts-chartered savings bank, Chicopee Savings Bank is also required to be a member of the Depositors Insurance Fund, a corporation that insures savings bank deposits in excess of federal deposit insurance coverage. See "Massachusetts Banking Laws and Supervision-Depositors Insurance Fund," above.

**Community Reinvestment Act.** Under the Community Reinvestment Act ("CRA"), a bank has a continuing and affirmative obligation, consistent with its safe and sound operation, to help meet the credit needs of its entire community, including low and moderate income neighborhoods. The CRA does not establish specific lending requirements or programs for financial institutions nor does it limit an institution's discretion to develop the types of

products and services that it believes are best suited to its particular community. The CRA does require the FDIC, in connection with its examination of a bank, to assess the institution's record of meeting the credit needs of its community and to take such record into account in its evaluation of certain applications by such institution, including applications to establish or acquire branches and merger with other depository institutions. The CRA requires the FDIC to provide a written evaluation of an institution's CRA performance utilizing a four-tiered descriptive rating system. Chicopee Savings Bank's latest FDIC CRA rating was "outstanding."

Massachusetts has its own statutory counterpart to the CRA which is also applicable to Chicopee Savings Bank. The Massachusetts version is generally similar to the CRA but utilizes a five-tiered descriptive rating system. The Massachusetts Commissioner of Banks is required to consider a bank's record of performance under the Massachusetts law in considering any application by the bank to establish a branch or other deposit-taking facility, relocate an office or to merge or consolidate with or acquire the assets and assume the liabilities of any other banking institution. Chicopee Savings Bank's most recent rating under Massachusetts law was "outstanding."

Federal Reserve System. The Federal Reserve Board regulations require savings institutions to maintain non-interest earning reserves against their transaction accounts (primarily Negotiable Order of Withdrawal (NOW) and regular checking accounts). The regulations currently provide that reserves be maintained against aggregate transaction accounts as follows: a 3% reserve ratio is assessed on net transaction accounts up to and including \$103.6 million; a 10% reserve ratio is applied above \$103.6 million. The first \$14.5 million of otherwise reservable balances are exempted from the reserve requirements. The amounts are adjusted annually. Chicopee Savings Bank complies with the foregoing requirements.

Federal Home Loan Bank System. Chicopee Savings Bank is a member of the Federal Home Loan Bank System, which consists of 12 regional Federal Home Loan Banks. The Federal Home Loan Bank System provides a central credit facility primarily for member institutions as well as other entities involved in home mortgage lending. As a member of the FHLB, Chicopee Savings Bank is required to acquire and hold shares of capital stock in the FHLB. As of December 31, 2014 and 2013, Chicopee Savings Bank was in compliance with this requirement with an investment in stock of the FHLB of \$3.9 million.

For the years ended December 31, 2014 and 2013, the Company received \$58,000, and \$15,000 in dividend income from its FHLB stock investment, respectively.

#### Other Regulations

Some interest and other charges collected or contracted for by Chicopee Savings Bank are subject to state usury laws and federal laws concerning interest rates. Chicopee Savings Bank's operations are also subject to state and federal laws applicable to credit transactions and other operations, including but not limited to, the:

- Truth-In-Lending Act, governing disclosures of credit terms to consumer borrowers;
  - Real Estate Settlement Procedures Act, requiring that borrowers for mortgage loans for one-to-four-family residential real estate receive various disclosures, including good faith estimates of settlement costs, lender servicing and escrow account practices, and prohibiting certain practices that increase the cost of settlement services;
  - Home Mortgage Disclosure Act, requiring financial institutions to provide information to enable the public and public officials to determine whether a financial institution is fulfilling its obligation to help meet the housing needs of the community it serves;
  - Equal Credit Opportunity Act, prohibiting discrimination on the basis of race, creed, or other prohibited factors in extending credit;
  - Fair Credit Reporting Act, governing the use and provision of information to credit reporting agencies; and
  - Fair Debt Collection Act, governing the manner in which consumer debts may be collected by collection agencies.
- The operations of Chicopee Savings Bank also are subject to the:
- Right to Financial Privacy Act, which imposes a duty to maintain confidentiality of consumer financial records and prescribes procedures for complying with administrative subpoenas of financial records;
  - Electronic Funds Transfer Act and Regulation E promulgated thereunder, that govern automatic deposits to and withdrawals from deposit accounts and customers' rights and liabilities arising from the use of automated teller machines and other electronic banking services;
  - Gramm-Leach-Bliley Act privacy statute which requires each depository institution to disclose its privacy policy, identify parties with whom certain nonpublic customer information is shared and provide customers with certain rights to "opt out" of disclosure to certain third parties; and





Title III of The Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (referred to as the “USA PATRIOT Act”), which significantly expanded the responsibilities of financial institutions, in preventing the use of the United States financial system to fund terrorist activities. Among other things, the USA PATRIOT Act and the related regulations requires banks operating in the United States to develop anti-money laundering compliance programs, due diligence policies and controls to facilitate the detection and reporting of money laundering.

#### Holding Company Regulation

Chicopee Bancorp, as a bank holding company, is subject to examination, regulation, and periodic reporting under the Bank Holding Company Act of 1956, as amended, as administered by the Federal Reserve Board. Chicopee Bancorp is required to obtain the prior approval of the Federal Reserve Board to acquire all, or substantially all, of the assets of any bank or bank holding company. Prior Federal Reserve Board approval would be required for Chicopee Bancorp to acquire direct or indirect ownership or control of any voting securities of any bank or bank holding company if it would, directly or indirectly, own or control more than 5% of any class of voting shares of the bank or bank holding company.

A bank holding company is generally prohibited from engaging in, or acquiring, direct or indirect control of more than 5% of the voting securities of any company engaged in non-banking activities. One of the principal exceptions to this prohibition is for activities found by the Federal Reserve Board to be so closely related to banking or managing or controlling banks as to be a proper incident thereto. Some of the principal activities that the Federal Reserve Board has determined by regulation to be closely related to banking are: (i) making or servicing loans; (ii) performing certain data processing services; (iii) providing securities brokerage services; (iv) acting as fiduciary, investment or financial advisor; (v) leasing personal or real property under certain conditions; (vi) making investments in corporations or projects designed primarily to promote community welfare; and (vii) acquiring a savings association.

The Gramm-Leach-Bliley Act of 1999 authorizes a bank holding company that meets specified conditions, including depository institutions subsidiaries that are “well capitalized” and “well managed,” to opt to become a “financial holding company.” A “financial holding company” may engage in a broader array of financial activities than permitted a typical bank holding company. Such activities can include insurance underwriting and investment banking. Chicopee Bancorp does not anticipate opting for “financial holding company” status at this time.

Chicopee Bancorp is subject to the Federal Reserve Board’s consolidated capital adequacy guidelines for bank holding companies. Traditionally, those guidelines have been structured similarly to the regulatory capital requirements for the subsidiary depository institutions, but were somewhat more lenient. For example, the holding company capital requirements allowed inclusion of certain instruments in Tier 1 capital that were not includable at the institution level. As previously noted, the Dodd-Frank Act directs the Federal Reserve Board to issue consolidated capital requirements for depository institution holding companies that are not less stringent, both quantitatively and in terms of components of capital, than those applicable to institutions themselves. The previously discussed final rule regarding regulatory capital requirements implements the Dodd-Frank Act as to bank holding company capital standards. Consolidated regulatory capital requirements identical to those applicable to the subsidiary banks apply to bank holding companies (with greater than \$500 million of assets) as of January 1, 2015. As is the case with institutions themselves, the capital conservation buffer will be phased in between 2016 and 2019.

A bank holding company is generally required to give the Federal Reserve Board prior written notice of any purchase or redemption of then outstanding equity securities if the gross consideration for the purchase or redemption, when combined with the net consideration paid for all such purchases or redemptions during the preceding 12 months, is equal to 10% or more of the company’s consolidated net worth. The Federal Reserve Board may disapprove such a purchase or redemption if it determines that the proposal would constitute an unsafe and unsound practice, or would violate any law, regulation, Federal Reserve Board order or directive, or any condition imposed by, or written agreement with, the Federal Reserve Board. The Federal Reserve Board has adopted an exception to that approval requirement for well-capitalized bank holding companies that meet certain other conditions.

The Federal Reserve Board has issued a policy statement regarding the payment of dividends and the repurchase of shares of common stock by bank holding companies. In general, the policy provides that dividends should be paid

only out of current earnings and only if the prospective rate of earnings retention by the holding company appears consistent with the organization's capital needs, asset quality and overall financial condition. Regulatory guidance provides for prior regulatory consultation with respect to dividends in certain circumstances such as where the company's net income for the past four quarters, net of dividends' previously paid over that period, is insufficient to fully fund the dividend or the company's overall rate of earnings retention is inconsistent with the company's capital needs and overall financial condition. The ability of a holding company to pay dividends may be restricted if a subsidiary bank becomes undercapitalized. The policy statement also provides for regulatory consultation prior to a holding company redeeming or repurchasing regulatory capital instruments when the holding company is experiencing

financial weaknesses or redeeming or repurchasing common stock or perpetual preferred stock that would result in a net reduction as of the end of a quarter in the amount of such equity instruments outstanding compared with the beginning of the quarter in which the redemption or repurchase occurred. These regulatory policies could affect the ability of the Chicopee Bancorp, Inc. to pay dividends, repurchase shares of its stock or otherwise engage in capital distributions.

The Federal Deposit Insurance Act, makes depository institutions liable to the FDIC for losses suffered or anticipated by the insurance fund in connection with the default of a commonly controlled depository institution or any assistance provided by the FDIC to such an institution in danger of default. That law would have potential applicability if Chicopee Bancorp ever held as a separate subsidiary a depository institution in addition to Chicopee Savings Bank. Chicopee Bancorp and Chicopee Savings Bank will be affected by the monetary and fiscal policies of various agencies of the United States Government, including the Federal Reserve System. In view of changing conditions in the national economy and in the money markets, it is impossible for management to accurately predict future changes in monetary policy or the effect of such changes on the business or financial condition of Chicopee Bancorp or Chicopee Savings Bank.

The status of Chicopee Bancorp as a registered bank holding company under the Bank Holding Company Act will not exempt it from certain federal and state laws and regulations applicable to corporations generally, including, without limitation, certain provisions of the federal securities laws.

**Change in Control Regulations.** Under the Change in Bank Control Act, no person may acquire control of a bank holding company such as Chicopee Bancorp, Inc. unless the Federal Reserve Board has been given 60 days' prior written notice and has not issued a notice disapproving the proposed acquisition, taking into consideration certain factors, including the financial and managerial resources of the acquirer and the competitive effects of the acquisition. Control, as defined under federal law, means ownership, control of or holding irrevocable proxies representing more than 25% of any class of voting stock, control in any manner of the election of a majority of the institution's directors, or a determination by the regulator that the acquiror has the power to direct, or directly or indirectly to exercise a controlling influence over, the management or policies of the institution. Acquisition of more than 10% of any class of a savings and loan holding company's voting stock constitutes a rebuttable determination of control under the regulations under certain circumstances including where, as will be the case with Chicopee Bancorp, Inc., the issuer has registered securities under Section 12 of the Securities Exchange Act of 1934.

**Massachusetts Holding Company Regulation.** Under Massachusetts banking laws, a company owning or controlling two or more banking institutions, including a savings bank, is regulated as a bank holding company. Each Massachusetts bank holding company: (i) must obtain the approval of the Massachusetts Board of Bank Incorporation before engaging in certain transactions, such as the acquisition of more than 5% of the voting stock of another banking institution; (ii) must register, and file reports, with the Massachusetts Division of Banks; and (iii) is subject to examination by the Division of Banks. Chicopee Bancorp would become a Massachusetts bank holding company if it acquires a second banking institution and holds and operates it separately from Chicopee Savings Bank.

#### Federal Securities Laws

Chicopee Bancorp's common stock is registered with the Securities and Exchange Commission. Chicopee Bancorp is subject to the information, proxy solicitation, insider trading restrictions and other requirements under the Securities Exchange Act of 1934.

#### Executive Officers of the Registrant

| Name              | Principal Position  |
|-------------------|---|
| William J. Wagner | President and Chief Executive Officer of Chicopee Bancorp and Chicopee Savings Bank   |
| Guida R. Sajdak   | Senior Vice President, Chief Financial Officer and Treasurer of Chicopee Bancorp and Senior Vice President and Treasurer of Chicopee Savings Bank |
| Russell J. Omer   | Executive Vice President of Chicopee Bancorp and Executive Vice President, Lending, of Chicopee Savings Bank                                      |

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Below is information regarding our executive officers who are not also Directors. Unless otherwise stated, each executive officer has held his or her position for at least the last five years. Ages presented are as of December 31, 2014.

Russell J. Omer has served as Executive Vice President of Chicopee Bancorp since December 2008, and Senior Vice President of Chicopee Bancorp since 2006, and Senior Vice President, Lending, since 1998. Age 64.

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Guida R. Sajdak was appointed Senior Vice President, Chief Financial Officer and Treasurer of the Company and Bank effective July 1, 2010. Ms. Sajdak has been employed by the Bank since 1989. Prior to her most recent appointment, Ms. Sajdak held the title of Senior Vice President of Finance. Age 41.

#### Item 1A. Risk Factors.

Our increased emphasis on commercial real estate and commercial business lending may expose us to increased lending risks. At December 31, 2014, our loan portfolio included \$249.6 million of commercial real estate loans, or 47.7% of total loans, and \$74.3 million of commercial business loans, or 14.1% of total loans. We have grown the commercial loan portfolio in recent years and intend to continue to grow commercial real estate and commercial loans. These types of loans generally expose a lender to greater risk of non-payment and loss than one-to-four-family residential real estate loans because repayment of the loans often depends on the successful operation of the property and the income stream of the borrowers. Such loans typically involve larger loan balances to single borrowers or groups of related borrowers compared to one-to-four-family residential real estate loans. Commercial business loans expose us to additional risks since they typically are made on the basis of the borrower's ability to make repayments from the cash flow of the borrower's business and are secured by non-real estate collateral that may depreciate over time. In addition, since such loans generally entail greater risk than one-to-four-family residential real estate loans, we may need to increase our allowance for loan losses in the future to account for the likely increase in probable credit losses associated with the growth of such loans. Also, many of our commercial borrowers have more than one loan outstanding with us. Consequently, an adverse development with respect to one loan or one credit relationship can expose us to a significantly greater risk of loss compared to an adverse development with respect to a one-to-four-family residential mortgage loan.

Our low return on equity may negatively affect our stock price. Net income divided by average equity, known as "return on equity," is a ratio many investors use to compare the performance of a financial institution to its peers. Our return on equity was reduced due to the large amount of capital that we raised in our 2006 stock offering and to expenses we will incur in pursuing our growth strategies, the costs of being a public company and added expenses associated with our employee stock ownership plan and equity incentive plan. Until we can increase our net interest income, non-interest income and decrease our non-interest expenses, we expect our return on equity to be below that of our peers, which may negatively affect the value of our common stock. For the year ended December 31, 2014, we reported a negative return on average equity of (0.64)%.

Negative developments in the financial industry and the domestic and international credit markets may adversely affect our operations and results. Since the latter half of 2007, negative developments in the global credit and securitization markets have resulted in uncertainty in the financial markets and a general economic downturn which has continued into 2014. The economic downturn was accompanied by deteriorated loan portfolio quality at many institutions, including Chicopee Savings Bank. In addition, the value of real estate collateral supporting many home mortgages has declined and may continue to decline. Bank and bank holding company stock prices have been negatively affected, as has the ability of banks and bank holding companies to raise capital or borrow in the debt markets. These negative developments along with the turmoil and uncertainties that have accompanied them have heavily influenced the formulation and enactment of the Dodd-Frank Act, along with its implications as described elsewhere in this "Risk Factors" section. In addition to the many future implementing rules and regulations of the Dodd-Frank Act, the potential exists for other new federal or state laws and regulations regarding lending and funding practices and liquidity standards to be enacted. Bank regulatory agencies are expected to continue to be active in responding to concerns and trends identified in examinations. Negative developments in the financial industry and the domestic and international credit markets, and the impact of new legislation in response to those developments, may negatively impact our operations by increasing our costs, restricting our business operations, including our ability to originate or sell loans, and adversely impact our financial performance. In addition, these risks could affect the value

of our loan portfolio as well as the value of our investment portfolio, which would also negatively affect our financial performance.

A downturn in the local economy or a decline in real estate values could decrease our profits. Nearly all of our real estate loans are secured by real estate in Hampden County. As a result of this concentration, a downturn in the local economy could cause significant increases in non-performing loans, which would decrease our profits. Additionally, a decrease in asset quality could require additions to our allowance for loan losses through increased provisions for loan losses, which would hurt our profits. A continued decline in real estate values could cause some of our real estate loans to become inadequately collateralized, which would expose us to a greater risk of loss. In addition, because we have a significant amount of commercial real estate loans, decreases in tenant occupancy may also have a negative effect on the ability of many of our borrowers to make timely repayments on their loans, which would have an adverse impact on our earnings.

We could be held responsible for environmental liabilities of properties we acquired through foreclosure. In the course of business, we may acquire, through foreclosure, properties securing loans originated or purchased that are in default. Particularly in commercial real estate lending, there is a risk that material environmental violations could be discovered on these properties. In this event, we might be required to remedy these violations at the affected properties at our sole cost and expense.

The cost of remedial action could substantially exceed the value of affected properties. We may not have adequate remedies against the prior owner or other responsible parties and could find it difficult or impossible to sell the affected properties. These events could have an adverse effect on our financial condition and results of operations.

We are subject to liquidity risk. Liquidity risk is the risk of potential loss if we are unable to meet our funding requirements at a reasonable cost. Our liquidity could be impaired by an inability to access the capital markets or by unforeseen outflows of cash. This situation may arise due to circumstances that we may be unable to control, such as a general market disruption or an operational problem that affects parties or us.

Changes in interest rates could adversely affect our results of operations and financial condition. Our results of operations and financial condition are significantly affected by changes in interest rates. Our results of operations depend substantially on our net interest income, which is the difference between the interest income we earn on our interest-earning assets, such as loans and securities, and the interest expense we pay on our interest-bearing liabilities, such as deposits and borrowings. Because our interest-earning assets generally reprice or mature more quickly than our interest-bearing liabilities, an increase in interest rates generally would tend to result in an increase in net interest income. Changes in interest rates also affect the current fair value of our interest-earning securities portfolio. Generally, the value of securities moves inversely with changes in interest rates. Additionally, a majority of our single-family real estate loans held for investment are adjustable-rate loans. Any rise in market interest rates may result in increased payments for borrowers who have adjustable rate loans, increasing the possibility of default.

For further discussion of how changes in interest rates could impact us, see Management's Discussion and Analysis of Financial Condition and Results of Operations-Risk Management-Interest Rate Risk Management.

Prepayments of loans may negatively impact our business. Generally, our customers may prepay the principal amount of their outstanding loans at any time. The speeds at which such prepayments occur, as well as the size of such prepayments, are within our customers' discretion. If customers prepay the principal amount of their loans, and we are unable to lend those funds to other borrowers or invest the funds at the same or higher interest rates, our interest income will be reduced. A significant reduction in interest income could have a negative impact on our results of operations and financial condition.

We face significant legal risks, both from regulatory investigations and proceedings and from private actions brought against us. From time to time, we may be named as a defendant or are otherwise involved in various legal proceedings, including class actions and other litigation or disputes with third parties. There is no assurance that litigation with private parties will not increase in the future. Future actions against us may result in judgments, settlements, fines, penalties or other results adverse to us, which could materially adversely affect our business, financial condition or results of operations, or cause serious reputational harm to us. As a participant in the financial services industry, we are exposed to a high level of potential litigation related to our businesses and operations. Although we maintain insurance, the scope of this coverage may not provide us with full, or even partial, coverage in any particular case. As a result, a judgment against us in any such litigation could have a material adverse effect on our financial condition and results of operation.

Our businesses and operations are also subject to increasing regulatory oversight and scrutiny, which may lead to additional regulatory investigations or enforcement actions. These and other initiatives from federal and state officials may subject us to further judgments, settlements, fines or penalties, or cause us to be required to restructure our operations and activities, all of which could lead to reputational issues, or higher operational costs, thereby reducing our revenue.

We are subject to reputational risk. We are dependent on our reputation within our market area, as a trusted and responsible financial company, for all aspects of our relationships with customers, employees, vendors, third-party

service providers, and others, with whom we conduct business or potential future business. Our actual or perceived failure to (a) identify and address potential conflicts of interest, ethical issues, money-laundering, or privacy issues; (b) meet legal and regulatory requirements applicable to the Bank and to the Company; (c) maintain the privacy of customer and accompanying personal information; (d) maintain adequate record keeping; (e) engage in proper sales and trading practices; and (f) identify the legal, reputational, credit, liquidity and market risks inherent in our products could give rise to reputational risk that could cause harm to the Bank and our business prospects. If we fail to address any of these issues in an appropriate manner, we could be subject to additional legal risks, which, in turn, could increase the size and number of litigation claims and damages asserted or subject us to enforcement actions, fines and penalties and cause us to incur related costs and expenses. Our ability to attract and retain customers and employees could be adversely affected to the extent our reputation is damaged.

We may incur fines, penalties and other negative consequences from regulatory violations, possibly even inadvertent or unintentional violations. We maintain systems and procedures designed to ensure that we comply with applicable laws and regulations. However, some legal/regulatory frameworks provide for the imposition of fines or penalties for noncompliance even though the noncompliance was inadvertent or unintentional and even though there was in place at the time systems and procedures



designed to ensure compliance. For example, we are subject to regulations issued by the Office of Foreign Assets Control, or “OFAC,” that prohibit financial institutions from participating in the transfer of property belonging to the governments of certain foreign countries and designated nationals of those countries. OFAC may impose penalties for inadvertent or unintentional violations even if reasonable processes are in place to prevent the violations. There may be other negative consequences resulting from a finding of noncompliance, including restrictions on certain activities. Such a finding may also damage our reputation as described below and could restrict the ability of institutional investment managers to invest in our securities.

Historically low interest rates may adversely affect our net interest income and profitability. During the past six years it has been the policy of the Board of Governors of the Federal Reserve System (“Federal Reserve Board”) to maintain interest rates at historically low levels through its targeted federal funds rate and the purchase of mortgage-backed securities. As a result, market rates on the loans we have originated and the yields on securities we have purchased have been at lower levels than available prior to 2008. As a general matter, our interest-bearing liabilities reprice or mature more quickly than our interest-earning assets, which has resulted in increases in net interest income as interest rates decreased. However, our ability to lower our interest expense is limited at these interest rate levels while the average yield on our interest-earning assets may continue to decrease. The Board of Governors of the Federal Reserve System has recently indicated its intention to increase short term rates. Accordingly, our net interest income (the difference between interest income earned on assets and interest expense paid on liabilities) may be adversely affected and may even decrease, which may have an adverse effect on our profitability.

If our allowance for loan losses is not sufficient to cover actual loan losses, our earnings will decrease. We make various assumptions and judgments about the collectability of our loan portfolio, including the creditworthiness of our borrowers and the value of the real estate and other assets serving as collateral for the repayment of many of our loans. In determining the amount of the allowance for loan losses, we review our loans and our loss and delinquency experience, and we evaluate economic conditions. If our assumptions are incorrect, our allowance for loan losses may not be sufficient to cover probable losses in our loan portfolio, resulting in additions to our allowance. Our allowance for loan losses was 0.94% of total loans at December 31, 2014. Material additions to our allowance could materially decrease our net income. In addition, bank regulators periodically review our allowance for loan losses and may require us to increase our allowance for loan losses or recognize further loan charge-offs. Any increase in our allowance for loan losses or loan charge-offs as required by these regulatory authorities might have a material adverse effect on our financial condition and results of operations.

We may be unable to attract and retain key personnel. Our success depends, in large part, on our ability to attract and retain key personnel. Competition for qualified personnel in the financial services industry can be intense and we may not be able to hire or retain the key personnel that we depend upon for success. The unexpected loss of services of one or more of our key personnel could have a material adverse impact on our business because of their skills, knowledge of the markets in which we operate, years of industry experience and the difficulty of promptly finding qualified replacement personnel.

We rely on other companies to provide key components of our business infrastructure. Third party vendors provide key components of our business infrastructure such as internet connections, network access and core application processing. While we have selected these third party vendors carefully, we do not control their actions. Any problems caused by these third parties, including as a result of their not providing us their services for any reason or their performing their services poorly, could adversely affect our ability to deliver products and services to our customers or otherwise conduct our business efficiently and effectively. Replacing these third party vendors could also entail significant delay and expense.

We are subject to extensive regulatory oversight. We are subject to extensive supervision, regulation, and examination by the Federal Reserve Board, the Federal Deposit Insurance Corporation and the Massachusetts Division of Banks.

As a result, we are limited in the manner in which we conduct our business, undertake new investments and activities, and obtain financing. This regulatory structure is designed primarily for the protection of the Deposit Insurance Fund of the FDIC, the Depositor's Insurance Fund of Massachusetts, and our depositors, and not to benefit our stockholders. This regulatory structure also gives the regulatory authorities extensive discretion in connection with their supervisory and enforcement actions and examination policies, including policies with respect to capital levels, the timing and amount of dividend payments, the classification of assets, the establishment of adequate loan loss reserves for regulatory purposes and the timing and amounts of assessments and fees.

In addition, we must comply with significant anti-money laundering and anti-terrorism laws and regulations, CRA laws and regulations, and fair lending laws and regulations. Government agencies have the authority to impose monetary penalties and other sanctions on institutions that fail to comply with these laws and regulations, which could significantly affect our business activities, including our ability to acquire other financial institutions or expand our branch network.

Financial reform legislation enacted in 2010 has, among other things, tightened capital standards and resulted in new laws and regulations that are expected to increase our costs of operations. The Dodd-Frank Wall Street Reform and Consumer Protection Act was enacted in 2010. This law is significantly changing the current bank regulatory structure and affects the lending, deposit, investment, trading and operating activities of financial institutions and their holding companies. The Dodd-Frank Act

requires various federal agencies to adopt a broad range of new implementing rules and regulations, and to prepare numerous studies and reports for Congress. The federal agencies are given significant discretion in drafting the implementing rules and regulations, and consequently, many of the details and much of the impacts of the Dodd-Frank Act remain unknown for many months or years.

The Dodd-Frank Act created 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 Consumer Financial Protection Bureau has examination and enforcement authority over all banks with more than \$10 billion in assets. Banks with \$10 billion or less in assets will continue to be examined for compliance with the consumer laws by their primary bank regulators. The Dodd-Frank Act also weakened 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 required 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, which will exclude certain instruments that previously have been eligible for inclusion by bank holding companies as Tier 1 capital, such as trust preferred securities and certain collateralized debt obligations.

A provision of the Dodd-Frank Act eliminated, as of July 21, 2011, 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 interest expense.

The Dodd-Frank Act also broadened the base for Federal Deposit Insurance Corporation deposit insurance assessments. Assessments are now based on the average consolidated total assets less tangible equity capital of a financial institution, rather than deposits. The Dodd-Frank Act also permanently increased the maximum amount of deposit insurance for banks, savings institutions and credit unions to \$250,000 per depositor, retroactive to January 1, 2009. The legislation also increased the required minimum reserve ratio for the Deposit Insurance Fund, from 1.15% to 1.35% of insured deposits, and directs the Federal Deposit Insurance Corporation to offset the effects of increased assessments on depository institutions with less than \$10 billion in assets.

The Dodd-Frank Act requires publicly traded companies to give stockholders a non-binding vote on executive compensation and so-called “golden parachute” payments. 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.

We expect that current and future rules and regulations promulgated pursuant to the Dodd-Frank Act will increase our operating and compliance costs and could increase our interest expense.

Legislative or regulatory responses to perceived financial and market problems could impair our rights against borrowers. Federal, state and local laws and policies could reduce the amount distressed borrowers are otherwise contractually obligated to pay under their mortgage loans, and may limit the ability of lenders to foreclose on mortgage collateral. Restrictions on Chicopee Savings Bank's rights as creditor could result in increased credit losses on our loans and mortgage-backed securities, or increased expense in pursuing our remedies as a creditor.

Strong competition within our market area could hurt our profits and slow growth. We face intense competition both in making loans and attracting deposits. This competition has made it more difficult for us to make new loans and attract deposits. Price competition for loans and deposits might result in us earning less on our loans and paying more on our deposits, which reduces net interest income. As of June 30, 2014, we held 4.87% of the deposits in Hampden County, which was the 8th largest market share of deposits out of the 19 financial institutions in the county. This data does not include deposits held by one of our primary competitors, credit unions, which, as tax-exempt organizations, are able to offer higher rates on retail deposits than banks. There are 15 credit unions headquartered in Hampden County, some of the larger of which are headquartered in Chicopee, Massachusetts. Some of the institutions with which we compete have substantially greater resources and lending limits than we have and may offer services that we

do not provide. We expect competition to increase in the future as a result of legislative, regulatory and technological changes and the continuing trend of consolidation in the financial services industry. Our profitability depends upon our continued ability to compete successfully in our market area.

We must adapt to information technology changes in the financial services industry, which could present operational issues, require significant capital spending, or impact our reputation. The financial services industry is constantly undergoing technological changes, with frequent introductions of new technology-driven products and services. The effective use of technology increases efficiency and enables financial institutions to better serve customers and reduce costs. Our future success will depend,

in part, upon our ability to address the needs of our customers by using technology to provide products and services that will satisfy customer demands for convenience, as well as to create additional efficiencies in our operations. We may not be able to effectively implement new technology-driven products and services or be successful in marketing these products and services to our customers.

Systems failures, interruptions or breaches of security could have an adverse effect on our financial condition and results of operations. We are subject to certain operational risks, including, but not limited to, data processing system failures and errors, inadequate or failed internal processes, customer or employee fraud and catastrophic failures resulting from terrorist acts or natural disasters. We depend upon data processing, software, communication, and information exchange on a variety of computing platforms and networks and over the Internet, and we rely on the services of a variety of vendors to meet our data processing and communication needs. Despite instituted safeguards, we cannot be certain that all of our systems are entirely free from vulnerability to attack or other technological difficulties or failures. Information security risks have increased significantly due to the use of online, telephone and mobile banking channels by customers and the increased sophistication and activities of organized crime, hackers, terrorists and other external parties. Our technologies, systems, networks and our customers' devices may be the target of, cyber-attacks, computer viruses, malicious code, phishing attacks or information security breaches that could result in the unauthorized release, gathering, monitoring, misuse, loss or destruction of our or our customers' confidential, proprietary and other information, the theft of customer assets through fraudulent transactions or disruption of our or our customers' or other third parties' business operations. If information security is breached or other technology difficulties or failures occur, information may be lost or misappropriated, services and operations may be interrupted and we could be exposed to claims from customers. While we maintain a system of internal controls and procedures, any of these results could have a material adverse effect on our business, financial condition, results of operations or liquidity.

The market value of wealth management assets under administration may be negatively affected by changes in economic and market conditions. A substantial portion of income from fiduciary services is dependent on the market value of wealth management assets under administration, which are primarily marketable securities. Changes in domestic and foreign economic conditions, volatility in financial markets, and general trends in business and finance, all of which are beyond our control, could adversely impact the market value of these assets and the fee revenues derived from the management of these assets.

We are a holding company and dependent upon our subsidiaries for dividends, distributions and other payments. We are a legal entity separate and distinct from our subsidiaries. Our revenue (on a parent-only basis) is derived primarily from interest and dividends paid to us by the Bank. Our right, and consequently the right of our shareholders, to participate in any distribution of the assets or earnings of the Bank through the payment of such dividends or otherwise is necessarily subject to the prior claims of creditors of the Bank (including depositors), except to the extent that certain claims of us in a creditor capacity may be recognized.

#### Item 1B. Unresolved Staff Comments.

Not applicable.

#### Item 2. Properties.

We conduct our business through our main office in Chicopee, Massachusetts, eight full service branch offices and our lending and operation center. Of our nine locations, we own six and lease three of the buildings. We also own the land for five of the six buildings we own. For one of our branches we own the building and lease the land. The net

book value of our land, buildings, and improvements was \$6.4 million at December 31, 2014. The following table sets forth ownership and lease information for the Company's offices as of December 31, 2014:

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|        | Location   | Year Opened | Lease Expires |
|--------|--|-------------|---------------|
| Owned  | Main Office:                                     |             |               |
|        | 70 Center Street<br>Chicopee, MA 01013           | 1973        |               |
|        | Branch Offices:                                  |             |               |
|        | 39 Morgan Road<br>West Springfield, MA 01089     | 2005        |               |
|        | 569 East Street<br>Chicopee, MA 01020            | 1976        |               |
|        | 435 Burnett Road<br>Chicopee, MA 01020           | 1990        |               |
|        | 219/229 Exchange Street<br>Chicopee, MA 01013    | 2009/1998   |               |
| Leased | 599 Memorial Drive<br>Chicopee, MA 01020         | 1977        | 2017          |
|        | 477A Center Street<br>Ludlow, MA 01056           | 2002        | 2022          |
|        | 350 Palmer Road<br>Ware, MA 01082                | 2009        | 2027          |
|        | 32 Willimansett Street<br>South Hadley, MA 01075 | 2008        | 2027 (1)      |

(1) The lease is for the land only, the building is owned by Chicopee Savings Bank.

## Item 3. Legal Proceedings.

Periodically, we are involved in routine litigation incidental to our business, such as claims to enforce liens and contracts, condemnation proceedings on properties in which we hold security interests, claims involving the making and servicing of real property loans and other issues incident to our business. We are not a party to any pending legal proceedings that we believe would have a material adverse effect on our financial condition, results of operations or cash flows.

## Item 4. Mine Safety Disclosures.

Not applicable.

## PART II

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

The Company's common stock is traded on the NASDAQ Global Market ("NASDAQ") under the symbol "CBNK." The following table sets forth the high and low closing prices of the common stock and dividends declared for the years ended December 31, 2014 and 2013, as reported by NASDAQ. The Company did not pay any dividend to shareholders during the year ended December 31, 2012. The first quarterly dividend declared by the Company was announced on January 24, 2013. The Company currently anticipates that comparable cash dividends will continue to be paid in the future.

|                | High     | Low      | Dividends<br>Declared |                | High     | Low      | Dividends<br>Declared |
|----------------|----------|----------|-----------------------|----------------|----------|----------|-----------------------|
| 2014           |          |          |                       | 2013           |          |          |                       |
| First Quarter  | \$ 17.88 | \$ 16.89 | \$ 0.07               | First Quarter  | \$ 17.05 | \$ 15.43 | \$ 0.05               |
| Second Quarter | 17.69    | 16.46    | 0.07                  | Second Quarter | 18.27    | 16.73    | 0.05                  |
| Third Quarter  | 16.85    | 14.81    | 0.07                  | Third Quarter  | 19.72    | 17.10    | 0.05                  |
| Fourth Quarter | 16.95    | 13.80    | 0.07                  | Fourth Quarter | 18.19    | 17.31    | 0.05                  |

The Company's ability to pay dividends is dependent on dividends received from Chicopee Savings Bank and its other subsidiaries. For a discussion of restrictions on the payment of cash dividends by Chicopee Savings Bank, see "Business—Regulation and Supervision—Massachusetts Banking Laws and Supervision—Dividends" in this Annual Report or Form 10-K.





## Stock Performance Graph

The following graph illustrates the annual percentage change in the cumulative total shareholder return of the Company's common stock for the period December 31, 2009 through December 31, 2014. For purposes of comparison, the graph illustrates comparable shareholder returns of the SNL Thrift \$500M – \$1B Bank Index and the NASDAQ Stock Index (U.S. Companies). The graph assumes a \$100 investment on December 31, 2009 in each case and measures the amount by which the market value, assuming reinvestment of dividends, has changed as of December 31, 2014.

|                          | 12/31/09 | 12/31/10 | 12/31/11 | 12/31/12 | 12/31/13 | 12/31/14 |
|--------------------------|----------|----------|----------|----------|----------|----------|
| Chicopee Bancorp, Inc.   | 100.00   | 101.36   | 112.98   | 127.32   | 141.16   | 138.10   |
| NASDAQ Composite         | 100.00   | 118.15   | 117.22   | 138.02   | 193.47   | 222.16   |
| SNL Thrift \$500M - \$1B | 100.00   | 109.75   | 103.58   | 131.04   | 161.06   | 187.92   |

## Shareholders and Issuer Purchases of Equity Securities

As of March 10, 2015, the Company had approximately 583 registered holders of record of the Company's common stock.

The following table provides information regarding the Company's purchase of its equity securities during the three months ended December 31, 2014.

| Period                | (a)<br>Total Number<br>of Shares<br>(or Units)<br>Purchased | (b)<br>Average Price<br>Paid Per<br>Share<br>(or Unit) | (c)<br>Total Number of<br>Shares<br>(or Units)<br>Purchased as Part<br>of Publicly<br>Announced Plans<br>or Programs (1) | (d)<br>Maximum<br>Number<br>(or Approximate<br>Dollar Value) of<br>Shares (or Units)<br>that<br>May Yet Be<br>Purchased Under<br>the<br>Plans or Programs |
|-----------------------|---|--|--|---|
| 10/01/2014-10/31/2014 | —   | \$—  | 171,269  | 100,731   |
| 11/01/2014-11/30/2014 | 40,000  | 16.30  | 211,269  | 60,731  |
| 12/01/2014-12/31/2014 | —   | —  | 211,269  | 60,731  |
| Total                 | 40,000  | \$16.30  | 211,269  | 60,731  |

On June 1, 2012, the Company announced that the Board of Directors authorized a common stock repurchase program (the "Plan"). The Plan allows for the repurchase of up to 272,000, or approximately 5.0%, of the Company's outstanding common stock. This program is expected to continue until the authorized number of shares is repurchased, or the Company's board of directors terminate the program. There is no specified expiration date of the Plan. The Company intends to repurchase its shares from time to time at prevailing prices in the open market, in block transactions or in privately negotiated transactions. Repurchases will be made under rule 10b-5(1) repurchase plans. The repurchased shares will be held by the Company as treasury stock and will be available for general corporate purposes. As of December 31, 2014, the Company repurchased 211,269 shares at an average price of \$16.21, or 77.7%, of the Plan's total allotment. A total of 60,731 shares may yet be purchased under the Plan.

## Item 6. Selected Financial Data.

We have derived the following selected consolidated financial and other data of the Company in part from our consolidated financial statements and notes appearing elsewhere in this Form 10-K.

|                               | At or for the year ended December 31, |           |           |           |           |
|-------------------------------|---------------------------------------|-----------|-----------|-----------|-----------|
|                               | 2014                                  | 2013      | 2012      | 2011      | 2010      |
|                               | (In Thousands)                        |           |           |           |           |
| Selected Financial Data:      |                                       |           |           |           |           |
| Total assets                  | \$639,222                             | \$587,727 | \$599,982 | \$616,306 | \$573,704 |
| Cash and cash equivalents     | 49,769                                | 18,915    | 39,608    | 61,122    | 35,873    |
| Loans                         | 523,740                               | 489,292   | 468,658   | 447,126   | 433,793   |
| Allowance for loan losses     | 4,927                                 | 4,596     | 4,364     | 4,576     | 4,431     |
| Available-for-sale securities | 414                                   | 602       | 621       | 613       | 362       |
| Held-to-maturity securities   | 33,747                                | 48,606    | 59,568    | 73,852    | 69,713    |

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|   |          |           |          |          |          |   |
|---|----------|-----------|----------|----------|----------|---|
| Deposits  | 483,558  | 449,766   | 466,177  | 453,377  | 391,937  |   |
| Federal Home Loan Bank advances                     | 67,039   | 44,992    | 33,332   | 59,265   | 71,915   |   |
| Stockholders' equity                                | 88,134   | 92,230    | 89,969   | 90,782   | 91,882   |   |
| Nonperforming assets                                | 12,243   | 7,241     | 4,559    | 5,624    | 6,756    |   |
| Selected Operating Data:                            |          |           |          |          |          |   |
| Interest and dividend income                        | \$23,354 | \$23,069  | \$24,397 | \$24,850 | \$24,857 |   |
| Interest expense                                    | 3,683    | 4,349     | 5,627    | 6,902    | 8,016    |   |
| Net interest and dividend income                    | 19,671   | 18,720    | 18,770   | 17,948   | 16,841   |   |
| Provision for loan losses                           | 5,271    | 425       | 442      | 842      | 1,223    |   |
| Net interest income after provision for loan losses | 14,400   | 18,295    | 18,328   | 17,106   | 15,618   |   |
| Non-interest income                                 | 2,817    | 3,100     | 3,023    | 2,650    | 2,626    |   |
| Non-interest expense                                | 18,900   | 18,155    | 18,305   | 18,734   | 18,009   |   |
| Income (loss) before provision for income taxes     | (1,683   | ) 3,240   | 3,046    | 1,022    | 235      |   |
| Income tax expense (benefit)                        | (1,105   | ) 687     | 581      | (78      | ) (230   | ) |
| Net income (loss)                                   | \$(578   | ) \$2,553 | \$2,465  | \$1,100  | \$465    |   |
| Basic earnings (loss) per share                     | \$(0.12  | ) \$0.51  | \$0.49   | \$0.21   | \$0.08   |   |
| Diluted earnings (loss) per share                   | \$(0.12  | ) \$0.50  | \$0.48   | \$0.21   | \$0.08   |   |

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|  | At or For the Years Ended December 31, |          |          |          |          |   |
|--|--|----------|----------|----------|----------|---|
|  | 2014                                   | 2013     | 2012     | 2011     | 2010     |   |
| Selected Operating Ratios and Other Data:                        |  |          |          |          |          |   |
| Performance Ratios:  |  |          |          |          |          |   |
| Average yield on interest-earning assets (1)                     | 4.30                                   | % 4.39   | % 4.55   | % 4.73   | % 4.96   | % |
| Average rate paid on interest-bearing liabilities                | 0.88                                   | % 1.04   | % 1.27   | % 1.57   | % 1.91   | % |
| Average interest rate spread (2)                                 | 3.42                                   | % 3.35   | % 3.28   | % 3.16   | % 3.05   | % |
| Net interest margin (3)  | 3.65                                   | % 3.60   | % 3.54   | % 3.47   | % 3.40   | % |
| Ratio of interest-earning assets to interest-bearing liabilities | 134.79                                 | % 132.02 | % 126.51 | % 124.18 | % 122.61 | % |
| Non-interest expenses as a percent of average assets             | 3.13                                   | % 3.10   | % 3.06   | % 3.21   | % 3.24   | % |
| Return on average assets   | (0.10)                                 | )% 0.44  | % 0.41   | % 0.19   | % 0.08   | % |
| Return on average equity   | (0.64)                                 | )% 2.79  | % 2.75   | % 1.20   | % 0.49   | % |
| Ratio of average equity to average assets                        | 15.01                                  | % 15.58  | % 15.02  | % 15.72  | % 17.04  | % |
| Efficiency ratio (4)   | 80.09                                  | % 79.00  | % 79.43  | % 88.06  | % 91.59  | % |
| Regulatory Capital Ratios:                                       |  |          |          |          |          |   |
| Total risk-based capital ratio                                   | 17.5                                   | % 19.6   | % 19.3   | % 19.6   | % 20.7   | % |
| Tier 1 risk-based capital ratio                                  | 16.5                                   | % 18.6   | % 18.4   | % 18.7   | % 19.7   | % |
| Tier 1 leverage capital ratio                                    | 13.8                                   | % 15.8   | % 15.0   | % 14.8   | % 16.1   | % |
| Asset Quality Ratios:  |  |          |          |          |          |   |
| Nonperforming loans as a percent of total loans                  | 2.14                                   | % 1.40   | % 0.85   | % 1.05   | % 1.49   | % |
| Nonperforming assets as a percent of total assets                | 1.92                                   | % 1.23   | % 0.76   | % 0.91   | % 1.18   | % |
| Allowance for loan losses as a percent of total loans            | 0.94                                   | % 0.94   | % 0.93   | % 1.02   | % 1.02   | % |
| Allowance for loan losses as a percent of nonperforming loans    | 44.02                                  | % 67.25  | % 109.46 | % 97.13  | % 68.49  | % |
| Net loans charged-off to average interest-earning loans          | 0.98                                   | % 0.04   | % 0.14   | % 0.16   | % 0.20   | % |
| Other Data:  |  |          |          |          |          |   |
| Banking offices at end of year                                   | 9                                      | 9        | 9        | 9        | 8        |   |

- Municipal securities income and net interest income are presented on a tax equivalent basis using a tax rate of
- (1) 41%. The tax equivalent adjustment is deducted from the tax equivalent net interest income to agree to the amount reported on the income statement.
  - (2) Tax equivalent net interest rate spread represents the difference between the weighted average yield on interest-earning assets and the weighted average cost of interest-bearing liabilities.
  - (3) Tax equivalent net interest margin represents tax equivalent net interest income divided by total average interest-earning assets.
  - (4) The efficiency ratio represents the ratio of non-interest expenses divided by the sum of tax equivalent net interest income and non-interest income. This ratio excludes gains (losses) on sales of investment securities, property, loans held for sale and other, net. At December 31, 2014 the ratio is calculated as follows (in thousands):

|                                    |          |
|------------------------------------|----------|
| Non-interest expenses              | \$18,900 |
| Tax equivalent net interest income | \$20,689 |
| Non-interest income                | 2,817    |
| Add back:                          |          |

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|  |          |   |
|--|----------|---|
| Net gain on sale of securities                         | (34      | ) |
| Loss and writedowns on sale of other real estate owned | 125      |   |
| Total income included in calculation                   | \$23,597 |   |
| Non-interest expenses divided by total income          | 80.09    | % |

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

The following discussion should be read in conjunction with the "Selected Financial Data" and the Company's Consolidated Financial Statements and notes thereto, each appearing elsewhere in this Annual Report on Form 10-K.

### Forward-Looking Statements

This Annual Report on Form 10-K contains certain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. The Company intends such forward-looking statements to be covered by the safe harbor provisions for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995, and is including this statement for purposes of these safe harbor provisions. Forward-looking statements, which are based on certain assumptions and describe future plans, strategies and expectations of the Company, are generally identified by use of the words "believe," "expect," "intend," "anticipate," "estimate," "project," or similar expressions. The Company's ability to predict results or the actual effect of future plans or strategies is inherently uncertain.

By identifying these forward-looking statements for you in this manner, we are alerting you to the possibility that our actual results and financial condition may differ, possibly materially, from the anticipated results and financial condition indicated in these forward-looking statements. Important factors that could cause our actual results and financial condition to differ from those indicated in the forward-looking statements include, among others, those discussed under "Risk Factors" in Part I, Item 1A of this Annual Report on Form 10-K. In addition to these risk factors, there are other factors that may impact any public company, including ours, which could have a material adverse effect on the operations and future prospects of the Company and its subsidiaries. These additional factors include, but are not limited to: (1) changes in consumer spending, borrowing and savings habits; (2) the financial health of certain entities, including government sponsored enterprises, the securities of which are owned or acquired by the Company; (3) adverse changes in the securities market; and (4) the costs, effects and outcomes of existing or future litigation. These risks and uncertainties should be considered in evaluating forward-looking statements and undue reliance should not be placed on such statements.

### Overview

**Income.** The Company's primary source of pre-tax income is net interest income. Net interest income is the difference between interest income, which is the income that we earn on our loans and securities, and interest expense, which is the interest that we pay on our deposits and borrowings. Other significant sources of pre-tax income are service charges fees and commissions, which include service charges on deposit accounts, brokerage fee income and other loan fees (including loan brokerage fees and late charges), income from bank-owned life insurance and income from loan sales and servicing. In addition, we recognize income or losses from the sale of available-for-sale securities in years that we have such sales.

**Allowance for Loan Losses.** The allowance for loan losses is a valuation allowance to cover the inherent probable losses in the loan portfolio. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance. Management estimates the allowance balance required using past loan loss experience, information about specific borrower situations, estimated collateral values, economic conditions, and other factors. Allocation of the allowance may be made for specific loans, but the entire allowance is available for any loan that, in management's judgment, should be charged off.

**Expenses.** The non-interest expenses we incur in operating our business consist of salaries and employee benefits expenses, occupancy expenses, furniture and equipment expenses, data processing expenses, foreclosure related

expenses, professional fees, advertising expense, FDIC insurance expense, stationery, supplies and postage expense, and various other miscellaneous expenses.

#### Critical Accounting Policies

We consider accounting policies involving significant judgments and assumptions by management that have, or could have, a material impact on the carrying value of certain assets or on income to be critical accounting policies. We consider the following to be our critical accounting policies:

**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 uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

Management believes the allowance for loan losses requires the most significant estimates and assumptions used in the preparation of the consolidated financial statements. The allowance for loan losses is based on management's evaluation of the level of the allowance required in relation to the probable loss exposure in the loan portfolio. The allowance for loan losses is



evaluated on a regular basis by management. Qualitative factors, or risks considered in evaluating the adequacy of the allowance for loan losses for all loan classes include historical loss experience; levels and trends in delinquencies, nonaccrual loans, impaired loans and net charge-offs; the character and size of the loan portfolio; effects of any changes in underwriting policies; experience of management and staff; current economic conditions and their effect on borrowers; effects of changes in credit concentrations, and management's estimation of probable losses. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

The allowance consists of specific and general components. The specific component relates to loans that are classified as doubtful, substandard, special mention, or loss. For such loans that are also classified as impaired, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan. The general component covers non-impaired loans and is based on historical loss experience adjusted for qualitative factors.

Loans individually considered for impairment include all loans included in the class of commercial and residential, as well as home equity loans. These are considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant 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.

Impairment is measured on a loan-by-loan basis by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price, or the fair value of the collateral if the loan is collateral dependent.

Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. Accordingly, the Company does not separately identify individual consumer loans for impairment evaluation, except for home equity loans.

Although we believe that we use the best information available to establish the allowance for loan losses, future adjustments to the allowance may be necessary if economic conditions differ substantially from the assumptions used in making the evaluation. In addition, our banking regulators, as an integral part of their examination process, periodically review our allowance for loan losses. Such agencies may require us to recognize adjustments to the allowance based on its judgments about information available to it at the time of its examination. A large loss could deplete the allowance and require increased provisions to replenish the allowance, which would negatively affect earnings.

**Valuation of OREO.** In connection with the determination of the carrying value of other real estate owned ("OREO") management obtains independent appraisals for significant properties. While management uses available information to recognize losses on OREO, future write-downs of OREO may be necessary based upon changes in economic and market conditions.

In addition, various regulatory agencies, as an integral part of their examination process, periodically review the Company's valuation of its OREO. Such agencies may require the Company to recognize write-downs of OREO based upon their judgment about information available to them at the time of their examination.

Deferred Income Taxes. We use the asset and liability method of accounting for income taxes. Under this method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. If current available information raises doubt as to the realization of the deferred tax assets, a valuation allowance is established. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. We exercise significant judgment in evaluating the amount and timing of recognition of the resulting tax liabilities and assets. These judgments require us to make projections of future taxable income. The judgments and estimates we make in determining our deferred tax assets, which are inherently subjective, are reviewed on a continual basis as regulatory and business factors change. Any reduction in estimated future taxable income may require us to record a valuation allowance against our deferred tax assets. A valuation allowance would result in additional income tax expense in the period, which would negatively affect earnings.

Mortgage Servicing Rights. Mortgage servicing rights associated with loans originated and sold, where servicing is retained, are capitalized and included in other assets in the consolidated balance sheet. Mortgage servicing rights are amortized into non-interest income in proportion to, and over the period of, estimated future net servicing income of the underlying financial

assets. Mortgage servicing rights are evaluated for impairment based upon the fair value of the rights as compared to amortized cost. The value of the capitalized servicing rights represents the present value of the future servicing fees arising from the right to service loans in the portfolio. Critical accounting policies for mortgage servicing rights relate to the initial valuation and subsequent impairment tests. The methodology used to determine the valuation of mortgage servicing rights requires the development and use of a number of estimates, including anticipated principal amortization and prepayments of that principal balance. Events that may significantly affect the estimates used are changes in interest rates, mortgage loan prepayment speeds and the payment performance of the underlying loans. The carrying value of the mortgage servicing rights is periodically reviewed for impairment based on a determination of fair value. Impairment, if any, is recognized through a valuation allowance and is recorded as a component of non-interest expense.

**Other-Than-Temporary Impairment.** “Accounting for Certain Investments in Debt and Equity Securities,” “The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Benefits,” and “Noncurrent Marketable Equity Securities,” require companies to perform periodic reviews of individual securities in their investment portfolios to determine whether decline in the value of a security is other than temporary. A review of other-than-temporary impairment requires companies to make certain judgments regarding the materiality of the decline, its effect on the financial statements and the probability, extent and timing of a valuation recovery and the company’s intent and ability to hold the security. Pursuant to these requirements, we assess valuation declines to determine the extent to which such changes are attributable to (1) fundamental factors specific to the issuer, such as financial condition, business prospects or other factors or (2) market-related factors, such as interest rates or equity market declines. Declines in the fair value of securities below their costs that are deemed to be other than temporary are recorded in earnings as realized losses. For declines in the fair value of individual debt available-for-sale securities below their cost that are deemed to be other-than-temporary, where the Company does not intend to sell the security and it is more likely than not that the Company will not be required to sell the security before recovery of its amortized cost basis, the other-than-temporary decline in the fair value of the debt security related to 1) credit loss is recognized in earnings and 2) other factors is recognized in other comprehensive income or loss. Credit loss is determined to exist if the present value of expected future cash flows using the effective rate at acquisition is less than the amortized cost basis of the debt security. For individual debt securities where the Company intends to sell the security or more likely than not will be required to sell the security before recovery of its amortized cost, the other-than-temporary impairment is recognized in earnings equal to the difference between the security’s cost basis and its fair value at the balance sheet date. Gains and losses on the sale of securities are recorded on the trade date and are determined using the specific identification method.

### Operating Strategy

Our mission is to operate and grow a profitable community-oriented financial institution serving primarily retail customers and businesses in our market areas. We plan to continue our strategy of:

- increasing our overall commercial relationships, as well as broadening individual commercial relationships, in our market area;
- increasing our deposit market share in our market area;
- increasing our sale of non-deposit investment products;
- improving operating efficiency and cost control; and
- applying disciplined underwriting practices to maintain a high quality loan portfolio.

Continuing to increase our commercial relationships in our market area. We have diversified our loan portfolio beyond residential loans by increasing our commercial relationships. Our goal is to increase the number of our commercial customers, while also broadening individual relationships. Our commercial real estate, commercial construction and commercial and industrial loan portfolio has increased \$98.2 million, or 37.5%, from \$261.6 million, or 62.5% of the total loan portfolio, at December 31, 2010 to \$359.7 million, or 68.7% of the total loan portfolio, at December 31, 2014. Business deposit accounts have increased \$26.8 million, or 33.7%, from \$52.7 million at December 31, 2010 to \$79.5 million at December 31, 2014. In order to support the growth in the commercial loan portfolio, we have also increased the number of commercial lenders and commercial underwriting and support staff.

Increasing our deposit market share in our market area. Retail deposits are our primary source of funds for investing and lending. By offering a variety of deposit products, special and tiered pricing, and superior customer service, we intend to retain and expand existing customer relationships as well as attract new deposit customers. Personalized service and flexibility with

regard to customer needs will continue to be augmented with a full array of delivery channels to maximize customer convenience. These include drive-up banking, ATMs, internet banking, automated bill payment, remote capture, and telephone banking. Through our continued focus on these deposit-gathering efforts in existing branch locations, couple with our plans for geographic expansion, we expect to increase the overall level of deposits and our market share in the markets we serve.

In addition, historically, one of our primary competitors for retail deposits in the Chicopee market area has been credit unions. Credit unions are formidable competitors since, as tax-exempt organizations, they are able to offer higher rates on retail deposits than banks. By expanding our market area beyond the immediate Chicopee market area, and beyond the market areas of our larger credit union competitors, we intend to increase our overall deposit market share of Hampden County.

Increasing our sale of non-deposit investment products. Our profits rely heavily on the spread between the interest earned on loans and securities and interest paid on deposits and borrowings. In order to decrease our reliance on interest rate spread income, we have pursued initiatives to increase non-interest income. We offer non-deposit investment products, including mutual funds, annuities, pension plans, life insurance, long-term care and 529 college savings plans through a third party registered broker-dealer, Linsco/Private Ledger. This initiative generated \$374,000, \$320,000 and \$312,000 of non-interest income during the years ended December 31, 2014, 2013, and 2012, respectively.

Improving operating efficiency and cost control. Non-interest expense increased \$745,000, or 4.1%, from \$18.2 million, or 3.10% of average total assets, at December 31, 2013 to \$18.9 million, or 3.13% of average total assets, at December 31, 2014. The increase in non-interest expenses was largely due to the increase in foreclosure related expenses of \$339,000, or 218.7%, an increase in professional fees of \$291,000, or 44.6%, an increase in FDIC insurance premium fees of \$193,000, or 83.5%, and an increase in data processing expense of \$146,000, or 11.7%. We recognize that our growth strategies have required greater investments in personnel, marketing, premises and equipment which have had a negative impact on our expense ratio over the short term. Our non-interest expenses are also impacted as a result of the financial, accounting, legal and compliance and other additional expenses usually associated with operating as a public company. We will also recognize additional annual employee compensation and benefit expenses stemming from our employee stock ownership plan and stock options. These additional expenses adversely affect our profitability. We recognize expenses for our employee stock ownership plan when shares are committed to be released to participants' accounts and recognize expenses for stock options over the vesting period of awards made to recipients pursuant to our 2007 Equity Incentive Plan.

Applying disciplined underwriting practices to maintain a high quality loan portfolio. We believe that high asset quality is a key to long-term financial success. We have sought to grow and diversify the loan portfolio, while maintaining a high level of asset quality and moderate credit risk, using underwriting standards that we believe are conservative and diligent monitoring and collection efforts. At December 31, 2014, our ratio of nonperforming loans (loans which are 90 or more days delinquent) to total loans was 2.14% of our total loan portfolio, compared to 1.40% at December 31, 2013. Although we intend to continue our efforts to originate commercial real estate, commercial business and construction loans, we intend to continue our philosophy of managing large loan exposures through our conservative approach to lending.

## Balance Sheet Analysis

### Comparison of Financial Condition at December 31, 2014 and December 31, 2013

Total Assets. Total assets increased \$51.5 million, or 8.8%, from \$587.7 million at December 31, 2013 to \$639.2 million at December 31, 2014. The increase in total assets was primarily due to the increase in net loans of \$34.1

million, or 7.0%, from \$485.6 million, or 82.6% of total assets, at December 31, 2013 to \$519.8 million, or 81.3% of total assets, at December 31, 2014 and the increase in cash and cash equivalents of \$30.9 million, or 163.1%, to \$49.8 million at December 31, 2014. These increases were partially offset by the \$15.0 million or 30.6%, decrease in investments to \$34.2 million at December 31, 2014.

**Cash and Cash Equivalents.** Cash, including correspondent bank balances and federal funds sold, increased \$30.9 million, or 163.1%, from \$18.9 million at December 31, 2013 to \$49.8 million at December 31, 2014.

**Investments.** The investment securities portfolio, including held-to-maturity and available-for-sale securities, decreased \$15.0 million, or 30.6%, from \$49.2 million at December 31, 2013 to \$34.2 million at December 31, 2014. The decrease in investments was primarily due to the \$5.0 million, or 100.0%, decrease in the U.S. Treasury portfolio, a decrease of \$8.4 million, or 100.0%, in certificates of deposit, a decrease of \$242,000, or 37.5%, in collateralized mortgage obligations, a decrease of \$188,000, or 31.2%, in securities available-for-sale and a decrease of \$1.2 million, or 3.6%, in tax-exempt industrial revenue bonds.

**Total Loans.** Total loans at December 31, 2014 increased \$34.4 million, or 7.0%, from \$489.3 million, or 83.3% of total assets, at December 31, 2013 to \$523.7 million, or 81.9% of total assets. The increase in total loans was due to the increase in commercial real estate loans of \$38.5 million, or 18.2%, to \$249.6 million, an increase in residential construction loans of \$2.0 million, or 32.6%, to \$8.1

million, an increase of \$2.4 million, or 7.5%, in home equity loans to \$34.5 million, and an increase in one- to four-family loans of \$6.2 million, or 5.5%, to \$118.7 million. These increases were partially offset by a decrease in commercial construction loans of \$2.7 million, or 6.9%, to \$35.8 million, and a decrease in commercial and industrial loans of \$12.2 million, or 14.1%, to \$74.3 million. In accordance with the Company's asset/liability management strategy and in an effort to reduce interest rate risk, the Company continues to sell fixed rate, low coupon residential real estate loans to the secondary market. For the year ended December 31, 2014, the Company sold \$4.7 million in low coupon residential real estate loans and currently services \$91.3 million in loans sold to the secondary market. In order to service our customers, the servicing rights will continue to be retained on all loans written and sold in the secondary market.

**Deposits and Borrowed Funds.** Total deposits increased \$33.8 million, or 7.5%, from \$449.8 million at December 31, 2013 to \$483.6 million at December 31, 2014. Core deposits, defined as savings accounts, money market accounts, demand deposit accounts and NOW accounts, increased \$19.4 million, or 6.6%, from \$292.5 million at December 31, 2013 to \$311.9 million at December 31, 2014. Money market accounts increased \$10.0 million, or 9.0%, to \$121.1 million, demand deposits increased \$7.1 million, or 7.8%, to \$97.9 million, savings accounts increased \$1.0 million, or 1.9%, to \$50.7 million, and NOW accounts increased \$1.4 million, or 3.4%, to \$42.2 million. Certificates of deposit increased \$14.4 million, or 9.2%, from \$157.2 million at December 31, 2013 to \$171.6 million at December 31, 2014. FHLB advances increased \$22.0 million, or 49.0%, from \$45.0 million at December 31, 2013 to \$67.0 million at December 31, 2014. FHLB advances increased to fund the \$34.4 million, or 7.0%, loan growth over the same period.

**Total Stockholders' Equity.** Stockholders' equity was \$88.1 million, or 13.8% of total assets, at December 31, 2014 compared to \$92.2 million, or 15.7% of total assets, at December 31, 2013. The Company's stockholders' equity decreased as a result of the \$578,000 net loss for the year ended December 31, 2014 and the \$1.4 million cash dividend paid during the year ended December 31, 2014, partially offset by an increase of \$303,000, or 8.5%, in stock-based compensation, and an increase of \$296,000, or 9.0%, in additional paid-in-capital. In addition, during the year ended December 31, 2014, the Company repurchased 174,915 shares of the Company stock at a cost of \$2.9 million, or \$16.36 average price per share and released 9,700 shares to fund employee stock options exercises. The Company's book value per share decreased by \$0.25, or 1.5%, from \$16.97 at December 31, 2013 to \$16.72 at December 31, 2014. The decrease in the book value was primarily due to the \$578,000 net loss and the cash dividend payment of \$1.4 million, or \$0.28 per share, made during the year ended December 31, 2014.

**Loans.** Our primary lending activity is the origination of loans secured by real estate. We originate one-to-four-family residential loans, commercial real estate loans and commercial business loans. To a lesser extent, we originate residential investment, construction and consumer loans.

Our residential real estate loan portfolio has increased from \$112.5 million, or 23.0% of total loans, at December 31, 2013 to \$118.7 million, or 22.7% of total loans, at December 31, 2014. In accordance with the Company's asset/liability management strategy and in an effort to reduce interest rate risk, the Company sold \$4.7 million of fixed rate, low coupon residential real estate loans originated in 2014 to the secondary market.

The commercial real estate portfolio increased \$38.5 million, or 18.2%, from \$211.2 million, or 43.1% of total loans, at December 31, 2013 to \$249.6 million, or 47.7% of total loans, at December 31, 2014 as a result of new commercial loan relationships. Commercial and industrial loans decreased \$12.2 million, or 14.1%, from \$86.5 million at December 31, 2013 to \$74.3 million at December 31, 2014 as a result of a \$2.0 million charge-off reported in the first quarter of 2014, a \$5.9 million payoff on a classified line of credit and other customer paydowns.

The construction loan portfolio decreased from \$44.6 million at December 31, 2013 to \$43.9 million at December 31, 2014. Commercial construction decreased \$2.7 million, or 6.9%, from \$38.4 million at December 31, 2013 to \$35.8 million at December 31, 2014 and residential construction increased \$2.0 million, or 32.6% to \$8.1 million.

The consumer and home equity loan portfolio increased \$2.7 million, or 7.8%, from \$34.5 million at December 31, 2013 to \$37.2 million at December 31, 2014, primarily due to the \$2.4 million, or 7.5% in Home Equity loans.



Loan Portfolio Composition. The following table sets forth the composition of the Company's loan portfolio in dollar amounts and as a percentage of the respective portfolio at the dates indicated.

|  | At December 31,        |         | 2013      |                  | 2012      |                  | 2011      |                  | 2010      |                  |  |
|--|------------------------|---------|-----------|------------------|-----------|------------------|-----------|------------------|-----------|------------------|--|
|  | 2014                   |         | Amount    | Percent of Total | Amount    | Percent of Total | Amount    | Percent of Total | Amount    | Percent of Total |  |
|  | (Dollars In Thousands) |         |           |                  |           |                  |           |                  |           |                  |  |
| Real estate loans                        |                        |         |           |                  |           |                  |           |                  |           |                  |  |
| Residential real estate                  | \$118,692              | 22.7 %  | \$112,524 | 23.0 %           | \$120,265 | 25.7 %           | \$123,294 | 27.6 %           | \$132,670 | 30.6 %           |  |
| Home equity                              | 34,508                 | 6.6 %   | 32,091    | 6.6 %            | 31,731    | 6.8 %            | 29,790    | 6.7 %            | 29,933    | 6.9 %            |  |
| Commercial                               | 249,632                | 47.7 %  | 211,161   | 43.1 %           | 189,472   | 40.4 %           | 174,761   | 39.0 %           | 162,107   | 37.4 %           |  |
| Total real estate loans                  | 402,832                | 77.0 %  | 355,776   | 72.7 %           | 341,468   | 72.9 %           | 327,845   | 73.3 %           | 324,710   | 74.9 %           |  |
| Construction loans:                      |                        |         |           |                  |           |                  |           |                  |           |                  |  |
| Residential                              | 8,129                  | 1.6 %   | 6,130     | 1.3 %            | 4,334     | 0.9 %            | 5,597     | 1.3 %            | 6,428     | 1.5 %            |  |
| Commercial                               | 35,786                 | 6.8 %   | 38,441    | 7.9 %            | 35,781    | 7.6 %            | 31,706    | 7.0 %            | 26,643    | 6.1 %            |  |
| Total construction loans                 | 43,915                 | 8.4 %   | 44,571    | 9.2 %            | 40,115    | 8.5 %            | 37,303    | 8.3 %            | 33,071    | 7.6 %            |  |
| Total real estate and construction loans | 446,747                | 85.4 %  | 400,347   | 81.9 %           | 381,583   | 81.4 %           | 365,148   | 81.6 %           | 357,781   | 82.5 %           |  |
| Consumer                                 | 2,662                  | 0.5 %   | 2,405     | 0.4 %            | 2,492     | 0.6 %            | 2,566     | 0.6 %            | 3,165     | 0.7 %            |  |
| Commercial and industrial                | 74,331                 | 14.1 %  | 86,540    | 17.7 %           | 84,583    | 18.0 %           | 79,412    | 17.8 %           | 72,847    | 16.8 %           |  |
| Total loans                              | 523,740                | 100.0 % | 489,292   | 100.0 %          | 468,658   | 100.0 %          | 447,126   | 100.0 %          | 433,793   | 100.0 %          |  |
| Deferred loan origination costs, net     | 944                    |         | 923       |                  | 917       |                  | 921       |                  | 945       |                  |  |
| Allowance for loan losses                | (4,927 )               |         | (4,596 )  |                  | (4,364 )  |                  | (4,576 )  |                  | (4,431 )  |                  |  |
| Loans, net                               | \$519,757              |         | \$485,619 |                  | \$465,211 |                  | \$443,471 |                  | \$430,307 |                  |  |

Loan Maturity. The following table sets forth certain information at December 31, 2014 regarding the dollar amount of loan principal repayments becoming due during the periods indicated. The table does not include any estimate of prepayments which significantly shorten the average life of all loans and may cause our actual repayment experience to differ from that shown. Demand loans having no stated schedule of repayments and no stated maturity are reported as due in one year or less. Real estate mortgage loans include residential and commercial real estate loans and home equity loans.

|             | Real Estate Mortgage<br>(In Thousands) | Construction | Commercial | Consumer | Total Loans |
|-------------|--|--------------|------------|----------|-------------|
| Amounts due |  |              |            |          |             |

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|                                  |           |          |          |         |           |
|----------------------------------|-----------|----------|----------|---------|-----------|
| One year or less                 | \$2,066   | \$21,966 | \$48,376 | \$147   | \$72,555  |
| More than one year to five years | 6,499     | 10,882   | 19,582   | 1,692   | 38,655    |
| More than five years             | 394,267   | 11,067   | 6,373    | 823     | 412,530   |
| Total amount due                 | \$402,832 | \$43,915 | \$74,331 | \$2,662 | \$523,740 |

The following table sets forth the dollar amount of all loans at December 31, 2014 that are due after December 31, 2015 that have either fixed interest rates or adjustable interest rates. The amounts shown below exclude unearned interest on consumer loans and deferred loan origination costs. Real estate loans include residential and commercial real estate loans and home equity loans.

|                   | Due After December 31, 2015 |            |           |
|-------------------|-----------------------------|------------|-----------|
|                   | Fixed                       | Adjustable | Total     |
|                   | (In Thousands)              |            |           |
| Real estate loans | \$47,305                    | \$353,461  | \$400,766 |
| Construction      | 4,495                       | 17,454     | 21,949    |
| Commercial        | 21,749                      | 4,206      | 25,955    |
| Consumer          | 2,468                       | 47         | 2,515     |
| Total loans       | \$76,017                    | \$375,168  | \$451,185 |

Investment Securities. The investment securities portfolio consists primarily of tax-exempt industrial revenue bonds, collateralized mortgage obligations and marketable equity securities. Total investment securities decreased \$15.0 million, or 30.6%, from \$49.2 million at December 31, 2013 to \$34.2 million at December 31, 2014. The \$15.0 million decrease was primarily due to maturities in certificates of deposit of \$8.4 million, maturities of U.S. Treasury securities of \$5.0 million, paydowns of tax-exempt industrial revenue bonds of \$1.2 million, and paydowns of collateralized mortgage obligations of \$242,000.

The amortized cost of available-for-sale securities decreased \$153,000, or 29.3%, from \$522,000 at December 31, 2013 to \$369,000 at December 31, 2014, due to the sale of 10,000 shares of common stock issued by one company in the financial industry with a realized gain of \$34,000. The fair value of available-for-sale securities decreased \$188,000, or 31.2%, from \$602,000 at December 31, 2013 to \$414,000 at December 31, 2014 due to the sale of the 10,000 shares. At December 31, 2014, available-for-sale securities had a net unrealized gain of \$45,000.

Total investment securities decreased \$11.0 million, or 18.2%, from \$60.1 million at December 31, 2012 to \$49.1 million at December 31, 2013. The decrease was primarily due to maturities of U.S. Treasury securities of \$20.2 million, paydowns of tax-exempt industrial revenue bonds of \$1.1 million, \$16.2 million of maturities in certificates of deposit, and maturities of collateralized mortgage obligations of \$535,000. These decreases were partially offset by purchases of U.S. Treasury securities and certificates of deposit of \$11.5 million and \$15.5 million, respectively.

The amortized cost of available-for-sale securities decreased \$59,000, or 10.2%, from \$581,000 at December 31, 2012 to \$522,000 at December 31, 2013, due to the sale of 6,000 shares of common stock issued by one company in the financial industry with a realized gain of \$37,000. The fair value of available-for-sale securities decreased \$19,000, or 3.1%, from \$621,000 at December 31, 2012 to \$602,000 at December 31, 2013 due to the sale of the 6,000 shares. At December 31, 2013, available-for-sale securities had a net unrealized gain of \$80,000.

During 2012, the Company recorded an OTTI charge of \$37,000 relating to three securities issued by one company in the financial industry. There were no sales of available-for-sale securities during 2012.

At December 31, 2014 and 2013, there were no investments in a single company or entity (other than the U.S. Government) that had an aggregate book value in excess of 10% of our equity.

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

|   | At December 31, |          | 2013      |          | 2012      |          |
|---|-----------------|----------|-----------|----------|-----------|----------|
|   | 2014            | Fair     | Amortized | Fair     | Amortized | Fair     |
|   | Cost            | Value    | Cost      | Value    | Cost      | Value    |
|   | (In Thousands)  |          |           |          |           |          |
| Available-for-sale securities             |                 |          |           |          |           |          |
| Marketable equity securities <sup>1</sup> | \$369           | \$414    | \$522     | \$602    | \$581     | \$621    |
| Total available-for-sale securities       | \$369           | \$414    | \$522     | \$602    | \$581     | \$621    |
| Held-to-maturity securities               |                 |          |           |          |           |          |
| U.S. Treasury securities                  | \$—             | \$—      | \$5,000   | \$5,000  | \$13,691  | \$13,693 |
| Corporate and industrial revenue bonds    | 33,344          | 33,811   | 34,588    | 35,269   | 35,656    | 43,137   |
| Certificates of deposit                   | —               | —        | 8,373     | 8,388    | 9,041     | 9,045    |
| Collateralized mortgage obligations       | 403             | 418      | 645       | 681      | 1,180     | 1,233    |
| Total held-to-maturity securities:        | \$33,747        | \$34,229 | \$48,606  | \$49,338 | \$59,568  | \$67,108 |
| Total investment securities               | \$34,116        | \$34,643 | \$49,128  | \$49,940 | \$60,149  | \$67,729 |

<sup>1</sup> Does not include investments in restricted stock consisting of FHLB stock of \$3.9 million at December 31, 2014 and 2013 and \$4.3 million at December 31, 2012. Investment in Banker's Bank Northeast stock of \$183,000 at December 31, 2014, 2013, and 2012 is included.

The table below sets forth the stated maturities and weighted average yields of debt securities at December 31, 2014. Weighted average yields on tax-exempt securities are not presented on a tax equivalent basis because the impact would be insignificant.

|                                     | One Year or Less |                        | More than One Year to Five Years |                        | More than Five Years to Ten Years |                        | More than Ten Years |                        | Total          |                        |
|-------------------------------------|------------------|------------------------|----------------------------------|------------------------|-----------------------------------|------------------------|---------------------|------------------------|----------------|------------------------|
|                                     | Amortized Cost   | Weighted Average Yield | Amortized Cost                   | Weighted Average Yield | Amortized Cost                    | Weighted Average Yield | Amortized Cost      | Weighted Average Yield | Amortized Cost | Weighted Average Yield |
| (Dollars in Thousands)              |                  |                        |                                  |                        |                                   |                        |                     |                        |                |                        |
| Held-to-maturity securities         |                  |                        |                                  |                        |                                   |                        |                     |                        |                |                        |
| Industrial revenue bonds            | \$—              | —                      | \$7,883                          | 4.25 %                 | \$—                               | —                      | \$25,461            | 4.10 %                 | \$33,344       | 4.14 %                 |
| Collateralized mortgage obligations | —                | —                      | 403                              | 0.22 %                 | —                                 | —                      | —                   | —                      | 403            | 0.22 %                 |
| Total held-to-maturity securities   | \$—              | —                      | \$8,286                          | 4.47 %                 | \$—                               | 4.47 %                 | \$25,461            | 4.10 %                 | \$33,747       | 4.19 %                 |

**Restricted Equity Securities.** At December 31, 2014 and 2013, the Company held \$3.9 million of FHLB stock. This stock is restricted and must be held as a condition of membership in the FHLB and as a condition for the Bank to borrow from the FHLB. The Company periodically evaluates its investment in FHLB stock for impairment based on, among other factors, the capital adequacy of the FHLB and its overall financial condition. No impairment losses have been recorded through December 31, 2014. The Company will continue to monitor its investment in FHLB stock. For additional information regarding our FHLB stock, see Note 3 to the notes to the consolidated financial statements. At December 31, 2014 and 2013, the Company held \$183,000 of Banker's Bank Northeast stock. The stock is restricted and carried at cost. The stock is evaluated for impairment based on an estimate of the ultimate recovery to par value.

**Deposits.** Our primary source of funds are deposits, which are comprised of certificates of deposit, money market deposit accounts, demand deposits, passbook accounts, and NOW accounts. These deposits are provided primarily by individuals and businesses within our market areas. At December 31, 2014, 2013 and 2012, we did not use brokered deposits as a source of funding.

Total deposits increased \$33.8 million, or 7.5%, from \$449.8 million at December 31, 2013 to \$483.6 million at December 31, 2014. Core deposits, defined as savings accounts, money market accounts, demand deposit accounts and NOW accounts, increased \$19.4 million, or 6.6%, from \$292.5 million at December 31, 2013 to \$311.9 million at December 31, 2014. Money market accounts increased \$10.0 million, or 9.0%, to \$121.1 million, demand deposits increased \$7.1 million, or 7.8%, to \$97.9 million, savings accounts increased \$1.0 million, or 1.9%, to \$50.7 million, and NOW accounts increased \$1.4 million, or 3.4%, to \$42.2 million. Certificates of deposit increased \$14.4 million, or 9.2%, from \$157.2 million at December 31, 2013 to \$171.6 million at December 31, 2014. The increase in certificates of deposit was the result of management's focus to replace maturing high cost accounts with lower cost accounts by offering promotional rates which are lower than the accounts scheduled to reprice. Demand accounts increased due to increases in commercial accounts as well as an increase in low cost relationship focused transaction and savings accounts.

At December 31, 2013, deposits increased \$16.4 million, or 3.5%, to \$449.8 million from \$466.2 million at December 31, 2012. The increase was primarily due to increases in NOW accounts of \$4.1 million, or 11.1%, demand accounts of \$15.5 million, or 20.5% and savings accounts of \$873,000, or 1.8%. These increases were partially offset by decreases in certificates of deposit of \$20.2 million, or 11.4% and money market accounts of \$16.6 million, or 13.0%. The decrease in certificates of deposits was mainly attributed to the strategic run-off of high cost accounts as a result of management's focus to lower the cost of deposits and allow higher cost, short-term time deposits to mature without renewals. Demand accounts increased due to increases in municipal and commercial accounts as well as an increase in low cost relationship focused transaction and savings accounts.

The following table sets forth the distribution of the Company's deposit accounts as of the dates indicated.

|                               | December 31,   |           |           |
|-------------------------------|----------------|-----------|-----------|
|                               | 2014           | 2013      | 2012      |
|                               | (In Thousands) |           |           |
| Demand deposits               | \$97,922       | \$90,869  | \$75,407  |
| NOW accounts                  | 42,177         | 40,774    | 36,711    |
| Savings accounts              | 50,716         | 49,755    | 48,882    |
| Money market deposit accounts | 121,106        | 111,126   | 127,730   |
| Certificates of deposit       | 171,637        | 157,242   | 177,447   |
| Total deposits                | \$483,558      | \$449,766 | \$466,177 |

The following table sets forth certificates of deposit of the Company classified by interest rate as of the dates indicated:

|                               | December 31,   |           |           |
|-------------------------------|----------------|-----------|-----------|
|                               | 2014           | 2013      | 2012      |
|                               | (In Thousands) |           |           |
| Interest rate                 |                |           |           |
| Less than 1.0%                | \$43,091       | \$66,675  | \$64,651  |
| 1.00% to 1.99%                | 96,362         | 32,466    | 29,669    |
| 2.00% to 2.99%                | 19,876         | 29,669    | 38,082    |
| 3.00% to 3.99%                | 12,308         | 28,432    | 35,183    |
| 4.00% to 4.99%                | —              | —         | 9,862     |
| Total certificates of deposit | \$171,637      | \$157,242 | \$177,447 |

The following table sets forth maturities of certificates of deposit by year of maturity and interest rate as of December 31, 2014:

|                               | 2015           | 2016     | 2017     | 2018     | 2019    | Total     |
|-------------------------------|----------------|----------|----------|----------|---------|-----------|
|                               | (In Thousands) |          |          |          |         |           |
| Interest rate                 |                |          |          |          |         |           |
| Less than 1.0%                | \$37,547       | \$4,657  | \$882    | \$5      | \$—     | \$43,091  |
| 1.00% to 1.99%                | 43,661         | 21,754   | 11,400   | 12,719   | 6,828   | 96,362    |
| 2.00% to 2.99%                | 10,514         | 8,098    | —        | 1,264    | —       | \$19,876  |
| 3.00% to 3.99%                | 12,308         | —        | —        | —        | —       | 12,308    |
| Total certificates of deposit | \$104,030      | \$34,509 | \$12,282 | \$13,988 | \$6,828 | \$171,637 |

As of December 31, 2014, the aggregate amount of outstanding certificates of deposits in amounts greater than or equal to \$100,000 was \$88.2 million, or 51.4%, of total certificates of deposits. The following table sets forth the maturity of those certificates of deposits as of December 31, 2014:

| Maturity Period                      | Amount                 | Weighted Average Rate |   |
|--------------------------------------|------------------------|-----------------------|---|
|                                      | (Dollars in Thousands) |                       |   |
| Three months or less                 | \$9,040                | 0.89                  | % |
| Over three months through six months | 18,267                 | 0.99                  | % |

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|   |          |      |   |
|---|----------|------|---|
| Over six months through 12 months                                 | 26,636   | 1.83 | % |
| Over 12 months  | 34,270   | 1.41 | % |
| Total certificates of deposit greater than or equal to \$100,000: | \$88,213 | 1.40 | % |

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Borrowings. The Company utilizes borrowings from a variety of sources to supplement our supply of funds for loans and investments.

|  | Years Ended December 31, |          |          |   |
|--|--------------------------|----------|----------|---|
|  | 2014                     | 2013     | 2012     |   |
|  | (Dollars in Thousands)   |          |          |   |
| Maximum amount of advances outstanding at any month-end during the year: |                          |          |          |   |
| FHLB advances  | \$67,039                 | \$44,992 | \$58,308 |   |
| Securities sold under agreements to repurchase                           | —                        | 15,312   | 12,982   |   |
| Average advances outstanding during the year:                            |                          |          |          |   |
| FHLB advances  | \$57,182                 | \$29,202 | \$46,907 |   |
| Securities sold under agreements to repurchase                           | —                        | 7,243    | 9,027    |   |
| Weighted average interest rate during the year:                          |                          |          |          |   |
| FHLB advances  | 1.59                     | % 2.41   | % 2.56   | % |
| Securities sold under agreements to repurchase                           | —                        | % 0.12   | % 0.14   | % |
| Balance outstanding at end of year:                                      |                          |          |          |   |
| FHLB advances  | \$67,039                 | \$44,992 | \$33,332 |   |
| Securities sold under agreements to repurchase                           | —                        | —        | —        |   |
| Weighted average interest rate at end of year:                           |                          |          |          |   |
| FHLB advances  | 1.43                     | % 1.93   | % 2.39   | % |
| Securities sold under agreements to repurchase                           | —                        | % —      | % 0.12   | % |

FHLB advances increased \$22.0 million, or 49.0%, to \$67.0 million at December 31, 2014 from \$45.0 million at December 31, 2013. The increase was due to long-term advances of \$33.0 million to fund loan growth and minimize interest rate risk, partially offset by paydowns of long-term advances of \$11.0 million.

FHLB advances increased \$11.7 million, or 35.0%, to \$45.0 million at December 31, 2013 from \$33.3 million at December 31, 2012. The increase was due to long-term advances of \$21.0 million to fund loan growth and minimize interest rate risk, partially offset by pay downs of long-term advances of \$9.3 million.

At December 31, 2013, securities sold under agreements to repurchase decreased to zero from \$9.8 million at December 31, 2012. At December 31, 2014, securities sold under agreements to repurchase were zero and all agreements were terminated in October of 2013.

At December 31, 2014, the Company had an Ideal Way Line of Credit with the FHLB of \$2.0 million and the ability to borrow a total of \$44.5 million with the Federal Reserve Bank of Boston's discount window. In addition, we had the ability to borrow a total of \$4.0 million from Banker's Bank Northeast. As of December 31, 2014, the Company did not utilize any of these contingency funding sources.

#### Analysis of Net Interest Income

Net interest income represents the difference between income on interest-earning assets and expense on interest-bearing liabilities. Net interest income depends on the relative amounts of interest-earning assets and interest-bearing liabilities and the interest rate earned or paid on them.

Average Balance Sheet. The following table sets forth information relating to the Company for the years ended December 31, 2014, 2013 and 2012. The average yields and costs are derived by dividing interest income or interest expense by the average balance of interest-earning assets or interest-bearing liabilities, respectively, for the periods

shown. Average balances are derived from average daily balances. The yields include fees which are considered adjustments to yields. Loan interest and yield data does not include any accrued interest from non-accruing loans.

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Average Balance, Interest and Yield/Rate Analysis

December 31,

2014

2013

2012

| (Dollars in Thousands)             | Average Balance | Interest | Average Yield/Rate | Average Balance | Interest | Average Yield/Rate | Average Balance | Interest | Average Yield/Rate |
|------------------------------------|-----------------|----------|--------------------|-----------------|----------|--------------------|-----------------|----------|--------------------|
| Interest-earning assets:           |                 |          |                    |                 |          |                    |                 |          |                    |
| Investments (1)                    | \$42,005        | \$2,607  | 6.21 %             | \$64,405        | \$2,754  | 4.28 %             | \$68,257        | \$2,721  | 3.99 %             |
| Loans:                             |                 |          |                    |                 |          |                    |                 |          |                    |
| Residential real estate loans      | 115,791         | 4,483    | 3.87 %             | 115,402         | 4,717    | 4.09 %             | 123,102         | 5,547    | 4.51 %             |
| Home equity loans                  | 32,470          | 1,124    | 3.46 %             | 31,840          | 1,151    | 3.61 %             | 30,744          | 1,191    | 3.87 %             |
| Commercial real estate loans       | 223,988         | 10,635   | 4.75 %             | 187,751         | 9,840    | 5.24 %             | 179,564         | 10,122   | 5.64 %             |
| Residential construction loans     | 7,477           | 299      | 4.00 %             | 4,778           | 198      | 4.14 %             | 5,208           | 226      | 4.34 %             |
| Commercial construction loans      | 42,550          | 1,762    | 4.14 %             | 34,824          | 1,574    | 4.52 %             | 38,089          | 1,874    | 4.92 %             |
| Consumer loans                     | 2,497           | 160      | 6.41 %             | 2,376           | 156      | 6.57 %             | 2,553           | 172      | 6.74 %             |
| Commercial and industrial loans    | 81,789          | 3,261    | 3.99 %             | 87,190          | 3,688    | 4.23 %             | 81,566          | 3,518    | 4.31 %             |
| Loans, net (2)                     | 506,562         | 21,724   | 4.29 %             | 464,161         | 21,324   | 4.59 %             | 460,826         | 22,649   | 4.91 %             |
| Other                              | 17,602          | 41       | 0.23 %             | 21,069          | 55       | 0.26 %             | 29,664          | 64       | 0.22 %             |
| Total interest-earning assets      | 566,169         | 24,372   | 4.30 %             | 549,635         | 24,133   | 4.39 %             | 558,747         | 25,434   | 4.55 %             |
| Noninterest-earning assets         | 42,037          |          |                    | 41,307          |          |                    | 44,665          |          |                    |
| Less: Allowance for loan losses    | (4,685 )        |          |                    | (4,362 )        |          |                    | (4,501 )        |          |                    |
| Total assets                       | \$603,521       |          |                    | \$586,580       |          |                    | \$598,911       |          |                    |
| Interest-bearing liabilities:      |                 |          |                    |                 |          |                    |                 |          |                    |
| Deposits:                          |                 |          |                    |                 |          |                    |                 |          |                    |
| Money market deposit accounts      | \$113,205       | \$339    | 0.30 %             | \$120,405       | \$378    | 0.31 %             | \$109,168       | \$358    | 0.33 %             |
| Savings accounts (3)               | 50,341          | 52       | 0.10 %             | 49,851          | 52       | 0.10 %             | 48,679          | 51       | 0.10 %             |
| NOW accounts                       | 41,761          | 322      | 0.77 %             | 39,435          | 371      | 0.94 %             | 31,401          | 322      | 1.03 %             |
| Certificates of deposit            | 157,564         | 2,060    | 1.31 %             | 170,195         | 2,834    | 1.67 %             | 196,491         | 3,681    | 1.87 %             |
| Total interest-bearing deposits    | 362,871         | 2,773    | 0.76 %             | 379,886         | 3,635    | 0.96 %             | 385,739         | 4,412    | 1.14 %             |
| Total interest-bearing borrowings: |                 |          |                    |                 |          |                    |                 |          |                    |
| FHLB advances                      | 57,182          | 910      | 1.59 %             | 29,202          | 705      | 2.41 %             | 46,907          | 1,202    | 2.56 %             |
|                                    | —               | —        | —                  | 7,243           | 9        | 0.12 %             | 9,027           | 13       | 0.14 %             |

Securities sold under  
agreement to  
repurchase

|   |           |       |      |   |           |       |      |   |           |       |      |   |
|---|-----------|-------|------|---|-----------|-------|------|---|-----------|-------|------|---|
| Total<br>interest-bearing<br>borrowings       | 57,182    | 910   | 1.59 | % | 36,445    | 714   | 1.96 | % | 55,934    | 1,215 | 2.17 | % |
| Total<br>interest-bearing<br>liabilities:     | 420,053   | 3,683 | 0.88 | % | 416,331   | 4,349 | 1.04 | % | 441,673   | 5,627 | 1.27 | % |
| Demand deposits                               | 92,347    |       |      |   | 77,949    |       |      |   | 66,840    |       |      |   |
| Other<br>noninterest-bearing<br>liabilities   | 546       |       |      |   | 887       |       |      |   | 464       |       |      |   |
| Total liabilities                             | 512,946   |       |      |   | 495,167   |       |      |   | 508,977   |       |      |   |
| Total stockholders'<br>equity                 | 90,575    |       |      |   | 91,413    |       |      |   | 89,934    |       |      |   |
| Total liabilities and<br>stockholders' equity | \$603,521 |       |      |   | \$586,580 |       |      |   | \$598,911 |       |      |   |
| Net interest-earning<br>assets                | \$146,116 |       |      |   | \$133,304 |       |      |   | \$117,074 |       |      |   |

Net interest income  
(fully-taxable  
equivalent)

|  |          |  |        |   |          |  |        |   |          |  |        |   |
|--|----------|--|--------|---|----------|--|--------|---|----------|--|--------|---|
|  | 20,689   |  |        |   | 19,784   |  |        |   | 19,807   |  |        |   |
| Less: tax equivalent adjustment<br>(1)                                       | (1,018 ) |  |        |   | (1,064 ) |  |        |   | (1,037 ) |  |        |   |
| Net interest income  | \$19,671 |  |        |   | \$18,720 |  |        |   | \$18,770 |  |        |   |
| Net interest rate<br>spread (fully-taxable<br>equivalent) (4)                |          |  | 3.42   | % |          |  | 3.35   | % |          |  | 3.28   | % |
| Net interest margin<br>(fully-taxable<br>equivalent) (5)                     |          |  | 3.65   | % |          |  | 3.60   | % |          |  | 3.54   | % |
| Ratio of<br>interest-earning<br>assets<br>to interest-bearing<br>liabilities |          |  | 134.79 | % |          |  | 132.02 | % |          |  | 126.51 | % |

- (1) Municipal securities income and net interest income are presented on a tax equivalent basis using a tax rate of 41%.  
The tax equivalent adjustment is deducted from the tax equivalent net interest income to agree to the amount reported on the statement of operations. See 'Explanation of Use of Non-GAAP Financial Measurements'.
- (2) Loans, net excludes loans held for sale and the allowance for loan losses and includes nonperforming loans.
- (3) Savings accounts include mortgagors' escrow deposits.
- (4) Tax equivalent interest rate spread represents the difference between the weighted average yield on interest-earning assets and the weighted average cost of interest-bearing liabilities  
Tax equivalent net interest margin represents tax equivalent net interest income divided by total average interest-earning assets.
- (5) interest-earning assets.

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 the Company's tax equivalent 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.

|                                      | Year Ended<br>December 31, 2014<br>Compared to<br>December 31, 2013<br>Increase (Decrease)<br>Due to |         |         | Year Ended<br>December 31, 2013<br>Compared to<br>December 31, 2012<br>Increase (Decrease)<br>Due to |            |            |
|--------------------------------------|--|---------|---------|--|------------|------------|
|                                      | Volume   | Rate    | Net     | Volume   | Rate       | Net        |
| (Dollars in Thousands)               |  |         |         |  |            |            |
| <b>Interest-earning assets:</b>      |  |         |         |  |            |            |
| Investment securities                | \$(1,146   | ) \$999 | \$(147  | ) \$(159   | ) \$192    | \$33       |
| <b>Loans:</b>                        |  |         |         |  |            |            |
| Residential real estate              | 16   | (250    | ) (234  | ) (407   | ) (491     | ) (898     |
| Home equity                          | 23   | (50     | ) (27   | ) 42   | (80        | ) (38      |
| Commercial real estate               | 1,779  | (984    | ) 795   | 396  | (611       | ) (215     |
| Residential construction             | 108  | (7      | ) 101   | (18  | ) (10      | ) (28      |
| Commercial construction              | 328  | (140    | ) 188   | (154   | ) (146     | ) (300     |
| Consumer                             | 8  | (4      | ) 4     | (10  | ) (6       | ) (16      |
| Commercial and industrial            | (221   | ) (206  | ) (427  | ) 239  | (69        | ) 170      |
| Total loans                          | 2,041  | (1,641  | ) 400   | 88   | (1,413     | ) (1,325   |
| Other                                | (8   | ) (6    | ) (14   | ) (21  | ) 12       | (9         |
| Total interest-earning assets        | \$887  | \$(648  | ) \$239 | \$(92  | ) \$(1,209 | ) \$(1,301 |
| <b>Interest-bearing liabilities:</b> |  |         |         |  |            |            |
| <b>Deposits:</b>                     |  |         |         |  |            |            |
| Money market deposit accounts        | \$(23  | ) \$(16 | ) \$(39 | ) \$36   | \$(16      | ) \$20     |
| Savings accounts (1)                 | —  | —       | —       | 1  | —          | 1          |

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|   |       |        |        |        |        |          |
|---|-------|--------|--------|--------|--------|----------|
| NOW accounts                                  | 21    | (70    | ) (49  | ) 77   | (28    | ) 49     |
| Certificates of deposit                       | (198  | ) (576 | ) (774 | ) (463 | ) (384 | ) (847   |
| Total interest-bearing deposits               | (200  | ) (662 | ) (862 | ) (349 | ) (428 | ) (777   |
| FHLB advances                                 | 511   | (306   | ) 205  | (431   | ) (66  | ) (497   |
| Securities sold under agreement to repurchase | (4    | ) (5   | ) (9   | ) (2   | ) (2   | ) (4     |
| Total interest-bearing borrowings             | 507   | (311   | ) 196  | (433   | ) (68  | ) (501   |
| Total interest-bearing liabilities            | 307   | (973   | ) (666 | ) (782 | ) (496 | ) (1,278 |
| Increase in net interest income               | \$580 | \$325  | \$905  | \$690  | \$(713 | ) \$(23  |

(1) Includes interest on mortgagors' escrow deposits.  
Results of Operations

Comparison of Operating Results for the Years Ended December 31, 2014 and December 31, 2013

**Net Loss.** The Company reported a net loss of \$578,000, or \$0.12 basic loss per share, for the year ended December 31, 2014, compared to net income of \$2.6 million, or \$0.51 basic earnings per share, for the year ended December 31, 2013. The net loss reported for the year ended December 31, 2014 was due to the increase in the provision for loan losses of \$4.8 million, or 1,140.2%, resulting primarily from charge-offs taken in three loan relationships, the increase in non-interest expense of \$745,000, or 4.1%, a decrease in non-interest income of \$283,000, or 9.1%, partially offset by the increase in net interest income of \$951,000, or 5.1%, and the decrease in income tax expense of \$1.8 million, or 260.8%. The tax benefit was the result of a change in the effective tax rate of 21.2% for the year ended December 31, 2013 to 65.7% for the year ended December 31, 2014, due to the net loss reported as well as the benefit of the tax-exempt investment income.

**Net Interest Income.** The tables on the preceding pages set forth the components of the Company's net interest income, yields on interest-earning assets and interest-bearing liabilities, and the effect on net interest income arising from changes in volume and rate. There was a increase in tax equivalent net interest income for the year ended December 31, 2014 of \$905,000, or 4.6%, to \$20.7 million, for the same period in 2013. Based on the methodology used in the Rate/Volume Analysis table, the increase in the volume of interest-earning assets increased interest and dividend income \$887,000. The decrease in the volume of interest bearing deposits, specially certificates of deposits, decreased interest expense \$200,000. The increase in the volume of interest-bearing borrowings increased interest expense \$511,000. The changes in volume had the effect of increasing net interest income \$580,000. The changes in the rates of interest-bearing liabilities decreased interest expense \$973,000, partially offset by changes in the rates of interest-earning assets which decreased interest income \$648,000. The changes in the rates of interest-earning assets and interest-bearing liabilities had the effect of increasing net interest income \$325,000. Net interest margin, on a tax equivalent basis, increased from 3.60% for the year ended December 31, 2013 to 3.65% for the year ended December 31, 2014.

**Interest and Dividend Income.** Interest and dividend income, on a tax equivalent basis, increased \$239,000, or 1.0%, to \$24.4 million for the year ended December 31, 2014 compared to \$24.1 million for the year ended December 31, 2013, largely reflecting the increase in income from loans of \$400,000, or 1.9%, partially offset by the decrease in income, on a tax equivalent basis, from investments of \$147,000, or 5.3%. Average interest-earning assets totaled \$566.2 million for the year ended December 31, 2014 compared to \$549.6 million for the same period 2013, representing an decrease of \$16.5 million, or 3.0%. Average loans increased \$42.4 million, or 9.1%, primarily due to commercial real estate lending, partially offset by the decrease in commercial and industrial loan activity. Average investment securities decreased \$22.4 million, or 34.8%, primarily due to maturities of U.S. Treasury securities and certificates of deposit and pay downs of collateralized mortgage obligations and tax-exempt industrial revenue bonds.

The tax equivalent yield on interest-earning assets decreased 3 basis points to 4.30% for the year ended December 31, 2014 from 4.39% for the year ended December 31, 2013, largely attributable to lower market rates of interest in 2014 and the increase in nonperforming loans.

**Interest Expense.** Total interest expense decreased \$666,000, or 15.3%, to \$3.7 million for the year ended December 31, 2014 from \$4.3 million for the year ended December 31, 2013. The decrease in interest expense was primarily due to the decrease in interest rates. Average interest-bearing liabilities totaled \$420.1 million for the year ended December 31, 2014, representing an increase of \$3.7 million, or 0.9%, from \$416.3 million for the same period in 2013, primarily due to the decrease in average interest-bearing deposits of \$17.0 million, or 4.5%, and an increase in average interest-bearing borrowings of \$20.7 million, or 56.9%. The rate paid on interest-bearing liabilities decreased 16 basis points to 0.88% for the year ended December 31, 2014 from 1.04% in 2013, reflecting the lower interest rate environment.

**Provision for Loan Losses.** The provision for loan losses increased \$4.8 million, or 1,140.2%, from \$425,000, for the year ended December 31, 2013 to \$5.3 million for the year ended December 31, 2014, due to charge-offs taken in three relationships. Charge-offs for the years ended December 31, 2014 and 2013 were \$5.1 million and \$493,000, respectively, partially offset by recoveries of \$181,000 and \$300,000 for the years ended December 31, 2014 and December 31, 2013, respectively.

The allowance for loan losses of \$4.9 million at December 31, 2014 represented 0.94% of total loans, as compared to an allowance for loan losses of \$4.6 million, representing 0.94% of total loans at December 31, 2013. An analysis of the changes in the allowance for loan losses is presented under “Risk Management – Analysis and Determination of the Allowance for Loan Losses” and in Note 4 of the financial statements.

**Non-interest Income.** Non-interest income decreased \$283,000, or 9.1%, from \$3.1 million for the year ended December 31, 2013 to \$2.8 million for the year ended December 31, 2014. The decrease in non-interest income was due to the \$425,000, or 68.3%, decrease in income from net loan sales and servicing, partially offset by the \$142,000, or 6.4%, increase in income from customer service fees and commissions, and a \$33,000, or 20.9%, decrease in net losses on the sale of OREO from \$158,000 for the year ended December 31, 2013 to \$125,000 for the year ended December 31, 2014.

Non-interest Expenses. Non-interest expense increased \$745,000, or 4.1%, for the year ended December 31, 2014 compared to the year ended December 31, 2013. Non-interest expense increased due to the increase of \$339,000, or 218.7%, in foreclosure and loan collection related expenses, an increase of \$291,000, or 44.6%, in professional fees, an increase of \$146,000, or 11.7%, in data processing, an increase of \$193,000, or 83.5%, in FDIC insurance expense, an increase of \$27,000, or 3.9%, in furniture and equipment, an increase of \$25,000, or 1.9%, in occupancy expense, and an increase of \$3,000, or 0.1%, in other non-interest expense. These increases were partially offset by a decrease in salaries and benefits of \$238,000, or 2.3%, a decrease of \$31,000, or 10.7%, in stationery, supplies and postage, and a decrease of \$10,000, or 1.7%, in advertising expense.

Income Taxes. Income tax expense decreased \$1.8 million, or 260.8% from a tax expense of \$687,000 for the year ended December 31, 2013 to a tax benefit of \$1.1 million for the year ended December 31, 2014. The tax benefit was the result of a change in the effective tax rate of 21.2%, for the year ended December 31, 2013 to 65.7%, for the year ended December 31, 2014, due to the net loss reported as well as the benefit of the tax-exempt investment income.

As of December 31, 2013, a valuation allowance of \$54,000 was established against deferred tax assets related to the uncertain utilization of the charitable contribution carry forward created primarily by the donation to the Foundation as part of the conversion, as well as to a capital loss carry forward. The decrease in the valuation reserve in 2014 is due to an increase in expected future capital gains. The judgment applied by management considers the likelihood that sufficient taxable income will be realized within the carry forward period in light of our tax planning strategies and changes in market conditions. See Note 10 for additional income tax disclosures.

#### Comparison of Operating Results for the Years Ended December 31, 2013 and December 31, 2012

Net Income. The Company had net income of \$2.6 million, or \$0.51 basic earnings per share, for the year ended December 31, 2013 as compared to net income of \$2.5 million, or \$0.49 basic earnings per share, for the year ended December 31, 2012. The \$88,000, or 3.6%, increase in net income for the year ended December 31, 2013 compared to the year ended December 31, 2012, was primarily due to the decrease in non-interest expense of \$150,000, or 0.8%, a decrease in provision for loan losses of \$17,000, or 3.8%, and an increase of \$77,000, or 2.5%, in non-interest income partially offset by a decrease of \$50,000, or 0.3%, in net interest income and a \$106,000, or 18.2%, increase in income tax expense.

Net Interest Income. The tables on the preceding pages set forth the components of the Company's net interest income, yields on interest-earning assets and interest-bearing liabilities, and the effect on net interest income arising from changes in volume and rate. There was a decrease in tax equivalent net interest income for the year ended December 31, 2013 of \$23,000, or 0.1%, to \$19.8 million compared to the same period in 2012. The decrease in the volume of interest-earning assets decreased interest and dividend income \$92,000. The increase in the volume of interest bearing deposits, especially, money market accounts, NOW accounts and savings accounts increased interest expense \$114,000, partially offset by the decrease in the volume of certificates of deposit which decreased interest expense \$463,000, for an overall decrease of \$349,000. In addition, the volume of interest-bearing borrowings decreased interest expense \$433,000. The changes in volume had the effect of increasing net interest income \$690,000. The changes in the rates of interest-earning assets decreased interest income \$1.2 million, partially offset by changes in the rates of interest-bearing liabilities which decreased interest expense \$496,000. The changes in the rates of interest-earning assets and interest-bearing liabilities had the effect of decreasing net interest income \$713,000. Net interest margin, on a tax equivalent basis, increased from 3.54% for the year ended December 31, 2012 to 3.60% for the year ended December 31, 2013.

Interest and Dividend Income. Interest and dividend income, on a tax equivalent basis, decreased \$1.3 million, or 5.1%, to \$24.1 million for the year ended December 31, 2013 compared to \$25.4 million for the year ended December



31, 2012, largely reflecting the decrease in income from loans. Average interest-earning assets totaled \$549.6 million for the year ended December 31, 2013 compared to \$558.7 million for the same period 2012, representing a decrease of \$9.1 million, or 1.6%. Average loans increased \$3.3 million, or 0.7%, primarily due to commercial lending and partially offset by the sale of low-coupon fixed rate residential real estate loans originated in 2013 to the secondary market. Average investment securities decreased \$3.9 million, or 5.6%, primarily due to maturities of U.S. Treasury securities and certificates of deposit and pay downs of collateralized mortgage obligations and tax-exempt industrial revenue bonds. The tax equivalent yield on interest-earning assets decreased 16 basis points to 4.39% for the year ended December 31, 2013 from 4.55% for the year ended December 31, 2012, largely attributable to lower market rates of interest for 2013.

Interest Expense. Total interest expense decreased \$1.3 million, or 22.7%, to \$4.3 million for the year ended December 31, 2013 from \$5.6 million for the year ended December 31, 2012. The decrease was primarily due to the decrease in deposit interest rates to manage interest rate risk, as well as decreased market rates of interest. Average interest-bearing liabilities totaled \$416.3 million for the year ended December 31, 2013, representing a decrease of \$25.3 million, or 5.7%, from \$441.7 million for the same period in 2012, primarily due to the decrease in average interest-bearing deposits of \$5.9 million, or 1.5%, and a decrease in average in

interest-bearing borrowings of \$19.5 million, or 34.8%. The rate paid on interest-bearing liabilities decreased 23 basis points to 1.04% for the year ended December 31, 2013 from 1.27% in 2012, reflecting the lower interest rate environment.

**Provision for Loan Losses.** For the year ended December 31, 2013, the provision for loan losses decreased \$17,000, or 3.8%, to \$425,000 from \$442,000 for the same period in 2012. Charge-offs for years ended December 31, 2013 and 2012 were \$493,000 and \$678,000, respectively, partially offset by recoveries of \$300,000 and \$24,000 for the year ended December 31, 2013 and December 31, 2012, respectively.

The allowance for loan losses of \$4.6 million at December 31, 2013 represented 0.94% of total loans, as compared to an allowance for loan losses of \$4.4 million, representing 0.93% of total loans at December 31, 2012. An analysis of the changes in the allowance for loan losses is presented under “Risk Management – Analysis and Determination of the Allowance for Loan Losses” and in Note 4 of the financial statements.

**Non-interest Income.** Non-interest income increased \$77,000, or 2.5%, to \$3.1 million for the year ended December 31, 2013. Income from customer service charges, fees and commissions decreased \$18,000, or 0.8%, income from bank owned life insurance decreased \$14,000, or 3.7%, and income from net loan sales and servicing decreased \$45,000, or 6.7%. These decreases were partially offset by the decrease on the loss on sale of OREO of \$91,000, or 36.5%.

**Non-interest Expenses.** Non-interest expense decreased \$150,000, or 0.8%, from \$18.3 million for the year ended December 31, 2012 to \$18.2 million for the year ended December 31, 2013. The decrease was primarily due to a decrease in salaries and employee benefits of \$264,000, or 2.5%. The decrease in salaries and employee benefits was directly attributed to the decrease in the expense related to the 2007 Equity Incentive Plan. The restricted stock awards and stock options granted in 2007 were fully expensed on July 27, 2012. FDIC insurance expense decreased \$126,000, or 35.3%, stationery, supplies and postage decreased \$46,000, or 13.6%, advertising expense decreased \$21,000, or 3.5%, furniture and equipment expense decreased \$29,000, or 4.0%, and other non-interest expense decreased \$115,000, or 4.3%. These decreases were partially offset by an increase in occupancy expense of \$63,000, or 5.0%, an increase in data processing of \$125,000, or 11.2%, and an increase in professional fees of \$102,000, or 18.5%.

**Income Taxes.** Income tax expense increased \$106,000, or 18.2% from \$581,000 for the year ended December 31, 2012 to \$687,000 for the year ended December 31, 2013 mainly due to the increase in income before income taxes of \$194,000, or 6.4%, which resulted in an increase in current tax expense of \$465,000, and a decrease of \$13,000 in the valuation reserve. As of December 31, 2013, a valuation allowance of \$54,000 was established against deferred tax assets related to the uncertain utilization of the charitable contribution carry forward created primarily by the donation to the Foundation as part of the conversion, as well as to a capital loss carry forward. The decrease in the valuation reserve is due to an increase in expected future capital gains. The judgment applied by management considers the likelihood that sufficient taxable income will be realized within the carry forward period in light of our tax planning strategies and changes in market conditions. See Note 10 for additional income tax disclosures.



Explanation of Use of Non-GAAP Financial Measurements. We believe that it is common practice in the banking industry to present interest income and related yield information on tax-exempt securities on a tax-equivalent basis and that such information is useful to investors because it facilitates comparisons among financial institutions. However, the adjustment of interest income and yields on tax-exempt securities to a tax-equivalent amount may be considered to include non-GAAP financial information. A reconciliation to GAAP is provided below.

|  | For the Years Ended December 31, |               |           |               |           |               |  |  |
|--|----------------------------------|---------------|-----------|---------------|-----------|---------------|--|--|
|  | 2014                             |               | 2013      |               | 2012      |               |  |  |
|  | (Dollars in Thousands)           |               |           |               |           |               |  |  |
|  | Interest                         | Average Yield | Interest  | Average Yield | Interest  | Average Yield |  |  |
| Investment securities (non-tax adjustment)   | \$ 1,589                         | 3.78 %        | \$ 1,690  | 2.62 %        | \$ 1,684  | 2.47 %        |  |  |
| Tax equivalent adjustment (1)                | 1,018                            |               | 1,064     |               | 1,037     |               |  |  |
| Investment securities (tax equivalent basis) | \$ 2,607                         | 6.21 %        | \$ 2,754  | 4.28 %        | \$ 2,721  | 3.99 %        |  |  |
| Net interest income (non-tax adjustment)     | \$ 19,671                        |               | \$ 18,720 |               | \$ 18,770 |               |  |  |
| Tax equivalent adjustment (1)                | 1,018                            |               | 1,064     |               | 1,037     |               |  |  |
| Net interest income (tax equivalent basis)   | \$ 20,689                        |               | \$ 19,784 |               | \$ 19,807 |               |  |  |
| Interest rate spread (no tax adjustment)     |                                  | 3.25 %        |           | 3.16 %        |           | 3.10 %        |  |  |
| Net interest margin (no tax adjustment)      |                                  | 3.47 %        |           | 3.41 %        |           | 3.36 %        |  |  |

(1) The tax equivalent adjustment is based on a tax rate of 41% for all periods presented.

## Risk Management

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

Credit Risk Management. Our strategy for credit risk management focuses on having well-defined credit policies and uniform underwriting criteria and providing prompt attention to potential problem loans.

Management performs a monthly review of all delinquent loans. The actions taken with respect to delinquency vary depending upon the nature of the delinquent loans and the period of delinquency. A late charge is normally assessed on loans where the scheduled payment remains unpaid after a 15 day grace period. After mailing delinquency notices, the Company's collection department calls the borrower to determine the reason for the delinquency and the repayment status. Through continued heightened account monitoring, collection, and workout efforts, the Company attempts to work out a payment schedule with the borrower in order to avoid foreclosure. If these actions do not result in a satisfactory resolution, the Company refers the loan to legal counsel and counsel initiates foreclosure proceedings. The Company is committed to assist the homeowners to remain in their homes.

Management reports to the executive committee monthly regarding the amount of loans delinquent. All loans that are delinquent greater than 90 days, loans that are in foreclosure, and all foreclosed and repossessed property that we own

are reported in greater detail to the executive committee monthly.

Analysis of Nonperforming and Classified Assets. We consider repossessed assets, loans that are 90 days or more past due, and other loans which have been identified by the Company as presenting uncertainty with respect to the collectability of interest or principal to be nonperforming assets. Loans are placed on nonaccrual status when they become 90 days delinquent, at which time the accrual of interest ceases and the allowance for any uncollectible accrued interest is established and charged against operations. Typically, payments received on a nonaccrual loan are applied to the outstanding principal and interest as determined at the time of collection of the loan.

For the year ended December 31, 2014, net charge offs were primarily due to three commercial relationships. The Company recorded a \$1.5 million charge off on a \$4.7 million commercial developer condo loan, a charge off of \$568,000 on a \$3.4 million commercial relationship in the process of foreclosure and an additional charge off of \$2.4 million on a \$4.5 million commercial relationship suspected of fraud. Management has completed its investigation into the potential fraudulent activities on the part of a commercial borrower. As a result, during the year ended December 31, 2014, the Company increased its provision for loan losses by approximately \$2.4 million and reduced the value of the borrower's loans by \$2.4 million. During the year ended December 31, 2014, management liquidated the collateral securing these loans and applied the proceeds to the remaining net loan balance and transferred one of the commercial properties to OREO. To the extent this litigation is settled or resolved the Company cannot predict whether or to what extent a recovery may occur.

Real estate that we acquire as a result of foreclosure or by deed-in-lieu of foreclosure is classified as OREO until it is sold. When property is acquired and placed in OREO, it is recorded at the fair value, less estimated selling expenses. Holding costs and declines in fair value after acquisition of the property result in charges against income. As of December 31, 2014 and 2013, the Company had \$1.1 million and \$407,000 classified as OREO, respectively.

The following table provides information with respect to our nonperforming assets at the dates indicated. We did not have any accruing loans past due 90 days or more at the dates presented.

|  | At December 31,        |         |         |         |         |   |
|--|------------------------|---------|---------|---------|---------|---|
|  | 2014                   | 2013    | 2012    | 2011    | 2010    |   |
|  | (Dollars in Thousands) |         |         |         |         |   |
| Nonaccrual loans   |                        |         |         |         |         |   |
| Residential real estate  | \$4,308                | \$2,415 | \$2,587 | \$2,222 | \$3,329 |   |
| Residential construction                                       | —                      | —       | 331     | —       | 316     |   |
| Commercial real estate   | 3,000                  | 3,362   | 902     | 798     | 2,158   |   |
| Commercial construction  | 2,396                  | —       | —       | —       | —       |   |
| Commercial   | 1,196                  | 806     | 47      | 1,306   | 391     |   |
| Home equity  | 261                    | 243     | 96      | 306     | 204     |   |
| Consumer   | 32                     | 8       | 24      | 79      | 72      |   |
| Total nonaccrual loans   | 11,193                 | 6,834   | 3,987   | 4,711   | 6,470   |   |
| Other real estate owned  | 1,050                  | 407     | 572     | 913     | 286     |   |
| Total nonperforming assets                                     | \$12,243               | \$7,241 | \$4,559 | \$5,624 | \$6,756 |   |
| Total nonperforming loans as a percentage of total loans (1)   | 2.14                   | % 1.40  | % 0.85  | % 1.05  | % 1.49  | % |
| Total nonperforming assets as a percentage of total assets (2) | 1.92                   | % 1.23  | % 0.76  | % 0.91  | % 1.18  | % |

(1) Total loans equals net loans plus the allowance for loan losses.

Nonperforming assets consist of nonperforming loans and other real estate owned. Nonperforming loans consist of all loans 90 days or more past due and other loans which have been identified by the Company as presenting (2) uncertainty with respect to the collectability of interest or principal. The Company had two troubled debt restructured loans included in nonperforming loans of \$2.1 million at December 31, 2014. These TDRs were modified during the year ended December 31, 2014.

As of December 31, 2014, the following loan classes were not accruing interest: there were 36 residential real estate loans, with total principal balances of \$4.3 million and total collateral values of \$5.3 million, 10 commercial real

estate loans, with total principal balances of \$3.0 million and total collateral values of \$3.1 million; there were 29 commercial and industrial loans, with total principal balances of \$1.2 million and total collateral values of \$1.4 million; there were three commercial construction loans with total principal balances of \$2.4 million and total collateral values of \$4.0 million; there were three consumer loans, with principal balances of \$32,000 and there were eight home equity loans, with principal balances of \$261,000 and total collateral values of \$402,000. We do not separately identify consumer loans for impairment. Any shortfalls of collateral were charged against the allowance for loan losses. At December 31, 2014, the Company's total nonperforming loans as a percentage of total loans of 2.14% was above the peer average of 1.24%. This statistical data was obtained from the December 31, 2014 UBPR Peer Group Average Report and included average data for 865 insured savings banks.

As of December 31, 2013, the following loan classes were not accruing interest: there were 17 residential real estate loans, with total principal balances of \$2.4 million and total collateral values of \$2.6 million, seven commercial real estate loans, with

total principal balances of \$3.4 million and total collateral values of \$2.4 million; there were 24 commercial and industrial loans, with total principal balances of \$806,000 and total collateral values of \$1.3 million; there were seven consumer loans, with principal balances of \$8,000 and there were four home equity loans, with principal balances of \$243,000 and total collateral values of \$432,000. We do not separately identify consumer loans for impairment. Any shortfalls of collateral were charged against the allowance for loan losses. At December 31, 2013, the Company's total nonperforming loans as a percentage of total loans of 1.40% was below the peer average of 1.59%. This statistical data was obtained from the December 31, 2013 UBPR Peer Group Average Report and included average data for 933 insured savings banks.

As of December 31, 2012, the following loan classes were not accruing interest: there were 20 residential real estate loans, with total principal balances of \$2.6 million and total collateral values of \$3.0 million, one residential construction loan, with a total principal balance \$331,000 and total collateral value of \$316,000, five commercial real estate loans, with total principal balances of \$902,000 and total collateral values of \$1.3 million; there were five commercial and industrial loans, with total principal balances of \$47,000 and total collateral values of \$47,000, and there were two home equity loans, with principal balances of \$96,000 and total collateral values of \$289,000. We do not separately identify consumer loans for impairment. Any shortfalls of collateral were charged against the allowance for loan losses. At December 31, 2012, the Company's total nonperforming loans as a percentage of total loans of 0.85% was below the peer average of 2.00%. This statistical data was obtained from the December 31, 2012 UBPR Peer Group Average Report and included average data for 982 insured savings banks.

Interest income that would have been recorded for the years ended December 31, 2014, 2013 and 2012 had nonperforming loans and troubled debt restructurings been current according to their original terms amounted to \$1.4 million, \$527,000 and \$92,000, respectively. Interest income recognized on impaired loans and troubled debt restructurings for the years ended December 31, 2014, 2013 and 2012 was \$381,000, \$542,000 and 423,000, respectively.

Regulators have adopted various regulations and practices regarding problem assets of financial institutions. Under such regulations, federal and state examiners have authority to identify problem assets during examinations and, if appropriate, require them to be classified. We perform an internal analysis of our loan portfolio and assets to classify such loans and assets similar to the manner in which such loans and assets are classified by the federal banking regulators. In addition, we regularly analyze the probable losses inherent in our loan portfolio and our nonperforming loans to determine the appropriate level of the allowance for loan losses. There are four classifications for problem assets: special mention, substandard, doubtful, and loss. Assets that do not currently expose the insured institution to sufficient risk to warrant classification in one of the aforementioned categories but possess weaknesses are designated "special mention". "Substandard" assets have one or more defined weaknesses and are characterized by the distinct possibility that the insured institution will sustain some loss if the deficiencies are not corrected. Non-accruing loans are normally classified as substandard. "Doubtful" assets have the weaknesses of substandard assets with the additional characteristic that the weaknesses make collection or liquidation in full on the basis of currently existing facts, conditions and values questionable, and there is a high possibility of loss. An asset classified as "loss" is normally fully charged-off.

The following table shows the aggregate amounts of our classified loans at the dates indicated.

|                        | December 31,           |          |          |
|------------------------|------------------------|----------|----------|
|                        | 2014                   | 2013     | 2012     |
| Classified loans       | (Dollars in Thousands) |          |          |
| Special mention loans  | \$20,868               | \$14,228 | \$23,699 |
| Substandard loans      | 14,513                 | 19,082   | 11,801   |
| Doubtful loans         | —                      | —        | 47       |
| Total classified loans | \$35,381               | \$33,310 | \$35,547 |



At December 31, 2014, special mention loans consisted of \$5.0 million in commercial and industrial loans, \$5.8 million in commercial construction loans, and \$10.0 million in commercial real estate loans. Substandard loans consisted of \$2.9 million in commercial and industrial loans, \$2.4 million in commercial constructions loans, \$4.7 million in commercial real estate loans and \$4.1 million in residential real estate loans and \$381,000 in consumer and home equity loans . The increase in classified loans of \$2.1 million was due to an increase of \$6.6 million in special mention loans, partially offset by the \$4.6 million decrease in substandard loans. At December 31, 2014, 80.5 % of our classified loans were current with payments. Other than disclosed in the above tables, there are no other loans at December 31, 2014 that management had serious doubts about the ability of the borrowers to comply with the present loan repayment terms.

At December 31, 2013, special mention loans consisted of \$4.1 million in commercial and industrial loans, \$6.6 million in commercial construction loans, and \$3.6 million in commercial real estate loans, Substandard loans consisted of \$5.0 million in commercial and industrial loans, \$3.9 million in commercial constructions loans, \$7.5 million in commercial real estate loans

and \$2.4 million in residential real estate loans and \$301,000 in consumer and home equity loans. The decrease in classified loans was due to an decrease in additions of special mention loan partially offset by the increase in additions to substandard loans. At December 31, 2013, 78.2% of our classified loans were current with payments. Other than disclosed in the above tables, there are no other loans at December 31, 2013 that management had serious doubts about the ability of the borrowers to comply with the present loan repayment terms.

**Analysis and Determination of the Allowance for Loan Losses.** The allowance for loan losses is a valuation allowance for probable credit losses inherent in the loan portfolio. We evaluate the need to establish allowances against losses on loans on a monthly basis. When additional allowances are necessary, a provision for loan losses is charged to earnings. The allowance for loan losses is maintained at an amount that management considers appropriate to cover inherent probable losses in the loan portfolio.

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

**Specific Allowance Required for Identified Problem Loans.** We establish an allowance on certain identified problem loans based on such factors as: (1) the strength of the customer's personal or business cash flows; (2) the availability of other sources of repayment; (3) the amount due or past due; (4) the type and value of collateral; (5) the strength of our collateral position; (6) the estimated cost to sell the collateral; and (7) the borrower's effort to cure the delinquency.

**General Valuation Allowance on the Remainder of the Loan Portfolio.** We establish a general allowance for loans that are not delinquent to recognize the probable losses associated with lending activities. This general valuation allowance is determined by segregating the loans by loan category and assigning percentages to each category. The percentages are adjusted for significant factors that, in management's judgment, affect the collectability of the portfolio as of the evaluation date. These significant factors include: levels and historical trends in delinquencies, impaired loans, nonaccrual loans, charge-offs, recoveries, and classified assets; trends in the volume and terms of loans; effects of any change in underwriting, policies, procedures, and practices; experience, ability, and depth of management and staff; national and local economic trends and conditions; trends and conditions in the industries in which borrowers operate; effects of changes in credit concentrations. The applied loss factors are reevaluated quarterly to ensure their relevance in the current economic environment.

We identify loans that may need to be charged off as a loss by reviewing all delinquent loans, classified loans and other loans that management may have concerns about collectability. For individually reviewed loans, the borrower's inability to make payments under the terms of the loan or a shortfall in collateral value would result in our allocating a portion of the allowance to the loan that was impaired.

At December 31, 2014, our allowance for loan losses represented 0.94% of total loans and 44.02% of nonperforming loans. The allowance for loan losses increased \$331,000, or 7.2%, from \$4.6 million at December 31, 2013 to \$4.9 million at December 31, 2014, due to a provision for loan losses of \$5.3 million, partially offset by net charge-offs of \$4.9 million, or 0.98%, of total average loans. The provision for loan losses increased \$4.8 million from \$425,000 for the year ended December 31, 2013 to \$5.3 million for the year ended December 31, 2014. Net charge-offs increased \$4.7 million from \$193,000, or 0.04% of total average loans, for the same period in December 31, 2013. The increases in the provision for loan losses and net charge-offs were primarily related to three loan relationships (see "Analysis of Nonperforming and Classified Assets"). Nonperforming loans increased \$4.4 million, or 63.7%, from \$6.8 million, or 1.40% of total loans, at December 31, 2013 to \$11.2 million, or 2.14% of total loans, at December 31, 2014.

The provision for loan losses in the year ended December 31, 2014 reflects management's assessment of several factors. In particular, nonaccrual loans increased \$4.4 million to \$11.2 million at December 31, 2014 from \$6.8 million at December 31, 2013.

At December 31, 2013, our allowance for loan losses represented 0.94% of total loans and 67.5% of nonperforming loans. The allowance for loan losses increased \$232,000, or 5.3% from \$4.4 million at December 31, 2012 to \$4.6 million at December 31, 2013, due to a provision for loan losses of \$425,000, partially offset by net charge-offs of \$193,000, or 0.4% of total average loans. Net charge-offs decreased \$461,000, or 70.5%, from \$654,000, or 0.14% of total average loans, from the same period in 2012. In the fourth quarter of 2013, a recovery of \$235,000 on a previous charge-off was recognized.

At December 31, 2012, our allowance for loan losses represented 0.93% of total loans and 109.46% of nonperforming loans. The allowance for loan losses decreased slightly from \$4.6 million at December 31, 2011 to \$4.4 million at December 31, 2012, due to a provision for loan losses of \$442,000, partially offset by net charge-offs of \$654,000. The provision for loan losses in the year ended December 31, 2012 reflects management's assessment of several factors. In particular, nonaccrual loans decreased \$700,000 from \$4.7 million at December 31, 2011 to \$4.0 million at December 31, 2012. Also, net charge-offs decreased \$43,000 from Dec

ember 31, 2011. In addition, management assessed the continued growth of the loan portfolio, particularly the increases in commercial real estate loans, construction loans and commercial business loans, as well as the weakening of the local and national economy.

The following table sets forth the Company's percent of allowance for loan losses by category to total allowances and the percent of loans to total loans in each of the categories listed at the dates indicated. Real estate includes residential, commercial and home equity loans.

|                            | For Years Ended December 31,<br>2014 |  |  | 2013    |  |  | 2012    |  |  |  |  |  |
|----------------------------|--------------------------------------|--|--|---------|--|--|---------|--|--|--|--|--|
|                            | Amount                               | % of Allowance in each Category to Total Allowance | Percent of Loans in each Category to Total Loans | Amount  | % of Allowance in each Category to Total Allowance | Percent of Loans in each Category to Total Loans | Amount  | % of Allowance in each Category to Total Allowance | Percent of Loans in each Category to Total Loans |  |  |  |
| Allowance for loan losses: | (Dollars in Thousands)               |  |  |         |  |  |         |  |  |  |  |  |
| Real estate                | \$3,338                              | 67.8 %   | 77.0 %   | \$2,922 | 63.6 %   | 72.7 %   | \$2,626 | 60.2 %   | 72.9 %   |  |  |  |
| Construction               | 675                                  | 13.7 %   | 8.4 %  | 529     | 11.5 %   | 9.2 %  | 595     | 13.6 %   | 8.5 %  |  |  |  |
| Commercial and industrial  | 879                                  | 17.8 %   | 14.1 %   | 1,110   | 24.2 %   | 17.7 %   | 1,099   | 25.2 %   | 18.0 %   |  |  |  |
| Consumer                   | 35                                   | 0.7 %  | 0.5 %  | 35      | 0.7 %  | 0.4 %  | 44      | 1.0 %  | 0.6 %  |  |  |  |
| Unallocated                | —                                    | —  | —  | —       | —  | —  | —       | —  | —  |  |  |  |
| Total:                     | \$4,927                              | 100.0 %  | 100.0 %  | \$4,596 | 100.0 %  | 100.0 %  | \$4,364 | 100.0 %  | 100.0 %  |  |  |  |

|                            | For Years Ended December 31,<br>2011 |  |  | 2010    |  |  |
|----------------------------|--------------------------------------|--|--|---------|--|--|
|                            | Amount                               | % of Allowance in each Category to Total Allowance | Percent of Loans in each Category to Total Loans | Amount  | % of Allowance in each Category to Total Allowance | Percent of Loans in each Category to Total Loans |
| Allowance for loan losses: | (Dollars in Thousands)               |  |  |         |  |  |
| Real estate                | \$2,571                              | 56.2 %   | 73.3 %   | \$2,424 | 54.7 %   | 74.9 %   |
| Construction               | 615                                  | 13.4 %   | 8.3 %  | 550     | 12.4 %   | 7.6 %  |
| Commercial and industrial  | 1,343                                | 29.4 %   | 17.8 %   | 1,429   | 32.3 %   | 16.8 %   |
| Consumer                   | 47                                   | 1.0 %  | 0.6 %  | 28      | 0.6 %  | 0.7 %  |
| Unallocated                | —                                    | —  | —  | —       | —  | —  |
| Total:                     | \$4,576                              | 100.0 %  | 100.0 %  | \$4,431 | 100.0 %  | 100.0 %  |

Although we believe that we use the best information available to establish the allowance for loan losses, future adjustments to the allowance for loan losses may be necessary and our results of operations could be adversely affected if circumstances differ substantially from the assumptions used in making the determinations. Furthermore, while we believe we have established our allowance for loan losses in conformity with U.S. generally accepted accounting principles, there can be no assurance that our banking regulators, in reviewing our loan portfolio, will not request us to increase our allowance for loan losses. Our banking regulators may require us to increase our allowance for loan losses based on judgments different from ours. In addition, because future events affecting borrowers and

collateral cannot be predicted with certainty, there can be no assurance that increases will not be necessary should the quality of any loans deteriorate as a result of the factors discussed above. Any material increase in the allowance for loan losses may adversely affect our financial condition and results of operations.

Analysis of Loan Loss Experience. The following table sets forth an analysis of the allowance for loan losses for the periods indicated.

|  | At or for the Years Ended December 31, |         |          |         |         |   |
|--|--|---------|----------|---------|---------|---|
|  | 2014                                   | 2013    | 2012     | 2011    | 2010    |   |
|  | (Dollars in Thousands)                 |         |          |         |         |   |
| Allowance for loan losses, beginning of period       | \$4,596                                | \$4,364 | \$4,576  | \$4,431 | \$4,077 |   |
| Charged-off loans:                                   |  |         |          |         |         |   |
| Residential real estate                              | (303)                                  | (183)   | (98)     | (87)    | (118)   | ) |
| Residential construction                             | —                                      | (62)    | —        | (76)    | (107)   | ) |
| Commercial real estate                               | (975)                                  | (68)    | (65)     | (164)   | (332)   | ) |
| Commercial construction                              | (1,539)                                | —       | —        | —       | —       | ) |
| Commercial and industrial                            | (2,181)                                | (117)   | (406)    | (317)   | (266)   | ) |
| Home equity  | (66)                                   | (10)    | (35)     | (6)     | —       | ) |
| Consumer   | (57)                                   | (53)    | (74)     | (65)    | (109)   | ) |
| Total charged-off loans                              | (5,121)                                | (493)   | (678)    | (715)   | (932)   | ) |
| Recoveries on loans previously charged-off:          |  |         |          |         |         |   |
| Residential real estate                              | —                                      | 1       | 1        | —       | —       |   |
| Residential construction                             | —                                      | —       | —        | —       | —       |   |
| Commercial real estate                               | 74                                     | 247     | —        | —       | —       |   |
| Commercial construction                              | —                                      | —       | —        | —       | —       |   |
| Commercial and industrial                            | 83                                     | 38      | 4        | —       | 38      |   |
| Home equity  | 23                                     | —       | —        | —       | —       |   |
| Consumer   | 1                                      | 14      | 19       | 18      | 25      |   |
| Total recoveries                                     | 181                                    | 300     | 24       | 18      | 63      |   |
| Net loans charged-off                                | (4,940)                                | (193)   | (654)    | (697)   | (869)   | ) |
| Provision for loan losses                            | 5,271                                  | 425     | 442      | 842     | 1,223   |   |
| Allowance for loan losses, end of period             | \$4,927                                | \$4,596 | \$4,364  | \$4,576 | \$4,431 |   |
| Net charge-offs to average loans outstanding         | 0.98                                   | % 0.04  | % 0.14   | % 0.16  | % 0.20  | % |
| Allowance for loan losses to total loans (1)         | 0.94                                   | % 0.94  | % 0.93   | % 1.02  | % 1.02  | % |
| Allowance for loan losses to nonperforming loans (2) | 44.02                                  | % 67.25 | % 109.46 | % 97.13 | % 68.49 | % |
| Net charge-offs to allowance for loan losses         | 100.26                                 | % 4.20  | % 14.99  | % 15.23 | % 19.61 | % |
| Recoveries to charge-offs                            | 3.53                                   | % 60.85 | % 3.54   | % 2.52  | % 6.76  | % |

(1) Total loans equals net loans plus the allowance for loan losses.

(2) Nonperforming loans consist of all loans 90 days or more past due and other loans which have been identified by the Company as presenting uncertainty with respect to the collectability of interest or principal.

**Interest Rate Risk Management.** We manage the interest rate sensitivity of our interest-bearing liabilities and interest-earning assets in an effort to minimize the adverse effects of changes in the interest rate environment. Deposit accounts typically react more quickly to changes in market interest rates than mortgage loans because of the shorter maturities of deposits. As a result, sharp increases in interest rates may adversely affect our earnings while decreases in interest rates may beneficially affect our earnings. To reduce the potential volatility of our earnings, we have sought to improve the match between asset and liability maturities and rates, while maintaining an acceptable interest rate spread. Our strategy for managing interest rate risk emphasizes: adjusting the maturities of borrowings; adjusting the investment portfolio mix and duration; increasing our focus on shorter-term, adjustable-rate commercial and

residential investment lending; selling fixed-rate mortgage loans; and periodically selling available-for-sale securities. We currently do not participate in hedging programs, interest rate swaps or other activities involving the use of derivative financial instruments.

We have an Asset/Liability Committee, which includes members of management and one member of the Board of Directors, to communicate, coordinate and control all aspects involving asset/liability management. The committee reports to the Board of Directors of the Bank quarterly and establishes and monitors the volume, maturities, pricing and mix of assets and funding

sources with the objective of managing assets and funding sources to provide results that are consistent with liquidity, growth, risk limits and profitability goals.

Net Interest Income Simulation Analysis. We use a simulation model to monitor interest rate risk. This model reports the net interest income at risk under seven primary different interest rate environments. Specifically, net interest income is measured in one scenario that assumes no change in interest rates, and six scenarios where interest rates increase 100 and 200 basis points instantaneous increase in interest rates, 300 basis point increase over a 12-month horizon, and a 400 and 500 basis point increase over a 24-month time horizon and a decrease of 100 basis points, from current rates over the one year time period following the current consolidated financial statements.

The changes in interest income and interest expense due to changes in interest rates reflect the rate sensitivity of our interest earning assets and interest bearing liabilities. For example, in a rising interest rate environment, the interest income from an adjustable rate loan is likely to increase depending on its repricing characteristics while the interest income from a fixed rate loan would not increase until the funds were repaid and loaned out at a higher interest rate.

The following table reflects changes in estimated net interest income for the Company at December 31, 2014 through December 31, 2015.

| Changes In Interest Rates<br>(Basis Points) | Net Interest<br>Income | Dollar Change in<br>Estimated Net Interest<br>Income Over Twelve<br>Months | Percentage Change in<br>Estimated Net Interest<br>Income Over Twelve<br>Months |    |
|---|------------------------|--|--|----|
| Flat Up 500 - 24 Months                     | \$19,156               | \$(114   | ) (0.6   | )% |
| Up 400 - 24 Months                          | 19,249                 | (21  | ) (0.1   | )% |
| Up 300 - instantaneous                      | 19,451                 | 181  | 0.9  | %  |
| Up 200 - 12 months                          | 19,249                 | (21  | ) (0.1   | )% |
| Up 100 - instantaneous                      | 19,416                 | 146  | 0.8  | %  |
| Base  | 19,270                 | —  | —  | %  |
| Down 100 - 12 Months                        | 19,064                 | (206   | ) (1.1   | )% |

As indicated in the table above, a 100 basis point decrease in interest rates is estimated to decrease net interest income by 1.1%. A 100 and 300 basis point instantaneous increase in interest rates is projected to increase net interest income by 0.8% and 0.9%, respectively. A 200 basis point gradual increase in interest rates over a 12 month period is projected to decrease net interest income by 0.1%. A 400 and flat 500 basis point increase in interest rates over a 24-month period is estimated to decrease net interest income by 0.1% and 0.6%, respectively, in the first 12 months.

The repricing and/or new rates of assets and liabilities moved in tandem with market rates. However, in certain deposit products, the use of data from a historical analysis indicated that the rates on these products would move only a fraction of the rate change amount. Pertinent data from each loan account, deposit account and investment security was used to calculate future cash flows. The data included such items as maturity date, payment amount, next repricing date, repricing frequency, repricing index and spread. Prepayment speed assumptions were based upon the difference between the account rate and the current market rate.

The income simulation analysis was based upon a variety of assumptions. These assumptions include but are not limited to asset mix, prepayment speeds, the timing and level of interest rates, and the shape of the yield curve. As market conditions vary from the assumptions in the income simulation analysis, actual results will differ. As a result, the income simulation analysis does not serve as a forecast of net interest income, nor do the calculations represent any actions that management may undertake in response to changes in interest rates. In all simulations, the lowest possible interest rate would be zero.



There are inherent shortcomings in any income simulation, given the number and variety of assumptions that must be made in performing the analysis. The assumptions relied upon in making these calculations of interest rate sensitivity include the level of market interest rates, the shape of the yield curve, the degree to which certain assets and liabilities with similar maturities or periods to repricing react to changes in market interest rates, the degree to which non-maturity deposits react to changes in market rates, the expected prepayment rates on loans and the degree to which early withdrawals occur on certificates of deposit and the volume of other deposit flows.

Although the analysis shown above provides an indication of the Company's sensitivity to interest rate changes at a point in time, these estimates are not intended to and do not provide a precise forecast of the effect of changes in market interest rates on the Company's net interest income and will differ from actual results.

Liquidity Management. Liquidity is the ability to meet current and future financial obligations of a short-term nature. Our primary sources of funds consist of deposit inflows, loan repayments, maturities and sales of securities, borrowings from the FHLB and securities sold under agreements to repurchase. While maturities and scheduled amortization of loans and securities are predictable sources of funds, deposit flows and loan prepayments are greatly influenced by general interest rates, economic conditions and competition. Prepayment rates can have a significant impact on interest income. Because of the large percentage of loans we hold, rising or falling interest rates have a significant impact on the prepayment speeds of our earning assets that in turn affect the rate sensitivity position. When interest rates rise, prepayments tend to slow. When interest rates fall, prepayments tend to rise. Our asset sensitivity would be reduced if prepayments slow and vice versa. While we believe these assumptions to be reasonable, there can be no assurance that assumed prepayment rates will approximate actual loan repayment activity. Our short-term investments primarily consist of U.S. Treasury and government agencies, which we use primarily for collateral for sweep accounts maintained by commercial customers. The balances of these investments fluctuate as the aggregate balance of our sweep accounts fluctuate.

We regularly adjust our investments in liquid assets based upon our assessment of: (1) expected loan demands; (2) expected deposit flows; (3) yields available on interest-earning deposits and securities; and (4) the objectives of our asset/liability management policy.

The Company's most liquid assets are cash and cash equivalents. The levels of these assets depend on our operating, financing, lending and investing activities during any given period. At December 31, 2014, total Bank cash and cash equivalents totaled \$42.9 million, net of reserve requirements. Securities classified as available-for-sale whose market value exceeds our cost, which provide additional sources of liquidity, totaled \$414,000 at December 31, 2014.

On December 31, 2014, we had \$67.0 million of borrowings outstanding with the FHLB and we had the ability to borrow an additional \$65.4 million based on the collateral pledged to the FHLB. The Company is able to pledge additional collateral to increase the availability of FHLB borrowings to 50% of its asset base. The Company's unused borrowing capacity with the Federal Reserve Bank was approximately \$44.5 million at December 31, 2014. In addition, at December 31, 2014 we had the following contingency funding sources available: a \$2.0 million available line of credit with the FHLB, and an unsecured line of credit of \$4.0 million with Bankers Bank, N.E. In addition, we had \$95.6 million, or 15.0% of total assets available from the brokered deposit market. During the year ended December 31, 2014, we did not utilize any of these three contingency funding sources. Future growth of our loan portfolio resulting from our expansion efforts may require us to borrow additional funds.

At December 31, 2014, we had \$35.4 million in loan commitments outstanding, which consisted of: \$28.4 million in commercial loan commitments, \$6.3 million of mortgage loan commitments, and \$647,000 in home equity and consumer commitments; \$17.2 million in unadvanced construction loan commitments; \$79.1 million in unused lines of credit; and \$904,000 in standby letters of credit. Certificates of deposit due within one year of December 31, 2014 totaled \$104.0 million, or 60.6% of certificates of deposit. If these maturing deposits do not remain with us, we will be required to seek other sources of funds, including other certificates of deposit and borrowings. Depending on market conditions, we may be required to pay higher rates on such deposits or other borrowings than we currently pay on the certificates of deposit due on or before December 31, 2015. We believe, however, based on past experience that a significant portion of our certificates of deposit will remain with us. We have the ability to attract and retain deposits by adjusting the interest rates offered.

The following table sets forth information relating to the Company's payments due under contractual obligations at December 31, 2014:

|       | Payments due by period |                       |                        |                         |  |
|-------|------------------------|-----------------------|------------------------|-------------------------|--|
| Total | Less Than<br>One Year  | One to<br>Three Years | Three to<br>Five Years | More Than<br>Five Years |  |

|   | (In Thousands) |          |          |          |         |
|---|----------------|----------|----------|----------|---------|
| Long-term debt  | \$67,039       | \$16,891 | \$29,302 | \$19,882 | \$964   |
| Operating lease obligations   | 5,014          | 476      | 931      | 861      | 2,746   |
| Other long-term liabilities reflected on the Company's balance sheet under GAAP | —              | —        | —        | —        | —       |
| Total   | \$72,053       | \$17,367 | \$30,233 | \$20,743 | \$3,710 |

Our primary investing activities are the origination and purchase of loans and the purchase of securities. Our primary financing activities consist of activity in deposit accounts and FHLB advances. Deposit flows are affected by the overall level of interest rates, the interest rates and products offered by us and our local competitors and other factors. We generally manage the

pricing of our deposits to be competitive and to increase core deposit relationships. Occasionally, we offer promotional rates on certain deposit products to attract deposits.

**Capital Management.** We are subject to various regulatory capital requirements administered by the FDIC, including a risk-based capital measure. The risk-based capital guidelines include both a definition of capital and a framework for calculating risk-weighted assets by assigning balance sheet assets and off-balance sheet items to broad risk categories. At December 31, 2014, we exceeded all of our regulatory capital requirements. We are considered “well capitalized” under regulatory guidelines.

Total stockholders' equity decreased \$4.1 million, or 4.4%, from \$92.2 million, or 15.7% of total assets, at December 31, 2013 to \$88.1 million, or 13.8% of total assets, at December 31, 2014. The Company's decrease in stockholders' equity of 4.4% was primarily as a result of the \$578,000 net loss for the year ended December 31, 2014 and the \$1.4 million cash dividend paid during the year ended December 31, 2014, partially offset by an increase of \$303,000, or 8.5%, in stock-based compensation, and an increase of \$296,000, or 9.0%, in additional paid-in-capital. In 2014, the Company repurchased 174,915 shares of the Company's common stock at a cost of \$2.9 million and an average per share price of \$16.36 and released 9,700 shares to fund employee stock option exercises at an average price per share of \$17.51.

The Company's book value per share decreased \$0.25, or 1.5%, to \$16.72 at December 31, 2014 compared to \$16.97 at December 31, 2013. During 2014 and 2013, the Company repurchased approximately \$2.9 million, or 174,915 shares, and \$242,000, or 13,700 shares, of the Company's stock, respectively.

**Off-Balance Sheet Arrangements.** In the normal course of operations, we engage in a variety of financial transactions that, in accordance with U.S. generally accepted accounting principles, are not recorded in our financial statements. These transactions involve, to varying degrees, elements of credit, interest rate and liquidity risk. Such transactions are used primarily to manage customers' requests for funding and take the form of loan commitments, letters of credit and lines of credit. For information about our loan commitments and unused lines of credit, see note 11 of the notes to the consolidated financial statements. We currently have no plans to engage in hedging activities in the future.

For the years ended December 31, 2014 and 2013, we engaged in no off-balance sheet transactions reasonably likely to have a material effect on our financial condition, results of operations or cash flows.

#### Impact of Inflation and Changing Prices.

The financial statements and related financial data presented in this Form 10-K have been prepared in accordance with U.S. generally accepted accounting principles, which require the measurement of financial position and operating results in terms of historical dollars without considering the change in the relative purchasing power of money over time due to inflation. The primary impact of inflation on our operations is reflected in increased operating costs. Unlike most industrial companies, virtually all the assets and liabilities of a financial institution are monetary in nature. As a result, interest rates generally have a more significant impact on a financial institution's performance than do general levels of inflation. Interest rates do not necessarily move in the same direction or to the same extent as the prices of goods and services.

#### Application of Critical Accounting Policies.

Our financial statements reflect the selection and application of accounting policies that require management to make significant estimates and judgments. The information pertaining to the Company's significant accounting policies is incorporated herein by reference to Note 1 “Summary of Significant Accounting Policies” in the Notes to the Consolidated Financial Statements and in the discussion under “Critical Accounting Policies” contained in Item 7 of this

Form 10-K.

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

The information required by this item is incorporated herein by reference to the Section captioned “Management’s Discussion and Analysis of Financial Condition and Results of Operations” in this Annual Report on Form 10-K.

Item 8. Financial Statements and Supplementary Data.

Information required by this item is included herein beginning on page F-1.

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

None.

Item 9A. Controls and Procedures.

(a) Disclosure Controls and Procedures

The Company's management, including the Company's principal executive officer and principal financial officer, have evaluated the effectiveness of the Company'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, the Company's disclosure controls and procedures were effective for the purpose of ensuring that the information required to be disclosed in the reports that the Company files or submits under the Exchange Act with the Securities and Exchange Commission (the "SEC") (1) is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and (2) is accumulated and communicated to the Company's management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure.

(b) Internal Controls Over Financial Reporting

Management's annual report on internal control over financial reporting is incorporated herein by reference to the Company's audited Consolidated Financial Statements in this 2014 Annual Report on Form 10-K.

(c) Changes to Internal Control Over Financial Reporting

There has been no change in the Company's internal control over financial reporting identified in connection with the evaluation required by Rule 13a-15 that occurred during the Company's last fiscal quarter that has materially affected or is reasonably likely to materially affect, the Company's internal control over financial reporting.

Item 9B. Other Information

Not applicable.

PART III

Item 10. Directors, Executive Officers and Corporate Governance.

Directors

For information relating to the directors of Chicopee Bancorp, the section captioned "Proposal 1 – Election of Directors" in Chicopee Bancorp's Proxy Statement for the 2015 Annual Meeting of Stockholders is incorporated by reference.

Executive Officers

For information relating to officers of Chicopee Bancorp, the information contained under "Proposal 1 – Election of Directors" in Chicopee Bancorp's Proxy Statement for the 2015 Annual Meeting of Stockholders and under Part I, Item 1, "Business — Executive Officers of the Registrant" of this Annual Report on Form 10-K is incorporated by reference.

Compliance with Section 16(a) of the Exchange Act

For information regarding compliance with Section 16(a) of the Exchange Act, the section captioned “Section 16(a) Beneficial Ownership Compliance” in Chicopee Bancorp’s Proxy Statement for the 2015 Annual Meeting of Stockholders is incorporated by reference.

Disclosure of Code of Ethics

A copy of the Code of Ethics and Business Conduct is available to stockholders on the Governance Documents portion of the Investors Relations section on Chicopee Bancorp’s website at [www.chicopeesavings.com](http://www.chicopeesavings.com).

Corporate Governance

For information regarding the audit committee and its composition and the audit committee financial expert, the section captioned “Corporate Governance – Committees of the Board of Directors – Audit Committee” in Chicopee Bancorp’s Proxy Statement for the 2015 Annual Meeting of Stockholders is incorporated by reference.

Item 11. Executive Compensation.

Executive Compensation

For information regarding executive compensation, the sections captioned “Compensation Disclosure and Analysis,” “Executive Compensation” and “Director Compensation” in Chicopee Bancorp’s Proxy Statement for the 2015 Annual Meeting of Stockholders is incorporated by reference.

Corporate Governance

For information regarding the compensation committee report, the section captioned “Compensation Committee Report” in Chicopee Bancorp’s Proxy Statement for the 2015 Annual Meeting of Stockholders is incorporated by reference.

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

Security Ownership of Certain Beneficial Owners Information required by this item is incorporated herein by (a) reference to the section captioned “Stock Ownership” in Chicopee Bancorp’s Proxy Statement for the 2015 Annual Meeting of Stockholders.

Security Ownership of Management Information required by this item is incorporated herein by reference to the (b) section captioned “Stock Ownership” in Chicopee Bancorp’s Proxy Statement for the 2015 Annual Meeting of Stockholders.

(c) Changes in Control

Management of Chicopee Bancorp knows of no arrangements, including any pledge by any person of securities of Chicopee Bancorp, the operation of which may at a subsequent date result in a change in control of the registrant.

(d) Equity Compensation Plan Information

The following table sets forth information as of December 31, 2014 about Company common stock that may be issued under the Chicopee Bancorp, Inc. 2007 Equity Incentive Plan. The plan was approved by the Company’s stockholders.

| Plan Category  | Number of Securities to be Issued Upon the Exercise of Outstanding Options | Weighted-Average Exercise Price of Outstanding Options | Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans (Excluding Securities Reflected in the First Column) |
|--|--|--|---|
| Equity compensation plans approved by security holders | Warrants and Rights<br>653,898   | Warrants and Rights<br>\$14.57                         | 46,174  |



|  |         |         |        |
|--|---------|---------|--------|
| Equity compensation plans<br>not approved by security<br>holders | n/a     | n/a     | n/a    |
| Total  | 653,898 | \$14.57 | 46,174 |

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

Certain Relationships and Related Transactions

For information regarding certain relationships and related transactions, the section captioned “Other Information Relating to Directors and Executive Officers-Transactions with Related Parties” and “Policies and Procedures for Approval of Related Person Transactions” in Chicopee Bancorp’s Proxy Statement for the 2015 Annual Meeting of Stockholders is incorporated by reference.

Director Independence

For information regarding director independence, the section captioned “Corporate Governance – Director Independence” in Chicopee Bancorp’s Proxy Statement for the 2015 Annual Meeting of Stockholders is incorporated by reference.

Item 14. Principal Accountant Fees and Services.

For information regarding the principal accountant fees and expenses, the section captioned “Proposal 2 – Ratification of Independent Registered Public Accounting Firm” in Chicopee Bancorp’s Proxy Statement for the 2015 Annual Meeting of Stockholders is incorporated by reference.

PART IV

Item 15. Exhibits and Financial Statements Schedules.

1. Financial Statements

The following consolidated financial statements of the Company and its subsidiaries are filed as part of this document under Item 8:

- Report of Independent Registered Public Accounting Firm
- Consolidated Balance Sheets at December 31, 2014 and 2013
- Consolidated Statements of Operations for the Years Ended December 31, 2014, 2013 and 2012
- Consolidated Statements of Other Comprehensive Income for the Years Ended December 31, 2014, 2013 and 2012
- Consolidated Statements of Changes in Stockholders’ Equity for the Years Ended December 31, 2014, 2013 and 2012
- Consolidated Statements of Cash Flows for the Years Ended December 31, 2014, 2013 and 2012
- Notes to Consolidated Financial Statements

2. Financial Statement Schedules

Financial Statement Schedules have been omitted because they are not applicable or the required information is shown in the Consolidated Financial Statements or notes thereto.

3. Exhibits

| No. | Description  |
|-----|--|
| 3.1 | Certificate of Incorporation of Chicopee Bancorp, Inc. (1) |
| 3.2 | Bylaws of Chicopee Bancorp, Inc. (2)                       |
| 4.1 | Stock Certificate of Chicopee Bancorp, Inc. (1)            |

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- 10.1\* Amended and Restated Employment Agreement between William J. Wagner and Chicopee Bancorp, Inc. (3)
- 10.2\* Amended and Restated Employment Agreement between William J. Wagner and Chicopee Savings Bank (3)
- 10.3\* Form of Chicopee Savings Bank Employee Stock Ownership Plan (1)
- 10.4\* Form of Trust Agreement between Chicopee Savings Bank and the Trustee for Chicopee Savings Bank Employee Stock Ownership Plan Trust (1)
- 10.5\* Form of Loan Agreement (1)
- 10.6\* Amended and Restated Chicopee Savings Bank Employee Severance Compensation Plan (3)
- 10.7\* Amended and Restated Chicopee Savings Bank Supplemental Executive Retirement Plan (3)
- 10.8\* Form of Executive Supplemental Retirement Income Agreement between Chicopee Savings Bank and Russell J. Omer and William J. Wagner (1)
- 10.9\* Form of First Amendment to the Executive Supplemental Retirement Income Agreement between Chicopee Savings Bank and Russell J. Omer and William J. Wagner (3)
- 10.10\* First Amendment to Amended and Restated Employment Agreement between William J. Wagner and Chicopee Bancorp, Inc. (3)
- 10.11\* First Amendment to Amended and Restated Employment Agreement between William J. Wagner and Chicopee Savings Bank (3)
- 10.12\* Change in Control Agreement between Guida R. Sajdak and Chicopee Savings Bank (4)
- 10.13\* First Amendment to Change in Control Employment Agreement between Guida R. Sajdak and Chicopee Savings Bank (6)
- 10.14\* Employment Agreement between Russell J. Omer and Chicopee Bancorp, Inc. (4)
- 10.15\* Employment Agreement between Russell J. Omer and Chicopee Savings Bank (4)
- 10.16\* Chicopee Bancorp, Inc. 2007 Equity Incentive Plan (5)
- 10.17\* 2012 Phantom Stock Unit Award and Long-Term Incentive Plan (7)
- 21.0 List of Subsidiaries
- 23.0 Consent of Berry Dunn McNeil & Parker, LLC
- 31.1 Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer
- 31.2 Rule 13a-14(a)/15d-14(a) Certification of Chief Financial Officer
- 32.0 Section 1350 Certification of Chief Executive Officer and Chief Financial Officer

\* Management contract or compensatory plan, contract or agreement.

(1 ) Incorporated by reference in this document to the exhibits to the Company's Registration Statement on Form S-1 (File No. 333-132512) and any amendments thereto, initially filed with the Securities and Exchange Commission on March 17, 2006.

(2 ) Incorporated by reference in this document to the Company's Current Report on Form 8-K filed on August 1, 2007 (File No. 000-51996).

(3 ) Incorporated by reference in this document to the Company's Annual Report on Form 10-K for the year ended December 31, 2009, filed on March 13, 2009 (File No. 000-51996).

(4 ) Incorporated by reference to the Company's Current Report on Form 8-K filed with the Securities and Exchange Commission on June 22, 2010.

(5 ) Incorporated herein by reference to Appendix A to the Company's definitive proxy statement filed with the Securities and Exchange Commission on April 18, 2007 (File No. 000-51996).

(6 ) Incorporated by reference to the Company's 8-K filed with the SEC on March 1, 2013.

(7 ) Incorporated by reference to the Company's 8-K filed with the SEC on March 14, 2012.

## SIGNATURES

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

By: /s/ William J. Wagner March 12, 2015  
William J. Wagner  
Chairman of the Board, President and Chief Executive Officer

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

| Name   | Title  | Date           |
|--|--|----------------|
| /s/ William J. Wagner<br>William J. Wagner   | Chairman of the Board, President<br>and Chief Executive Officer<br>(principal executive officer)                         | March 12, 2015 |
| /s/ Guida R. Sajdak<br>Guida R. Sajdak       | Senior Vice President, Chief<br>Financial Officer and Treasurer<br>(principal financial and chief<br>accounting officer) | March 12, 2015 |
| /s/ James P. Lynch<br>James P. Lynch         | Director   | March 12, 2015 |
| /s/ William D. Masse<br>William D. Masse     | Director   | March 12, 2015 |
| /s/ William J. Giokas<br>William J. Giokas   | Director   | March 12, 2015 |
| /s/ Gregg F. Orlen<br>Gregg F. Orlen         | Director   | March 12, 2015 |
| /s/ Judith T. Tremble<br>Judith T. Tremble   | Director   | March 12, 2015 |
| /s/ Thomas J. Bardon<br>Thomas J. Bardon     | Director   | March 12, 2015 |
| /s/ James H. Bugbee<br>James H. Bugbee       | Director   | March 12, 2015 |
| /s/ Gary G. Fitzgerald<br>Gary G. Fitzgerald | Director   | March 12, 2015 |
| /s/ Paul C. Picknelly<br>Paul C. Picknelly   | Director   | March 12, 2015 |

## Management's Annual Report on Internal Control over Financial Reporting

The management of Chicopee Bancorp, Inc. and Subsidiaries (collectively the "Company") is responsible for establishing and maintaining adequate internal control over financial reporting. The Company's internal control system is a process designed to provide reasonable assurance to the management and board of directors regarding the preparation and fair presentation of published consolidated financial statements.

The Company's internal control over financial reporting includes policies and procedures that pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect transactions and dispositions of assets; provide reasonable assurances that transactions are recorded as necessary to permit preparation of consolidated financial statements in accordance with U.S. generally accepted accounting principles ("GAAP"), and that receipts and expenditures are being made only in accordance with authorizations of management and the directors of the Company; and provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company's assets that could have a material effect on our consolidated financial statements.

All internal control systems, no matter how well designed, have inherent limitations. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to consolidated financial statement preparation and presentation. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

The Company's management assessed the effectiveness of internal control over financial reporting as of December 31, 2014. In making this assessment, management used the criteria set forth in the Internal Control - Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on its assessment, management believes that, as of December 31, 2014, the Company's internal control over financial reporting is effective based on those criteria.

The Company's independent registered public accounting firm that audited the consolidated financial statements has issued an audit report on our assessment of, and the effective operation of, the Company's internal control over financial reporting as of December 31, 2014, a copy of which is included in this annual report.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Stockholders and Board of Directors  
Chicopee Bancorp, Inc.

We have audited the accompanying consolidated balance sheets of Chicopee Bancorp, Inc. and Subsidiaries as of December 31, 2014 and 2013, and the related consolidated statements of operations, comprehensive income (loss), changes in stockholders' equity, and cash flows for each of the years in the three-year period ended December 31, 2014. We have also audited Chicopee Bancorp, Inc.'s internal control over financial reporting as of December 31, 2014, based on criteria established in the Internal Control - Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO"). Chicopee Bancorp, Inc.'s management is responsible for these financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Annual Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on these financial statements and an opinion on the Company's internal control over financial reporting based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with U.S. generally accepted accounting principles ("GAAP"). A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with GAAP, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Chicopee Bancorp, Inc. and Subsidiaries as of December 31, 2014 and 2013, and the consolidated results of their operations and their consolidated cash flows for each of the years in the three-year period ended

December 31, 2014, in conformity with GAAP. Also, in our opinion, Chicopee Bancorp, Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2014, based on criteria established in COSO.

Berry Dunn McNeil & Parker, LLC  
Portland, Maine

March 12, 2015

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## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## CONSOLIDATED BALANCE SHEETS

|   | December 31,                      |           |
|---|-----------------------------------|-----------|
|   | 2014                              | 2013      |
|   | (In Thousands, except share data) |           |
| <b>ASSETS</b>   |                                   |           |
| Cash and due from banks   | \$8,794                           | \$9,100   |
| Federal funds sold  | 2,915                             | 426       |
| Interest-bearing deposits with the Federal Reserve Bank of Boston   | 38,060                            | 9,389     |
| Cash and cash equivalents   | 49,769                            | 18,915    |
| Available-for-sale securities, at fair value  | 414                               | 602       |
| Held-to-maturity securities, at cost (fair value \$34,229 and \$49,338 at December 31, 2014 and December 31, 2013, respectively)  | 33,747                            | 48,606    |
| Federal Home Loan Bank stock, at cost   | 3,914                             | 3,914     |
| Loans held for sale   | —                                 | 70        |
| Loans receivable, net of allowance for loan losses (\$4,927 and \$4,596 at December 31, 2014 and December 31, 2013, respectively)   | 519,757                           | 485,619   |
| Other real estate owned   | 1,050                             | 407       |
| Mortgage servicing rights   | 269                               | 381       |
| Bank owned life insurance   | 14,531                            | 14,173    |
| Premises and equipment, net   | 8,855                             | 9,181     |
| Accrued interest receivable   | 1,591                             | 1,609     |
| Deferred income tax asset   | 3,683                             | 3,042     |
| Other assets  | 1,642                             | 1,208     |
| Total assets  | \$639,222                         | \$587,727 |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>   |                                   |           |
| Deposits  |                                   |           |
| Demand deposits   | \$97,922                          | \$90,869  |
| NOW accounts  | 42,177                            | 40,774    |
| Savings accounts  | 50,716                            | 49,755    |
| Money market deposit accounts   | 121,106                           | 111,126   |
| Certificates of deposit   | 171,637                           | 157,242   |
| Total deposits  | 483,558                           | 449,766   |
| Federal Home Loan Bank advances   | 67,039                            | 44,992    |
| Accrued expenses and other liabilities  | 491                               | 739       |
| Total liabilities   | 551,088                           | 495,497   |
| Commitments and contingencies (Notes 10,11,12,13,15,16,17 and 20)   |                                   |           |
| Stockholders' equity  |                                   |           |
| Common stock (no par value, 20,000,000 shares authorized, 7,439,368 shares issued; 5,270,670 and 5,435,885 shares outstanding at December 31, 2014 and December 31, 2013, respectively) | 72,479                            | 72,479    |
| Treasury stock, at cost, 2,168,698 and 2,003,483 shares at December 31, 2014 and December 31, 2013, respectively  | (29,119)                          | (26,435)  |
| Additional paid-in capital  | 3,595                             | 3,299     |
| Unearned compensation (restricted stock awards)   | (7)                               | (12)      |



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|   |           |           |   |
|---|-----------|-----------|---|
| Unearned compensation (Employee Stock Ownership Plan) | (3,273    | ) (3,571  | ) |
| Retained earnings                                     | 44,430    | 46,418    |   |
| Accumulated other comprehensive income                | 29        | 52        |   |
| Total stockholders' equity                            | 88,134    | 92,230    |   |
| Total liabilities and stockholders' equity            | \$639,222 | \$587,727 |   |

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

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## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF OPERATIONS

|   | Years Ended December 31,          |           |          |
|---|-----------------------------------|-----------|----------|
|   | 2014                              | 2013      | 2012     |
|   | (In Thousands, except share data) |           |          |
| Interest and dividend income:                       |                                   |           |          |
| Loans, including fees                               | \$21,724                          | \$21,324  | \$22,649 |
| Interest and dividends on securities                | 1,589                             | 1,690     | 1,684    |
| Other interest-earning assets                       | 41                                | 55        | 64       |
| Total interest and dividend income                  | 23,354                            | 23,069    | 24,397   |
| Interest expense:                                   |                                   |           |          |
| Deposits  | 2,773                             | 3,635     | 4,412    |
| Securities sold under agreements to repurchase      | —                                 | 9         | 13       |
| Other borrowed funds                                | 910                               | 705       | 1,202    |
| Total interest expense                              | 3,683                             | 4,349     | 5,627    |
| Net interest income                                 | 19,671                            | 18,720    | 18,770   |
| Provision for loan losses                           | 5,271                             | 425       | 442      |
| Net interest income after provision for loan losses | 14,400                            | 18,295    | 18,328   |
| Non-interest income:                                |                                   |           |          |
| Service charges, fee and commissions                | 2,352                             | 2,210     | 2,228    |
| Loan sales and servicing, net                       | 197                               | 622       | 667      |
| Net gain on sales of available-for-sale securities  | 34                                | 37        | —        |
| Loss on sale of other real estate owned             | (125)                             | ) (158    | ) (249)  |
| Other than temporary impairment charge              | —                                 | —         | (37)     |
| Income from bank owned life insurance               | 359                               | 366       | 380      |
| Other non-interest income                           | —                                 | 23        | 34       |
| Total non-interest income                           | 2,817                             | 3,100     | 3,023    |
| Non-interest expenses:                              |                                   |           |          |
| Salaries and employee benefits                      | 9,927                             | 10,165    | 10,429   |
| Occupancy expenses                                  | 1,357                             | 1,332     | 1,269    |
| Furniture and equipment                             | 726                               | 699       | 728      |
| FDIC insurance assessment                           | 424                               | 231       | 357      |
| Data processing                                     | 1,390                             | 1,244     | 1,119    |
| Professional fees                                   | 943                               | 652       | 550      |
| Advertising   | 563                               | 573       | 594      |
| Foreclosure expense                                 | 494                               | 155       | 224      |
| Stationery, supplies and postage                    | 260                               | 291       | 337      |
| Other non-interest expense                          | 2,816                             | 2,813     | 2,698    |
| Total non-interest expenses                         | 18,900                            | 18,155    | 18,305   |
| Income (loss) before income tax expense (benefit)   | (1,683)                           | ) 3,240   | 3,046    |
| Income tax expense (benefit)                        | (1,105)                           | ) 687     | 581      |
| Net income (loss)                                   | \$(578)                           | ) \$2,553 | \$2,465  |
| Earnings (loss) per share:                          |                                   |           |          |

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|  |           |           |           |
|--|-----------|-----------|-----------|
| Basic (loss) earnings per share                              | \$ (0.12  | ) \$ 0.51 | \$ 0.49   |
| Diluted (loss) earnings per share                            | \$ (0.12  | ) \$ 0.50 | \$ 0.48   |
| Basic weighted average number of common shares outstanding   | 5,020,140 | 5,037,783 | 5,072,875 |
| Diluted weighted average number of common shares outstanding | 5,090,723 | 5,129,527 | 5,088,734 |

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

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## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

|  | Years Ended December 31, |           |         |   |
|--|--------------------------|-----------|---------|---|
|  | 2014                     | 2013      | 2012    |   |
|  | (In Thousands)           |           |         |   |
| Net income (loss)  | \$(578                   | ) \$2,553 | \$2,465 |   |
| Other comprehensive income (loss), net of tax                |                          |           |         |   |
| Available-for-sale securities:                               |                          |           |         |   |
| Net unrealized holding gains (losses) arising during period  | (1                       | ) 77      | 8       |   |
| Other than temporary impairment charge realized in income    | —                        | —         | 37      |   |
| (1)  |                          |           |         |   |
| Reclassification adjustment for gains realized in net income | (34                      | ) (37     | ) —     |   |
| (1)  |                          |           |         |   |
| Tax effect   | 12                       | (14       | ) (16   | ) |
| Total other comprehensive income (loss), net of tax          | (23                      | ) 26      | 29      |   |
| Total comprehensive income (loss)                            | \$(601                   | ) \$2,579 | \$2,494 |   |

(1) Reclassified into the consolidated statements of operations in net gain on sales of available-for-sale securities and other than temporary impairment charge.

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

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## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

Years Ended December 31, 2014, 2013, and 2012

| (In Thousands, except<br>number of shares)   | Common<br>Stock | Treasury<br>Stock | Additional<br>Paid-in<br>Capital | Unearned<br>Compensation<br>(Equity<br>Incentive<br>Plan) | Unearned<br>Compensation<br>(ESOP) | Retained<br>Earnings | Accumulated<br>Other<br>Comprehensive<br>(Loss)<br>Income | Total    |
|--|-----------------|-------------------|----------------------------------|---|------------------------------------|----------------------|---|----------|
| Balance at December 31,<br>2011  | \$72,479        | \$(22,190)        | \$ 2,800                         | \$ (546 )   | \$ (4,166 )                        | \$42,408             | \$ (3 )   | \$90,782 |
| Comprehensive income:  |                 |                   |                                  |   |                                    |                      |   |          |
| Net income   | —               | —                 | —                                | —   | —                                  | 2,465                | —   | 2,465    |
| Change in net unrealized<br>gain on available-for-sale<br>securities (net of deferred<br>income taxes of \$16) | —               | —                 | —                                | —   | —                                  | —                    | 29  | 29       |
| Total comprehensive<br>income  | —               | —                 | —                                | —   | —                                  | —                    | —   | 2,494    |
| Treasury stock purchased<br>(307,718 shares)   | —               | (4,377 )          | —                                | —   | —                                  | —                    | —   | (4,377 ) |
| Adjustment to treasury<br>shares   | —               | —                 | —                                | 32  | —                                  | —                    | —   | 32       |
| Stock options exercised  | —               | —                 | (53 )                            | —   | —                                  | —                    | —   | (53 )    |
| Stock option expense   | —               | —                 | 278                              | —   | —                                  | —                    | —   | 278      |
| Change in unearned<br>compensation:  |                 |                   |                                  |   |                                    |                      |   |          |
| Restricted stock award<br>expense  | —               | —                 | (113 )                           | 496   | —                                  | —                    | —   | 383      |
| Common stock held by<br>ESOP committed to be<br>released   | —               | —                 | 132                              | —   | 298                                | —                    | —   | 430      |
| Balance at December 31,<br>2012  | 72,479          | (26,567 )         | 3,044                            | (18 )   | (3,868 )                           | 44,873               | 26  | 89,969   |
| Comprehensive income:  |                 |                   |                                  |   |                                    |                      |   |          |
| Net income   | —               | —                 | —                                | —   | —                                  | 2,553                | —   | 2,553    |
| Change in net unrealized<br>gain on available-for-sale<br>securities (net of deferred<br>income taxes of \$14) | —               | —                 | —                                | —   | —                                  | —                    | 26  | 26       |
| Total comprehensive<br>income  | —               | —                 | —                                | —   | —                                  | —                    | —   | 2,579    |
| Treasury stock purchased<br>(13,700 shares)  | —               | (242 )            | —                                | —   | —                                  | —                    | —   | (242 )   |
| Stock options exercised  | —               | 374               | (75 )                            | —   | —                                  | —                    | —   | 299      |
| Stock option expense   | —               | —                 | 118                              | —   | —                                  | —                    | —   | 118      |

|   |          |            |         |         |            |          |       |          |
|---|----------|------------|---------|---------|------------|----------|-------|----------|
| Change in unearned compensation:  |          |            |         |         |            |          |       |          |
| Restricted stock award expense  | —        | —          | —       | 6       | —          | —        | —     | 6        |
| Common stock held by ESOP committed to be released  | —        | —          | 212     | —       | 297        | —        | —     | 509      |
| Cash dividends (\$0.20 per share)   | —        | —          | —       | —       | —          | (1,008 ) | —     | (1,008 ) |
| Balance at December 31, 2013  | 72,479   | (26,435 )  | 3,299   | (12 )   | (3,571 )   | 46,418   | 52    | 92,230   |
| Comprehensive loss:   |          |            |         |         |            |          |       |          |
| Net loss  | —        | —          | —       | —       | —          | (578 )   | —     | (578 )   |
| Change in net unrealized gain on available-for-sale securities (net of deferred income taxes of \$12) | —        | —          | —       | —       | —          | —        | (23 ) | (23 )    |
| Total comprehensive loss  | —        | —          | —       | —       | —          | —        | —     | (601 )   |
| Treasury stock purchased (174,915 shares)   | —        | (2,862 )   | —       | —       | —          | —        | —     | (2,862 ) |
| Stock options exercised   | —        | 178        | (37 )   | —       | —          | —        | —     | 141      |
| Stock option expense  | —        | —          | 140     | —       | —          | —        | —     | 140      |
| Change in unearned compensation:  |          |            |         |         |            |          |       |          |
| Restricted stock award expense  | —        | —          | —       | 5       | —          | —        | —     | 5        |
| Common stock held by ESOP committed to be released  | —        | —          | 193     | —       | 298        | —        | —     | 491      |
| Cash dividends (\$0.28 per share)   | —        | —          | —       | —       | —          | (1,410 ) | —     | (1,410 ) |
| Balance at December 31, 2014  | \$72,479 | \$(29,119) | \$3,595 | \$ (7 ) | \$(3,273 ) | \$44,430 | \$ 29 | \$88,134 |

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

## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF CASH FLOWS

|  | Years Ended December 31, |           |           |
|--|--------------------------|-----------|-----------|
|  | 2014                     | 2013      | 2012      |
|  | (In Thousands)           |           |           |
| Cash flows from operating activities:  |                          |           |           |
| Net income (loss)  | \$(578 )                 | \$2,553   | \$2,465   |
| Adjustments to reconcile net income (loss) to net cash provided by operating activities: |                          |           |           |
| Depreciation and amortization  | 703                      | 945       | 906       |
| Gain on disposal of premises and equipment   | —                        | (24 )     | —         |
| Provision for loan losses  | 5,271                    | 425       | 442       |
| Increase in cash surrender value of life insurance                                       | (359 )                   | (366 )    | (380 )    |
| Net realized gain on sales of available-for-sale securities                              | (34 )                    | (37 )     | —         |
| Other than temporary impairment charge   | —                        | —         | 37        |
| Realized gains on sales of mortgages   | (55 )                    | (367 )    | (429 )    |
| Change in mortgage servicing rights  | 112                      | (13 )     | (24 )     |
| Net loss on sales and write downs of other real estate owned                             | 125                      | 158       | 249       |
| Loans originated for sale  | (4,681 )                 | (26,398 ) | (22,752 ) |
| Proceeds from loan sales   | 4,806                    | 26,695    | 24,816    |
| Deferred income taxes  | (629 )                   | 196       | (375 )    |
| Decrease in FDIC prepaid insurance   | —                        | 467       | 357       |
| (Increase) decrease in other assets  | (434 )                   | (35 )     | 233       |
| Decrease (increase) in accrued interest receivable                                       | 18                       | (42 )     | (40 )     |
| (Decrease) increase in other liabilities   | (248 )                   | (2 )      | 199       |
| Stock option expense   | 140                      | 118       | 278       |
| Change in unearned compensation  | 496                      | 515       | 813       |
| Net cash provided by operating activities  | 4,653                    | 4,788     | 6,795     |
| Cash flows from investing activities:  |                          |           |           |
| Purchase of premises and equipment   | (375 )                   | (439 )    | (437 )    |
| Net increase in loans  | (40,619 )                | (21,650 ) | (22,984 ) |
| Proceeds from sales of other real estate owned   | 442                      | 644       | 730       |
| Proceeds from sales of available-for-sale securities                                     | 187                      | 97        | —         |
| Purchases of held-to-maturity securities   | —                        | (27,015 ) | (49,833 ) |
| Maturities of held-to-maturity securities  | 13,373                   | 36,390    | 62,182    |
| Proceeds from principal paydowns of held-to-maturity securities                          | 1,486                    | 1,595     | 1,928     |
| Proceeds from the sale of FHLB stock   | —                        | 362       | 213       |
| Net cash used in investing activities  | (25,506 )                | (10,016 ) | (8,201 )  |
| Cash flows from financing activities:  |                          |           |           |
| Net increase (decrease) in deposits  | 33,791                   | (16,411 ) | 12,800    |
| Net decrease in securities sold under agreements to repurchase                           | —                        | (9,763 )  | (2,577 )  |
| Proceeds from long-term FHLB advances  | 33,000                   | 21,000    | —         |
| Payments on long-term FHLB advances  | (10,953 )                | (9,340 )  | (25,933 ) |
| Treasury stock purchased   | (2,862 )                 | (242 )    | (4,377 )  |
| Stock options exercised  | 141                      | 299       | (53 )     |
| Adjustment to treasury shares  | —                        | —         | 32        |
| Cash dividends paid on common stock  | (1,410 )                 | (1,008 )  | —         |

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|  |          |           |           |
|--|----------|-----------|-----------|
| Net cash provided by (used in) financing activities  | 51,707   | (15,465 ) | (20,108 ) |
| Net increase (decrease) in cash and cash equivalents | 30,854   | (20,693 ) | (21,514 ) |
| Cash and cash equivalents at beginning of year       | 18,915   | 39,608    | 61,122    |
| Cash and cash equivalents at end of year             | \$49,769 | \$18,915  | \$39,608  |
| Supplemental cash flow information:                  |          |           |           |
| Interest paid on deposits                            | \$2,773  | \$3,635   | \$4,412   |
| Interest paid on borrowings                          | 887      | 715       | 1,287     |
| Income taxes paid                                    | 22       | 571       | 767       |
| Transfers from loans to other real estate owned      | 1,211    | 636       | 639       |
| Gain on acquisition of other real estate owned       | —        | —         | 34        |

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

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CHICOPEE BANCORP, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Years Ended December 31, 2014, 2013 and 2012

Nature of Business

Chicopee Bancorp, Inc. (the "Company"), a Massachusetts corporation, was formed on March 14, 2006 by Chicopee Savings Bank (the "Bank") to become the holding company for the Bank upon completion of the Bank's conversion from a mutual savings bank to a stock savings bank. The conversion of the Bank was completed on July 19, 2006.

The Company provides a variety of financial services to individuals and businesses through its bank subsidiary Chicopee Savings Bank. The Bank is a Massachusetts state-chartered savings bank operating eight full service branch offices and our lending and operation center in Western Massachusetts. The Bank's primary source of revenue is earned by providing loans to small and middle-market businesses and to residential property homeowners. The Bank's primary deposit products are savings and term certificate accounts.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation and consolidation

The consolidated financial statements include the accounts of Chicopee Bancorp, Inc. and its wholly-owned subsidiaries, Chicopee Savings Bank and Chicopee Funding Corporation. The accounts of the Bank include all of its wholly-owned subsidiaries, Cabot Management Corporation, Cabot Realty, LLC, CSB Colts, Inc., and CSB Investment Corporation.

All significant intercompany balances and transactions have been eliminated in consolidation.

Use of estimates

In preparing consolidated financial statements in conformity with U.S. generally accepted accounting principles ("GAAP"), 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, the valuation of servicing assets, the valuation of other real estate owned ("OREO"), the determination of other-than-temporary impairment of investment securities ("OTTI"), and the deferred tax valuation allowance. In connection with the determination of the allowance for loan losses and the carrying value of OREO, management obtains independent appraisals for significant properties. While management uses available information to recognize losses on loans and OREO, future additions to the allowance for loan losses or future write-downs of OREO may be necessary based upon changes in economic and market conditions.

In addition, various regulatory agencies, as an integral part of their examination process, periodically review the Company's allowance for loan losses and the valuation of its OREO. Such agencies may require the Company to recognize additions to the allowance for loan losses or write-down of OREO based upon their judgment about information available to them at the time of their examination.

Significant group concentrations of credit risk

The Company does not have any significant concentrations to any one industry or customer. Although the Company has a diversified loan portfolio, most of the Company's activities are with customers located in Western Massachusetts. As a result, the Company and its borrowers may be especially vulnerable to the consequences of changes in the local economy.

#### Cash and cash equivalents

For purposes of the consolidated statements of cash flows, cash and cash equivalents include cash, due from banks, short-term investments with original maturities of ninety days or less and federal funds sold. The Company's due from bank accounts, at times, may exceed federally insured limits. The Company has not experienced any losses in such accounts. The Company believes it is not exposed to any significant risk on cash and cash equivalents.

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CHICOPEE BANCORP, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Securities

Debt securities that management has the positive intent and ability to hold to maturity are classified as “held-to-maturity” and recorded at amortized cost. Securities not classified as held-to-maturity, including equity securities with readily determinable fair values, are classified as “available-for-sale” and recorded at fair value, with unrealized gains and losses excluded from earnings and reported in other comprehensive income (loss). Restricted stock is carried at cost and evaluated for impairment.

Purchase premiums and discounts are recognized in interest income over the period to call or maturity using a method which yields results that do not differ materially from those which would be recognized by use of the effective-yield method.

For declines in the fair value of individual debt available-for-sale securities below their cost that are deemed to be other-than-temporary, where the Company does not intend to sell the security and it is more likely than not that the Company will not be required to sell the security before recovery of its amortized cost basis, the other-than-temporary decline in the fair value of the debt security related to 1) credit loss is recognized in earnings and 2) other factors is recognized in other comprehensive income or loss. Credit loss is determined to exist if the present value of expected future cash flows using the effective rate at acquisition is less than the amortized cost basis of the debt security. For individual debt securities where the Company intends to sell the security or more likely than not will be required to sell the security before recovery of its amortized cost, the other-than-temporary impairment is recognized in earnings equal to the difference between the security’s cost basis and its fair value at the balance sheet date. Gains and losses on the sale of securities are recorded on the trade date and are determined using the specific identification method.

Other-than-temporary impairment of investment securities

One of the significant estimates related to investment securities is the evaluation of OTTI. The evaluation of securities for OTTI is a quantitative and qualitative process, which is subject to risks and uncertainties and is intended to determine whether declines in the fair value of investments should be recognized in current period earnings. The risks and uncertainties include changes in general economic conditions, the issuer’s financial condition and/or future prospects, the effects of changes in interest rates or credit spreads and the expected recovery period of unrealized losses. Securities that are in an unrealized loss position are reviewed at least monthly to determine if OTTI is present based on certain quantitative and qualitative factors and measures. The primary factors considered in evaluating whether a decline in the value of securities is other-than-temporary include: (a) the length of time and extent to which the fair value has been less than cost or amortized cost and the expected recovery period of the security, (b) the financial condition, credit rating and future prospects of the issuer, (c) whether the debtor is current on contractually obligated interest and principal payments, (d) the volatility of the securities market price, (e) the intent and ability of the Company to retain the investment for a period of time sufficient to allow for recovery, which may be at maturity and (f) any other information and observable data considered relevant in determining whether other-than-temporary impairment has occurred, including the expectation of receipt of all principal and interest due.

Federal Home Loan Bank stock

As a member of the Federal Home Loan Bank of Boston (“FHLB”), the Company is required to maintain an investment in capital stock of the FHLB. Based on redemption provisions of the FHLB, the stock has no quoted market value and is carried at cost. At its discretion, the FHLB may declare dividends on its stock. The Company

reviews its investment in FHLB stock for impairment based on the ultimate recoverability of the cost basis in the FHLB stock. As of December 31, 2014 and 2013, no impairment has been recognized.

#### Loans held for sale

Loans originated and intended for sale in the secondary market are carried at the lower of amortized cost or estimated fair value, as determined by current investor yield requirements, in the aggregate. Net unrealized losses, if any, are recognized through a valuation allowance by charges to non-interest income.

#### Loans

The Company grants residential real estate, commercial and consumer loans to customers. Residential real estate loans include residential loans secured by owner-occupied, first lien real estate and residential construction loans.

Commercial and industrial loans include commercial real estate, commercial and industrial, commercial construction and residential investment loans. Consumer loans include second mortgages, home improvement loans, equity loans, automobile and, to a lesser extent, personal

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CHICOPEE BANCORP, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

loans. For purposes of evaluating the risk in the loan portfolio, management identified the following loan classes, which are used in evaluating the adequacy of the allowance for loan losses: residential real estate, residential construction, commercial real estate, commercial construction, commercial and industrial, consumer and home equity loans.

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or pay-off generally are reported at their outstanding unpaid principal balances adjusted for charge-offs, the allowance for loan losses, and any deferred fees or costs on originated loans. Interest income is accrued on the unpaid principal balance. Loan origination fees, net of certain direct origination costs, are deferred and recognized as an adjustment of the related loan yield using the interest method.

Delinquency and nonaccrual

The Company considers all loan classes past due greater than 30 days delinquent based on the contractual terms of the loan and factored on a 30-day month. Management continuously monitors delinquency and nonaccrual levels and trends. The accrual of interest on residential real estate, commercial real estate, construction and commercial and industrial loans is discontinued at the earlier of when reasonable doubt exists as to the full collection of interest and principal or at the time the loan is 90 days past due or earlier if the loan is considered impaired. Other loans are typically charged off no later than 120 days past due. In all cases, loans are placed on nonaccrual or charged off at an earlier date if collection of principal or interest is considered doubtful. All interest accrued but not collected for loans that are placed on nonaccrual or charged off is reversed against interest income. The interest on these loans is accounted for on the cash-basis until qualifying for return to accrual status. Nonaccrual loans, including modified loans, are returned to accrual status when the borrower has shown the ability and an acceptable history of repayment and when subsequent performance reduces the concern as to the collectability of principal and interest. In order to demonstrate the ability and acceptable history of repayment, the borrower must be current with the payments in accordance with the loan terms for a minimum of six months as determined on a case-by-case basis.

Loans charged off

Commercial and industrial loans. Loans past due more than 120 days are considered for one of three options: charge off the balance of the loan, charge off any excess balance over the fair value of the collateral securing the loan, or continue collection efforts subject to a monthly review until either the balance is collected or a charge-off recommendation can be reasonably made.

Residential loans. In general, one-to-four family residential loans and home equity loans that are delinquent 90 days or more are classified substandard. An updated appraisal is obtained when the loan is 90 days or more delinquent. Any outstanding balance in excess of the fair value of the property, less cost to sell, is charged-off against the allowance for loan losses.

Consumer loans. Generally all loans are automatically considered for charge-off at 90 to 120 days from the contractual due date, unless there is liquid collateral in hand sufficient to repay principal and interest in full.

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

uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

Management believes the allowance for loan losses requires the most significant estimates and assumptions used in the preparation of the consolidated financial statements. The allowance for loan losses is based on management's evaluation of the level of the allowance required in relation to the probable loss exposure in the loan portfolio. The allowance for loan losses is evaluated on a regular basis by management. Qualitative factors or risks considered in evaluating the adequacy of the allowance for loan losses for all loan classes include historical loss experience; levels and trends in delinquencies, nonaccrual loans, impaired loans and net charge-offs; the character and size of the loan portfolio; effects of any changes in underwriting policies; experience of management and staff; current economic conditions and the effect on borrowers; effects of changes in credit concentrations; and management's estimation of probable losses. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

The allowance consists of specific, general and unallocated components. The specific component relates to loans that are classified as doubtful, substandard, special mention, or loss. For such loans that are also classified as impaired, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan. The general component covers non-classified loans and is based on historical loss experience adjusted for qualitative factors. An unallocated component is maintained to cover uncertainties that could affect management's estimate of

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CHICOPEE BANCORP, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

probable losses. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general losses in the portfolio. There was no unallocated component of the allowance at December 31, 2014 and 2013.

There were no changes in the allowance for loan losses methodology during the year ended December 31, 2014.

Impairment

Loans individually considered for impairment include all classes of commercial and residential, as well as home equity loans. These loans are considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant 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.

Impairment is measured on a loan-by-loan basis by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price, or the fair value of the collateral, less costs to sell, if the loan is collateral dependent.

Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. Accordingly, the Company does not separately identify individual consumer loans for impairment evaluation, except for home equity loans.

The Company 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 troubled debt restructuring ("TDR"). All TDRs are classified as impaired.

Other real estate owned

The Company classifies property acquired through foreclosure or acceptance of a deed-in-lieu of foreclosure as OREO in its consolidated financial statements. The Company generally obtains a new or updated valuation of OREO at the time of acquisition, including periodic reappraisals, at least annually, to ensure any material change in market conditions or the physical aspects of the property are recognized. When property is placed in OREO, it is recorded at fair value less estimated cost to sell at the date of foreclosure or acceptance of deed-in-lieu of foreclosure. At the time of transfer to OREO, any excess of carrying value over fair value less estimated cost to sell is charged to the allowance for loan losses. Management, or its designee, inspects all OREO property periodically. Holding costs and declines in fair value result in charges to expense after the property is acquired.

Loan servicing

The valuation of mortgage servicing rights is a critical accounting policy, which requires significant estimates and assumptions. The Company often sells mortgage loans it originates and retains the ongoing servicing of such loans,

receiving a fee for these services, generally 1% of the outstanding balance of the loan per annum. Servicing assets are recognized at fair value as separate assets when servicing rights are acquired through the sale of loans. Capitalized servicing rights are reported in other assets and are amortized against non-interest income in proportion to, and over the period of, the estimated future net servicing income of the underlying financial assets. Management uses an independent firm which specializes in the valuation of mortgage servicing rights to determine fair value. The most important assumption is the anticipated loan prepayment rate, and increases in prepayment speed result in lower valuations of mortgage servicing rights. Servicing assets are evaluated for impairment based upon the fair value of the rights as compared to amortized cost. Impairment is determined by stratifying rights by predominant characteristics, such as interest rate in increments of 50 basis points and term primarily of 15 and 30 years. Fair value is based upon discounted cash flows using market-based assumptions. Projected prepayments on the portfolio are estimated using the Public Securities Association Standard Prepayment Model. Impairment is recognized through a valuation allowance for an individual stratum, to the extent that fair value is less than the capitalized amount for the stratum. The use of different assumptions could produce a different valuation. All of the assumptions are based on standards the Company believes would be utilized by market participants in valuing mortgage servicing rights and are consistently derived and/or benchmarked against independent public sources.



CHICOPEE BANCORP, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Credit related financial instruments

In the ordinary course of business, the Company has entered into commitments to extend credit, including commercial letters of credit and standby letters of credit. Such financial instruments are recorded when they are funded.

Premises and equipment

Land is carried at cost. Buildings, leasehold improvements and equipment are stated at cost, less accumulated depreciation and amortization, computed on the straight-line method over the shorter of the estimated useful lives of the assets or the lease term. The cost of maintenance is expensed as incurred.

Income taxes

Deferred income tax assets and liabilities are determined using the liability (or balance sheet) method. Under this method, the net deferred tax asset or liability is determined based on the tax effects of the temporary differences between the book and tax bases of the various balance sheet assets and liabilities and certain carryforwards of losses and deductions that are available to offset future taxable income and gives current recognition to changes in tax rates and laws.

Employee stock ownership plan ("ESOP")

Compensation expense is recognized as ESOP shares are committed to be released and is calculated based upon the average market price for the current year. Allocated and committed-to-be-released ESOP shares are considered outstanding for earnings per share calculations based on debt service payments. Other ESOP shares are excluded from earnings per share calculations. Dividends declared on allocated ESOP shares are charged to retained earnings. Dividends declared on unallocated ESOP shares are used to satisfy debt service. The value of unearned shares to be allocated to ESOP participants for future services not yet performed is reflected as a reduction of stockholders' equity.

Equity Incentive Plan

The Company expenses compensation cost associated with share-based payment transactions, such as options and restricted stock awards, in the consolidated financial statements over the requisite service (vesting) period.

Advertising

Advertising costs are expensed as incurred.

Earnings (loss) per common share

Basic earnings (loss) per share represents income available to common stockholders divided by the weighted-average number of common shares outstanding during the period. The adjusted outstanding common shares equals the gross number of common shares issued less treasury shares, unallocated shares of the Chicopee Savings Bank ESOP, and nonvested restricted stock awards under the 2007 Equity Incentive Plan. Diluted earnings per 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 the Company relate to outstanding stock options and certain stock awards and

are determined using the treasury stock method.

Unvested share-based payment awards that contain non-forfeitable rights to dividends or dividend equivalents are participating securities and, therefore, are included in computing earnings per share pursuant to the two-class method. The two-class method determines earnings per share for each class of common stock and participating securities according to dividends or dividend equivalents and their respective participation rights in undistributed earnings. The Company's stock options and stock awards receive non-forfeitable dividends at the same rate as common stock. During the years ended December 31, 2014 and 2013, the Company paid a quarterly cash dividend of \$0.07 and \$0.05 per share, respectively. There were no dividends paid prior to 2013. The first dividend was declared on January 20, 2013. The following table sets forth the computation of basic and diluted earnings per share under the two-class method:

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## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

| (In Thousands)  | Years Ended December 31, |               |               |
|---|--------------------------|---------------|---------------|
|   | 2014                     | 2013          | 2012          |
| Net income (loss)   | \$ (578)                 | ) \$ 2,553    | \$ 2,465      |
| Weighted average number of common shares issued               | 7,439,368                | 7,439,368     | 7,439,368     |
| Less: average number of treasury shares                       | (2,061,264)              | ) (2,013,461) | ) (1,918,041) |
| Less: average number of unallocated ESOP shares               | (357,089)                | ) (386,848)   | ) (416,605)   |
| Less: average number of nonvested restricted stock awards     | (875)                    | ) (1,276)     | ) (31,847)    |
| Adjusted weighted average number of common shares outstanding | 5,020,140                | 5,037,783     | 5,072,875     |
| Plus: dilutive nonvested restricted stock awards              | 297                      | 395           | 15,358        |
| Plus: dilutive outstanding stock options                      | 70,286                   | 91,349        | 501           |
| Weighted average number of diluted shares outstanding         | 5,090,723                | 5,129,527     | 5,088,734     |
| Net income (loss) per share:                                  |                          |               |               |
| Basic- common stock   | \$ (0.12)                | ) \$ 0.51     | \$ 0.49       |
| Basic- unvested share-based payment awards                    | \$ (0.12)                | ) \$ 0.51     | \$ 0.49       |
| Diluted- common stock   | \$ (0.12)                | ) \$ 0.50     | \$ 0.48       |
| Diluted- unvested share-based payment awards                  | \$ (0.12)                | ) \$ 0.50     | \$ 0.48       |

There were 92,000, 97,000, and 583,198 stock options for the years ended December 31, 2014, 2013, and 2012, which were excluded from the diluted earnings per share because their effect is anti-dilutive.

## Segment reporting

The Company's operations are solely in the financial services industry and consist of providing traditional banking services to its customers. Management makes operating decisions and assesses performance based on an ongoing review of the Company's consolidated financial results. Therefore, the Company has a single operating segment for financial reporting purposes.

## Recent accounting pronouncements

In January 2014, Financial Accounting Standards Board ("FASB") issued Accounting Standard Update ("ASU") No. 2014-04, Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure. The amendments in this ASU clarify that an in substance repossession or foreclosure occurs, and a creditor is considered to have received physical possession of residential real estate property collateralizing a consumer mortgage loan, upon either (1) the creditor obtaining legal title to the residential real estate property upon completion of a foreclosure or (2) the borrower conveying all interest in the residential real estate property to the creditor to satisfy that loan through completion of a deed in lieu of foreclosure or through a similar legal agreement. Additionally, the amendments require disclosure of both (1) the amount of foreclosed residential real estate property held by the creditor and (2) the recorded investment in consumer mortgage loans collateralized by residential real estate property that are in the process of foreclosure. The amendments in this ASU are effective for annual periods beginning after December 15, 2014. Management has reviewed the ASU and does not believe that it will have a material effect on the Company's consolidated financial statements.

In May 2014, FASB issued ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606). The ASU was issued to clarify the principles for recognizing revenue and to develop a common revenue standard. The ASU is effective for annual reporting periods beginning after December 15, 2016, including interim periods within that

reporting period. The Company is currently evaluating the potential impact of the ASU on its consolidated financial statements.

In June 2014, FASB issued ASU No. 2014-11, Transfers and Servicing (Topic 860): Repurchase-to-Maturity Transactions, Repurchase Financings, and Disclosures. The ASU was issued to respond to concerns about current accounting and disclosures for repurchase agreements and similar transactions. The concern was that under current accounting guidance there is an unnecessary distinction between the accounting for different types of repurchase agreements. Under current guidance, the repurchase-to-maturity transactions are accounted for as sales with forward agreements, whereas repurchase agreements that settle before the maturity of the transferred financial asset are accounted for as secured borrowings. The ASU amendments require new disclosures for repurchase agreements, securities lending transactions, and repurchase-to-maturity transactions accounted for as secure borrowings. The ASU

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## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

is effective for annual periods, and interim periods within those annual periods, beginning after December 15, 2014. The ASU will not have a material effect on the Company's consolidated financial statements.

In June 2014, FASB issued ASU No. 2014-12, Compensation - Stock Compensation (Topic 718): Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period. The ASU was issued because current U.S. GAAP does not contain explicit guidance on how to account for share-based payments when a performance target could be achieved after the requisite service period. The ASU is effective for annual periods and interim periods within those annual periods beginning after December 15, 2015. The ASU will not have a material effect on the Company's consolidated financial statements.

## Reclassifications

Certain amounts in the 2013 and 2012 financial statements have been reclassified to conform to the 2014 presentation.

## 2. RESTRICTIONS ON CASH AND AMOUNTS DUE FROM BANKS

The Company is required to maintain average balances on hand or deposits with the Federal Reserve Bank of Boston. At December 31, 2014 and 2013, these reserve balances amounted to \$6.9 million and \$8.5 million, respectively, and are included in interest bearing deposits.

## 3. INVESTMENT SECURITIES

The following tables set forth, at the dates indicated, information regarding the amortized cost and fair value, with gross unrealized gains and losses of the Company's investment securities:

|  | December 31, 2014 |                              |                               |               |
|--|-------------------|------------------------------|-------------------------------|---------------|
|  | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Fair<br>Value |
|  | (In Thousands)    |                              |                               |               |
| Available-for-sale securities:         |                   |                              |                               |               |
| Marketable equity securities           | \$ 369            | \$ 45                        | \$—                           | \$ 414        |
| Total available-for-sale securities    | \$ 369            | \$ 45                        | \$—                           | \$ 414        |
| Held-to-maturity securities:           |                   |                              |                               |               |
| Corporate and industrial revenue bonds | \$ 33,344         | \$ 467                       | \$—                           | \$ 33,811     |
| Collateralized mortgage obligations    | 403               | 15                           | —                             | 418           |
| Total held-to-maturity securities      | \$ 33,747         | \$ 482                       | \$—                           | \$ 34,229     |
| Non-marketable securities:             |                   |                              |                               |               |
| Federal Home Loan Bank stock           | \$ 3,914          | \$—                          | \$—                           | \$ 3,914      |
| Banker's Bank Northeast stock          | 183               | —                            | —                             | 183           |
| Total non-marketable securities        | \$ 4,097          | \$—                          | \$—                           | \$ 4,097      |

## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

|                                     | December 31, 2013 |                              |                               |               |
|-------------------------------------|-------------------|------------------------------|-------------------------------|---------------|
|                                     | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Fair<br>Value |
|                                     | (In Thousands)    |                              |                               |               |
| Available-for-sale securities:      |                   |                              |                               |               |
| Marketable equity securities        | \$522             | \$80                         | \$—                           | \$602         |
| Total available-for-sale securities | \$522             | \$80                         | \$—                           | \$602         |
| Held-to-maturity securities:        |                   |                              |                               |               |
| U.S. Treasury securities            | \$5,000           | \$—                          | \$—                           | \$5,000       |
| Industrial revenue bonds            | 34,588            | 681                          | —                             | 35,269        |
| Certificates of deposit             | 8,373             | 15                           | —                             | 8,388         |
| Collateralized mortgage obligations | 645               | 36                           | —                             | 681           |
| Total held-to-maturity securities   | \$48,606          | \$732                        | \$—                           | \$49,338      |
| Non-marketable securities:          |                   |                              |                               |               |
| Federal Home Loan Bank stock        | \$3,914           | \$—                          | \$—                           | \$3,914       |
| Banker's Bank Northeast stock       | 183               | —                            | —                             | 183           |
| Total non-marketable securities     | \$4,097           | \$—                          | \$—                           | \$4,097       |

The amortized cost and estimated fair value of debt securities by contractual maturity at December 31, 2014 are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without prepayment penalties. The collateralized mortgage obligations are allocated to maturity categories according to final maturity date.

|                    | Held-to-maturity  |            |
|--------------------|-------------------|------------|
|                    | Amortized<br>Cost | Fair Value |
|                    | (In Thousands)    |            |
| Within 1 year      | \$—               | \$—        |
| From 1 to 5 years  | 8,286             | 8,610      |
| From 5 to 10 years | —                 | —          |
| Over 10 years      | 25,461            | 25,619     |
| Total              | \$33,747          | \$34,229   |

During the years ended December 31, 2014 and 2013, proceeds from sales of available-for-sale securities amounted to \$187,000 and \$97,000, respectively. Gross realized gains of \$34,000 and \$37,000 were realized during the years ended December 31, 2014 and 2013, respectively. There were no gross realized losses for the years ended December 31, 2014 and 2013. The tax provision applicable to these net realized gains in 2014 and 2013 was \$12,000 and \$13,000, respectively.

Management conducts, at least on a monthly basis, a review of its investment portfolio including available-for-sale and held-to-maturity securities to determine if the value of any security has declined below its cost or amortized cost and whether such decline is OTTI.

For the year ended December 31, 2014 and 2013, management determined that there were no securities other-than-temporarily impaired.

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CHICOPEE BANCORP, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Unrealized Losses on Investment Securities

There were no continuous unrealized losses for the years ended December 31, 2014 and 2013, respectively.

Non-Marketable Securities

The Company is a member of the FHLB, a cooperatively owned wholesale bank for housing and finance in the six New England States. Its mission is to support the residential mortgage and community development lending activities of its members, which include over 450 financial institutions across New England. As a requirement of membership in the FHLB, the Company must own a minimum required amount of FHLB stock, calculated periodically based primarily on the Company's level of borrowings from the FHLB. The Company uses the FHLB for much of its wholesale funding needs. As of December 31, 2014 and 2013, the Company's investment in FHLB stock totaled \$3.9 million.

FHLB stock is a non-marketable equity security and therefore is reported at cost, which equals par value. Shares held in excess of the minimum required amount are generally redeemable at par value. For the years ended December 31, 2014 and 2013, the Company received \$58,000 and \$15,000, respectively, in dividend income from its FHLB stock investment.

The Company periodically evaluates its investment in FHLB stock for impairment based on, among other factors, the capital adequacy of the FHLB and its overall financial condition. There have not been any impairment losses recorded through December 31, 2014 and the Company will continue to monitor its FHLB stock investment.

Banker's Bank Northeast (BBN) stock is reported under other assets in the consolidated balance sheets and is carried at cost. The BBN stock investment is evaluated for impairment based on an estimate of the ultimate recovery to par value. As of December 31, 2014 and 2013, the Company's investment in BBN totaled \$183,000. There have not been any impairment losses recorded through December 31, 2014 and the Company will continue to monitor its BBN stock investment.



## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## 4. LOANS

The following table sets forth the composition of the Company's loan portfolio in dollar amounts and as a percentage of the respective portfolio.

|                                      | December 31, 2014 |                  | December 31, 2013 |                  |   |
|--------------------------------------|-------------------|------------------|-------------------|------------------|---|
|                                      | Amount            | Percent of Total | Amount            | Percent of Total |   |
|                                      | (In Thousands)    |                  |                   |                  |   |
| Real estate loans:                   |                   |                  |                   |                  |   |
| Residential real estate <sup>1</sup> | \$ 118,692        | 22.7             | % \$ 112,524      | 23.0             | % |
| Home equity                          | 34,508            | 6.6              | % 32,091          | 6.6              | % |
| Commercial                           | 249,632           | 47.7             | % 211,161         | 43.1             | % |
| Total                                | 402,832           | 77.0             | % 355,776         | 72.7             | % |
| Construction-residential             | 8,129             | 1.6              | % 6,130           | 1.3              | % |
| Construction-commercial              | 35,786            | 6.8              | % 38,441          | 7.9              | % |
| Total construction                   | 43,915            | 8.4              | % 44,571          | 9.2              | % |
| Total real estate loans              | 446,747           | 85.4             | % 400,347         | 81.9             | % |
| Consumer loans                       | 2,662             | 0.5              | % 2,405           | 0.4              | % |
| Commercial and industrial loans      | 74,331            | 14.1             | % 86,540          | 17.7             | % |
| Total loans                          | 523,740           | 100.0            | % 489,292         | 100.0            | % |
| Deferred loan origination costs, net | 944               |                  | 923               |                  |   |
| Allowance for loan losses            | (4,927)           | )                | (4,596)           | )                |   |
| Loans, net                           | \$ 519,757        |                  | \$ 485,619        |                  |   |

<sup>1</sup> Excludes loans held for sale of \$70,000 at December 31, 2013.

## Risk characteristics

Residential real estate includes loans which enable the borrower to purchase or refinance existing homes, most of which serve as the primary residence of the owner. Repayment is dependent on the credit quality of the borrower. Factors attributable to failure of repayment may include a weakened economy and/or unemployment, as well as possible personal considerations. While management anticipates adjustable-rate mortgages will better offset the potential adverse effects of an increase in interest rates as compared to fixed-rate mortgages, the increased mortgage payments required of adjustable-rate loan borrowers in a rising interest rate environment could cause an increase in delinquencies and defaults. The marketability of the underlying property also may be adversely affected in a high interest rate environment.

Commercial real estate loans are secured by commercial real estate and residential investment real estate and generally have larger balances and involve a greater degree of risk than one- to four-family residential mortgage loans. Risks in commercial real estate and residential investment lending include the borrower's creditworthiness and the feasibility and cash flow potential of the project. Payments on loans secured by income properties often depend on successful operation and management of the properties. As a result, repayment of such loans may be subject to a greater extent than residential real estate loans to adverse conditions in the real estate market or the economy.

Construction loans are generally considered to involve a higher degree of risk of loss than long-term financing on improved, occupied real estate. Risk of loss on a construction loan depends largely upon the accuracy of the initial estimate of the property's value at completion of construction and the estimated cost (including interest) of construction.

Commercial and industrial loans are of higher risk and typically are made on the basis of the borrower's ability to make repayment from the cash flow of the borrower's business. As a result, the availability of funds for the repayment of these loans may depend substantially on the success of the business itself. Further, any collateral securing such loans may depreciate over time, may be difficult to appraise and may fluctuate in value.

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CHICOPEE BANCORP, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

Credit quality

To evaluate the risk in the loan portfolio, internal credit risk ratings are used for the following loan classes: commercial real estate, commercial construction and commercial and industrial. The risks evaluated in determining an adequate credit risk rating, include the financial strength of the borrower and the collateral securing the loan. Commercial loans, including commercial and industrial, commercial real estate and commercial construction loans are rated from one through nine. Credit risk ratings one through five are considered pass ratings. Classified assets include credit risk ratings of special mention through loss. At least quarterly, classified assets are reviewed by management and by an independent third party. Credit risk ratings are updated as soon as information is obtained that indicates a change in the credit risk rating may be warranted.

Residential real estate and residential construction loans are categorized into pass and substandard risk ratings. Substandard residential loans are loans that are on nonaccrual status and are individually evaluated for impairment.

Consumer loans are considered nonperforming when they are 90 days past due or have not returned to accrual status. Consumer loans are not individually evaluated for impairment.

Home equity loans are considered nonperforming when they are 90 days past due or have not returned to accrual status. Each nonperforming home equity loan is individually evaluated for impairment.

The following describes the credit risk ratings for classified assets:

**Special mention.** Assets that do not currently expose the Company to sufficient risk to warrant classification in one of the following categories but possess potential weaknesses.

**Substandard.** Assets that have one or more defined weaknesses and are characterized by the distinct possibility that the Company will sustain some loss if the deficiencies are not corrected. Non-accruing loans are typically classified as substandard.

**Doubtful.** Assets that have the weaknesses of substandard assets with the additional characteristic that the weaknesses make collection or liquidation in full on the basis of currently existing facts, conditions and values questionable, and there is a high possibility of loss.

**Loss.** Assets rated in this category are considered uncollectible and are charged off against the allowance for loan losses.

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## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following table presents an analysis of total loans segregated by risk rating and class at December 31, 2014:

|                         | Commercial Credit Risk Exposure  |                             |                           | Total     |
|-------------------------|----------------------------------|-----------------------------|---------------------------|-----------|
|                         | Commercial<br>and Industrial     | Commercial<br>Construction  | Commercial<br>Real Estate |           |
|                         | (In Thousands)                   |                             |                           |           |
| Pass                    | \$66,442                         | \$27,547                    | \$234,866                 | \$328,855 |
| Special mention         | 4,991                            | 5,843                       | 10,034                    | 20,868    |
| Substandard             | 2,898                            | 2,396                       | 4,732                     | 10,026    |
| Doubtful                | —                                | —                           | —                         | —         |
| Loss                    | —                                | —                           | —                         | —         |
| Total commercial loans  | \$74,331                         | \$35,786                    | \$249,632                 | \$359,749 |
|                         | Residential Credit Risk Exposure |                             |                           | Total     |
|                         | Residential<br>Real Estate       | Residential<br>Construction |                           |           |
|                         | (In Thousands)                   |                             |                           |           |
| Pass                    | \$114,586                        | \$8,129                     |                           | \$122,715 |
| Nonperforming           | 4,106                            | —                           |                           | 4,106     |
| Total residential loans | \$118,692                        | \$8,129                     |                           | \$126,821 |
|                         | Consumer Credit Risk Exposure    |                             |                           | Total     |
|                         | Consumer                         | Home Equity                 |                           |           |
|                         | (In Thousands)                   |                             |                           |           |
| Performing              | \$2,630                          | \$34,159                    |                           | \$36,789  |
| Nonperforming           | 32                               | 349                         |                           | 381       |
| Total consumer loans    | \$2,662                          | \$34,508                    |                           | \$37,170  |

## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following table presents an analysis of total loans segregated by risk rating and class at December 31, 2013:

|                         | Commercial Credit Risk Exposure  |                             |                           |           |
|-------------------------|----------------------------------|-----------------------------|---------------------------|-----------|
|                         | Commercial and<br>Industrial     | Commercial<br>Construction  | Commercial<br>Real Estate | Total     |
|                         | (In Thousands)                   |                             |                           |           |
| Pass                    | \$77,483                         | \$27,969                    | \$200,096                 | \$305,548 |
| Special mention         | 4,050                            | 6,584                       | 3,594                     | 14,228    |
| Substandard             | 5,007                            | 3,888                       | 7,471                     | 16,366    |
| Doubtful                | —                                | —                           | —                         | —         |
| Loss                    | —                                | —                           | —                         | —         |
| Total commercial loans  | \$86,540                         | \$38,441                    | \$211,161                 | \$336,142 |
|                         | Residential Credit Risk Exposure |                             |                           |           |
|                         | Residential<br>Real Estate       | Residential<br>Construction |                           | Total     |
|                         | (In Thousands)                   |                             |                           |           |
| Pass                    | \$110,109                        | \$6,130                     |                           | \$116,239 |
| Nonperforming           | 2,415                            | —                           |                           | 2,415     |
| Total residential loans | \$112,524                        | \$6,130                     |                           | \$118,654 |
|                         | Consumer Credit Risk Exposure    |                             |                           |           |
|                         | Consumer                         | Home Equity                 |                           | Total     |
|                         | (In Thousands)                   |                             |                           |           |
| Performing              | \$2,397                          | \$31,798                    |                           | \$34,195  |
| Nonperforming           | 8                                | 293                         |                           | 301       |
| Total consumer loans    | \$2,405                          | \$32,091                    |                           | \$34,496  |

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## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following table presents the allowance for loan losses and select loan information for the year ended December 31, 2014:

|   | Residential<br>Real<br>Estate | Residential<br>Construction | Commercial<br>Real Estate | Commercial<br>Construction | Commercial<br>and<br>Industrial | Consumer | Home<br>Equity | Total     |
|---|-------------------------------|-----------------------------|---------------------------|----------------------------|---------------------------------|----------|----------------|-----------|
| Allowance for loan losses:                | (In Thousands)                |                             |                           |                            |                                 |          |                |           |
| Balance as of December 31, 2013           | \$650                         | \$94                        | \$2,121                   | \$435                      | \$1,110                         | \$35     | \$151          | \$4,596   |
| Provision for loan losses                 | 139                           | 13                          | 1,479                     | 1,672                      | 1,867                           | 43       | 58             | 5,271     |
| Recoveries                                | —                             | —                           | 74                        | —                          | 83                              | 23       | 1              | 181       |
| Loans charged off                         | (303)                         | —                           | (975)                     | (1,539)                    | (2,181)                         | (66)     | (57)           | (5,121)   |
| Balance as of December 31, 2014           | \$486                         | \$107                       | \$2,699                   | \$568                      | \$879                           | \$35     | \$153          | \$4,927   |
| Ending balance allowance for loan losses: |                               |                             |                           |                            |                                 |          |                |           |
| Collectively evaluated for impairment     | \$481                         | \$107                       | \$2,634                   | \$568                      | \$879                           | \$35     | \$150          | \$4,854   |
| Individually evaluated for impairment     | 5                             | —                           | 65                        | —                          | —                               | —        | 3              | 73        |
| Total:                                    | \$486                         | \$107                       | \$2,699                   | \$568                      | \$879                           | \$35     | \$153          | \$4,927   |
| Total loans ending balance:               |                               |                             |                           |                            |                                 |          |                |           |
| Collectively evaluated for impairment     | \$114,586                     | \$8,129                     | \$246,123                 | \$33,391                   | \$73,286                        | \$2,662  | \$34,160       | \$512,337 |
| Individually evaluated for impairment     | 4,106                         | —                           | 3,509                     | 2,395                      | 1,045                           | —        | 348            | 11,403    |
| Total:                                    | \$118,692                     | \$8,129                     | \$249,632                 | \$35,786                   | \$74,331                        | \$2,662  | \$34,508       | \$523,740 |



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## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following table presents the allowance for loan losses and select loan information as of December 31, 2013:

|   | Residential<br>Real Estate | Residential<br>Construction | Commercial<br>Real Estate | Commercial<br>Construction | Commercial<br>and<br>Industrial | Consumer | Home<br>Equity | Total     |
|---|----------------------------|-----------------------------|---------------------------|----------------------------|---------------------------------|----------|----------------|-----------|
| (In Thousands)                              |                            |                             |                           |                            |                                 |          |                |           |
| Allowance for loan losses:                  |                            |                             |                           |                            |                                 |          |                |           |
| Balance as of<br>December 31,<br>2012       | \$536                      | \$93                        | \$1,966                   | \$502                      | \$1,099                         | \$44     | \$124          | \$4,364   |
| Provision<br>(reduction) for<br>loan losses | 296                        | 63                          | (24)                      | (67)                       | 90                              | 30       | 37             | 425       |
| Recoveries                                  | 1                          | —                           | 247                       | —                          | 38                              | 14       | —              | 300       |
| Loans charged off                           | (183)                      | (62)                        | (68)                      | —                          | (117)                           | (53)     | (10)           | (493)     |
| Balance as of<br>December 31,<br>2013       | \$650                      | \$94                        | \$2,121                   | \$435                      | \$1,110                         | \$35     | \$151          | \$4,596   |
| Ending balance allowance for loan:          |                            |                             |                           |                            |                                 |          |                |           |
| Collectively<br>evaluated for<br>impairment | \$407                      | \$94                        | \$2,109                   | \$435                      | \$1,100                         | \$35     | \$137          | \$4,317   |
| Individually<br>evaluated for<br>impairment | 243                        | —                           | 12                        | —                          | 10                              | —        | 14             | 279       |
| Total:                                      | \$650                      | \$94                        | \$2,121                   | \$435                      | \$1,110                         | \$35     | \$151          | \$4,596   |
| Total loans ending balance:                 |                            |                             |                           |                            |                                 |          |                |           |
| Collectively<br>evaluated for<br>impairment | \$109,866                  | \$6,130                     | \$206,813                 | \$34,553                   | \$85,168                        | \$2,405  | \$31,798       | \$476,733 |
| Individually<br>evaluated for<br>impairment | 2,658                      | —                           | 4,348                     | 3,888                      | 1,372                           | —        | 293            | 12,559    |
| Total:                                      | \$112,524                  | \$6,130                     | \$211,161                 | \$38,441                   | \$86,540                        | \$2,405  | \$32,091       | \$489,292 |

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## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following table presents a summary of information pertaining to impaired loans by class as of December 31, 2014:

|   | Recorded<br>Investment | Unpaid<br>Balance | Average<br>Recorded<br>Investment | Related<br>Allowance | Interest<br>Income<br>Recognized |
|---|------------------------|-------------------|-----------------------------------|----------------------|----------------------------------|
|   | (In Thousands)         |                   |                                   |                      |                                  |
| Impaired loans without a valuation allowance: |                        |                   |                                   |                      |                                  |
| Residential real estate                       | \$3,495                | \$3,617           | \$2,634                           | \$—                  | \$105                            |
| Residential construction                      | —                      | —                 | —                                 | —                    | —                                |
| Commercial real estate                        | 2,700                  | 3,317             | 3,535                             | —                    | 55                               |
| Commercial construction                       | 2,395                  | 3,934             | 3,270                             | —                    | 111                              |
| Commercial and industrial                     | 1,045                  | 1,057             | 1,300                             | —                    | 43                               |
| Consumer                                      | —                      | —                 | —                                 | —                    | —                                |
| Home equity                                   | 301                    | 366               | 238                               | —                    | 10                               |
| Total   | \$9,936                | \$12,291          | \$10,977                          | \$—                  | \$324                            |
| Impaired loans with a valuation allowance:    |                        |                   |                                   |                      |                                  |
| Residential real estate                       | \$611                  | \$611             | \$859                             | \$5                  | \$32                             |
| Residential construction                      | —                      | —                 | —                                 | —                    | —                                |
| Commercial real estate                        | 809                    | 809               | 694                               | 65                   | 23                               |
| Commercial construction                       | —                      | —                 | —                                 | —                    | —                                |
| Commercial and industrial                     | —                      | —                 | 47                                | —                    | 1                                |
| Consumer                                      | —                      | —                 | —                                 | —                    | —                                |
| Home equity                                   | 47                     | 47                | 65                                | 3                    | 1                                |
| Total   | \$1,467                | \$1,467           | \$1,665                           | \$73                 | \$57                             |
| Total impaired loans:                         |                        |                   |                                   |                      |                                  |
| Residential real estate                       | \$4,106                | \$4,228           | \$3,493                           | \$5                  | \$137                            |
| Residential construction                      | —                      | —                 | —                                 | —                    | —                                |
| Commercial real estate                        | 3,509                  | 4,126             | 4,229                             | 65                   | 78                               |
| Commercial construction                       | 2,395                  | 3,934             | 3,270                             | —                    | 111                              |
| Commercial and industrial                     | 1,045                  | 1,057             | 1,347                             | —                    | 44                               |
| Consumer                                      | —                      | —                 | —                                 | —                    | —                                |
| Home equity                                   | 348                    | 413               | 303                               | 3                    | 11                               |
| Total   | \$11,403               | \$13,758          | \$12,642                          | \$73                 | \$381                            |

The \$11.4 million of impaired loans include \$11.2 million of non-accrual loans. The remaining impaired loans are TDRs or loans for which the Company believes, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement.

The Company does not have any commitments to lend additional funds to borrowers whose loans have been modified or are not performing.

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## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following table presents a summary of information pertaining to impaired loans by class as of December 31, 2013:

|   | Recorded<br>Investment | Unpaid<br>Balance | Average<br>Recorded<br>Investment | Related<br>Allowance | Interest<br>Income<br>Recognized |
|---|------------------------|-------------------|-----------------------------------|----------------------|----------------------------------|
|   | (In Thousands)         |                   |                                   |                      |                                  |
| Impaired loans without a valuation allowance: |                        |                   |                                   |                      |                                  |
| Residential real estate                       | \$ 1,535               | \$ 1,535          | \$ 1,455                          | \$—                  | \$ 52                            |
| Residential construction                      | —                      | —                 | —                                 | —                    | —                                |
| Commercial real estate                        | 4,099                  | 4,232             | 3,725                             | —                    | 192                              |
| Commercial construction                       | 3,888                  | 3,888             | 4,068                             | —                    | 193                              |
| Commercial and industrial                     | 1,254                  | 1,584             | 937                               | —                    | 44                               |
| Consumer                                      | —                      | —                 | —                                 | —                    | —                                |
| Home equity                                   | 131                    | 131               | 131                               | —                    | 4                                |
| Total   | \$ 10,907              | \$ 11,370         | \$ 10,316                         | \$—                  | \$ 485                           |
| Impaired loans with a valuation allowance:    |                        |                   |                                   |                      |                                  |
| Residential real estate                       | \$ 1,123               | \$ 1,123          | \$ 1,056                          | \$ 243               | \$ 30                            |
| Residential construction                      | —                      | —                 | 132                               | —                    | —                                |
| Commercial real estate                        | 249                    | 249               | 403                               | 12                   | 23                               |
| Commercial construction                       | —                      | —                 | —                                 | —                    | —                                |
| Commercial and industrial                     | 118                    | 118               | 134                               | 10                   | 3                                |
| Consumer                                      | —                      | —                 | —                                 | —                    | —                                |
| Home equity                                   | 162                    | 162               | 108                               | 14                   | 1                                |
| Total   | \$ 1,652               | \$ 1,652          | \$ 1,833                          | \$ 279               | \$ 57                            |
| Total impaired loans:                         |                        |                   |                                   |                      |                                  |
| Residential real estate                       | \$ 2,658               | \$ 2,658          | \$ 2,511                          | \$ 243               | \$ 82                            |
| Residential construction                      | —                      | —                 | 132                               | —                    | —                                |
| Commercial real estate                        | 4,348                  | 4,481             | 4,128                             | 12                   | 215                              |
| Commercial construction                       | 3,888                  | 3,888             | 4,068                             | —                    | 193                              |
| Commercial and industrial                     | 1,372                  | 1,702             | 1,071                             | 10                   | 47                               |
| Consumer                                      | —                      | —                 | —                                 | —                    | —                                |
| Home equity                                   | 293                    | 293               | 239                               | 14                   | 5                                |
| Total   | \$ 12,559              | \$ 13,022         | \$ 12,149                         | \$ 279               | \$ 542                           |

The \$12.6 million of impaired loans include \$6.8 million of non-accrual loans. The remaining impaired loans are TDRs or loans for which the Company believes, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement.

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## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following table presents a summary of information pertaining to impaired loans by class as of December 31, 2012:

|   | Recorded<br>Investment | Unpaid<br>Balance | Average<br>Recorded<br>Investment | Related<br>Allowance | Interest<br>Income<br>Recognized |
|---|------------------------|-------------------|-----------------------------------|----------------------|----------------------------------|
|   | (In Thousands)         |                   |                                   |                      |                                  |
| Impaired loans without a valuation allowance: |                        |                   |                                   |                      |                                  |
| Residential real estate                       | \$1,512                | \$1,512           | \$1,228                           | \$—                  | \$53                             |
| Residential construction                      | —                      | —                 | —                                 | —                    | —                                |
| Commercial real estate                        | 2,835                  | 3,225             | 3,410                             | —                    | 141                              |
| Commercial construction                       | 4,403                  | 4,403             | 2,691                             | —                    | 131                              |
| Commercial and industrial                     | 666                    | 891               | 723                               | —                    | 25                               |
| Consumer                                      | —                      | —                 | —                                 | —                    | —                                |
| Home equity                                   | 96                     | 96                | 217                               | —                    | 5                                |
| Total   | \$9,512                | \$10,127          | \$8,269                           | \$—                  | \$355                            |
| Impaired loans with a valuation allowance:    |                        |                   |                                   |                      |                                  |
| Residential real estate                       | \$1,142                | \$1,142           | \$722                             | \$183                | \$48                             |
| Residential construction                      | 331                    | 331               | 265                               | 31                   | —                                |
| Commercial real estate                        | 344                    | 344               | 422                               | 47                   | 20                               |
| Commercial construction                       | —                      | —                 | 43                                | —                    | —                                |
| Commercial and industrial                     | —                      | —                 | 623                               | —                    | —                                |
| Consumer                                      | —                      | —                 | —                                 | —                    | —                                |
| Home equity                                   | —                      | —                 | 34                                | —                    | —                                |
| Total   | \$1,817                | \$1,817           | \$2,109                           | \$261                | \$68                             |
| Total impaired loans:                         |                        |                   |                                   |                      |                                  |
| Residential real estate                       | \$2,654                | \$2,654           | \$1,950                           | \$183                | \$101                            |
| Residential construction                      | 331                    | 331               | 265                               | 31                   | —                                |
| Commercial real estate                        | 3,179                  | 3,569             | 3,832                             | 47                   | 161                              |
| Commercial construction                       | 4,403                  | 4,403             | 2,734                             | —                    | 131                              |
| Commercial and industrial                     | 666                    | 891               | 1,346                             | —                    | 25                               |
| Consumer                                      | —                      | —                 | —                                 | —                    | —                                |
| Home equity                                   | 96                     | 96                | 251                               | —                    | 5                                |
| Total   | \$11,329               | \$11,944          | \$10,378                          | \$261                | \$423                            |

The \$11.3 million of impaired loans include \$4.3 million of non-accrual loans. The remaining impaired loans are TDRs or loans for which the Company believes, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement.



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## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following table presents an aging analysis of past due and nonaccrual loans as of December 31, 2014:

|                              | 31-59 Days<br>Past Due | 60-89 Days<br>Past Due | 90 Days or<br>Greater<br>Past Due | Total<br>Past Due | Current   | Total<br>Loans | Nonaccrual<br>Loans |
|------------------------------|------------------------|------------------------|-----------------------------------|-------------------|-----------|----------------|---------------------|
| (In Thousands)               |                        |                        |                                   |                   |           |                |                     |
| Residential real estate      | \$3,396                | \$542                  | \$1,212                           | \$5,150           | \$113,542 | \$118,692      | \$4,308             |
| Residential construction     | —                      | —                      | —                                 | —                 | 8,129     | 8,129          | —                   |
| Commercial real estate       | 913                    | —                      | 2,385                             | 3,298             | 246,334   | 249,632        | 3,000               |
| Commercial construction      | 550                    | —                      | 1,558                             | 2,108             | 33,678    | 35,786         | 2,396               |
| Commercial and<br>industrial | 218                    | 434                    | 513                               | 1,165             | 73,166    | 74,331         | 1,196               |
| Consumer                     | 28                     | —                      | 13                                | 41                | 2,621     | 2,662          | 32                  |
| Home equity                  | 77                     | 30                     | 263                               | 370               | 34,138    | 34,508         | 261                 |
| Total                        | \$5,182                | \$1,006                | \$5,944                           | \$12,132          | \$511,608 | \$523,740      | \$11,193            |

The following table presents an aging analysis of past due and nonaccrual loans as of December 31, 2013:

|                              | 31-59 Days<br>Past Due | 60-89 Days<br>Past Due | 90 Days or<br>Greater<br>Past Due | Total<br>Past Due | Current   | Total<br>Loans | Nonaccrual<br>Loans |
|------------------------------|------------------------|------------------------|-----------------------------------|-------------------|-----------|----------------|---------------------|
| (In Thousands)               |                        |                        |                                   |                   |           |                |                     |
| Residential real estate      | \$2,962                | \$510                  | \$1,063                           | \$4,535           | \$107,989 | \$112,524      | \$2,415             |
| Residential construction     | —                      | —                      | —                                 | —                 | 6,130     | 6,130          | —                   |
| Commercial real estate       | 662                    | —                      | 2,802                             | 3,464             | 207,697   | 211,161        | 3,362               |
| Commercial construction      | —                      | —                      | —                                 | —                 | 38,441    | 38,441         | —                   |
| Commercial and<br>industrial | 264                    | 149                    | 816                               | 1,229             | 85,311    | 86,540         | 806                 |
| Consumer                     | 80                     | 2                      | 6                                 | 88                | 2,317     | 2,405          | 8                   |
| Home equity                  | 76                     | 8                      | 209                               | 293               | 31,798    | 32,091         | 243                 |
| Total                        | \$4,044                | \$669                  | \$4,896                           | \$9,609           | \$479,683 | \$489,292      | \$6,834             |

There were no loans greater than ninety days past due and still accruing at December 31, 2014 and 2013.

TDR loans consist of loans where the Company, for economic or legal reasons related to the borrower's financial difficulties, granted a concession to the borrower that the Company would not otherwise consider. TDR loans can take the form of a reduction in the stated interest rate, receipts of assets from a debtor in partial or full satisfaction of a loan, the extension of the maturity date, or the reduction of either the interest or principal. Once a loan has been identified as a TDR, it is classified as impaired and will continue to be reported as a TDR until the loan is paid in full.

In the normal course of business, the Company may modify a loan for a credit worthy borrower where the modified loan is not considered a TDR. In these cases, the modified terms are consistent with loan terms available to credit worthy borrowers and within normal loan pricing. The modifications to such loans are done according to existing underwriting standards which include review of historical financial statements, including current interim information if available, and an analysis of the borrower's performance and projections to assess repayment ability going forward.

During the year ended December 31, 2014, the Company granted four TDRs totaling \$4.7 million. Of the four TDRs granted in 2014, three totaling \$4.5 million had defaulted. During the year ended December 31, 2013 the Company had one TDR totaling \$201,000, that had defaulted and had been modified within the previous twelve month period. TDR loans are considered defaulted when based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement.

## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following tables provide new TDR activity by segment during the periods indicated:

| For the year ended December 31, 2014 | Number of<br>Modifications<br>(In Thousands) | Recorded<br>Investment<br>Pre-Modification | Recorded<br>Investment<br>Post-Modification | Current<br>Balance |
|--------------------------------------|--|--|---|--------------------|
| Residential real estate              | 2  | \$ 510                                     | \$ 510                                      | \$505              |
| Residential construction             | —  | —  | —   | —                  |
| Commercial real estate               | —  | —  | —   | —                  |
| Commercial construction              | —  | —  | —   | —                  |
| Commercial and industrial            | 2  | 4,225                                      | 2,687                                       | 2,108              |
| Consumer                             | —  | —  | —   | —                  |
| Home equity                          | —  | —  | —   | —                  |
| Total                                | 4  | \$ 4,735                                   | \$ 3,197                                    | \$2,613            |

| For the year ended December 31, 2013 | Number of<br>Modifications<br>(In Thousands) | Recorded<br>Investment<br>Pre-Modification | Recorded<br>Investment<br>Post-Modification | Current<br>Balance |
|--------------------------------------|--|--|---|--------------------|
| Residential real estate              | —  | \$ —                                       | \$ —  | \$—                |
| Residential construction             | —  | —  | —   | —                  |
| Commercial real estate               | 1  | 249  | 249   | 249                |
| Commercial construction              | —  | —  | —   | —                  |
| Commercial and industrial            | —  | —  | —   | —                  |
| Consumer                             | —  | —  | —   | —                  |
| Home equity                          | —  | —  | —   | —                  |
| Total                                | 1  | \$ 249                                     | \$ 249                                      | \$249              |

The following is a summary of TDR loans by segment as of the dates indicated:

|                           | As of December 31, 2014 |                        | As of December 31, 2013 |                        |
|---------------------------|-------------------------|------------------------|-------------------------|------------------------|
|                           | Number of<br>Loans      | Recorded<br>Investment | Number of<br>Loans      | Recorded<br>Investment |
|                           | (In Thousands)          |                        |                         |                        |
| Residential real estate   | 4                       | \$865                  | \$2                     | \$364                  |
| Residential construction  | —                       | —                      | —                       | —                      |
| Commercial real estate    | 4                       | \$575                  | 4                       | 620                    |
| Commercial construction   | 2                       | 2,108                  | —                       | —                      |
| Commercial and industrial | 4                       | \$141                  | 4                       | 155                    |
| Consumer                  | —                       | —                      | —                       | —                      |
| Home equity               | 1                       | 33                     | 1                       | 34                     |
| Total                     | 15                      | \$3,722                | \$11                    | \$1,173                |

TDRs granted in 2014 and 2013 were primarily the result of concessions to reduce the interest rate or extension of the maturity date. The TDRs granted during 2014 resulted in a \$1.5 million reduction of the recorded investment. One of the four modifications

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## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

granted in 2014 was in compliance with modified terms. The TDRs granted during 2013 did not result in a reduction of the recorded investment.

The Company reviews TDRs on a loan by loan basis and applies specific reserves to loan balances. The reserve balance is typically calculated using the present value of future cash flows or using the fair value of the collateral method if sufficient borrower cash flow cannot be identified. There were no specific reserves related to TDRs that were granted for the year ended December 31, 2014.

## 5. LOAN SERVICING

Mortgage loans serviced for others are not included in the accompanying consolidated balance sheets. The unpaid principal balances of mortgage loans serviced for others were \$91.3 million and \$97.6 million at December 31, 2014 and 2013, respectively. The risks inherent in the mortgage servicing assets relate primarily to changes in prepayments that result from changes in mortgage interest rates. Capitalized mortgage servicing rights were \$39,000, \$194,000, and \$187,000 for the years ended December 31, 2014, 2013 and 2012, respectively. The balance of capitalized servicing rights, net of valuation allowances, at December 31, 2014, 2013 and 2012, was \$269,000, \$381,000 and \$368,000, respectively. At December 31, 2014, 2013 and 2012, the fair value of these rights was \$622,000, \$831,000 and \$444,000, respectively. At December 31, 2014, 2013 and 2012, the valuation allowance was \$2,000, \$0, and \$32,000, respectively.

Residential real estate mortgages are originated by the Company both for its portfolio and for sale into the secondary market. The Company may sell its loans to institutional investors such as the Federal Home Loan Mortgage Corporation. Under loan sale and servicing agreements with the investor, the Company generally continues to service the residential real estate mortgages. The Company pays the investor an agreed-upon rate on the loan, which is less than the interest rate received from the borrower. The Company retains the difference as a fee for servicing the residential real estate mortgages. The Company capitalizes mortgage servicing rights at their fair value upon sale of the related loans, amortizes the asset over the estimated life of the serviced loan, and periodically assesses the asset for impairment. The significant assumptions used by a third party to estimate the fair value of capitalized servicing rights at December 31, 2014, include weighted average prepayment speed for the portfolio using the Public Securities Association Standard Prepayment Model (203 PSA), weighted average discount rate (8.12%), weighted average servicing fee (0.2504)%, and net cost to service loans (\$43.23 per loan). The estimated fair value of capitalized servicing rights may vary significantly in subsequent periods primarily due to changing market interest rates, and their effect on prepayment speeds and discount rates.

A summary of the activity in the balances of mortgage servicing rights follows:

|                                       | Years Ended December 31, |        |        |
|---------------------------------------|--------------------------|--------|--------|
|                                       | 2014                     | 2013   | 2012   |
|                                       | (In Thousands)           |        |        |
| Balance at the beginning of year:     | \$381                    | \$368  | \$344  |
| Capitalized mortgage servicing rights | 39                       | 194    | 187    |
| Change in valuation allowance         | (2                       | ) 32   | 20     |
| Amortization                          | (149                     | ) (213 | ) (183 |
| Balance at the end of year            | \$269                    | \$381  | \$368  |

## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## 6. PREMISES AND EQUIPMENT

A summary of the cost and accumulated depreciation of premises and equipment is as follows:

|                             | December 31,   |          |
|-----------------------------|----------------|----------|
|                             | 2014           | 2013     |
|                             | (In Thousands) |          |
| Land                        | \$1,529        | \$1,529  |
| Buildings                   | 9,845          | 9,823    |
| Leasehold improvements      | 1,461          | 1,461    |
| Furniture and equipment     | 6,281          | 6,064    |
| Total cost                  | 19,116         | 18,877   |
| Accumulated depreciation    | (10,261        | ) (9,696 |
| Premises and equipment, net | \$8,855        | \$9,181  |

Depreciation expense related to premises and equipment for the years ended December 31, 2014, 2013 and 2012 amounted to \$701,000, \$717,000 and \$714,000, respectively.

## 7. DEPOSITS

A summary of deposit balances by type is as follows:

|  | December 31,   |           |
|--|----------------|-----------|
|  | 2014           | 2013      |
|  | (In Thousands) |           |
| Demand deposits                          | \$97,922       | \$90,869  |
| NOW accounts                             | 42,177         | 40,774    |
| Savings accounts                         | 50,716         | 49,755    |
| Money market deposit accounts            | 121,106        | 111,126   |
| Total core accounts                      | 311,921        | 292,524   |
| Certificate accounts less than \$100,000 | 83,424         | 79,829    |
| Certificate accounts \$100,000 or more   | 88,213         | 77,413    |
| Total certificate of deposit accounts    | 171,637        | 157,242   |
| Total deposits                           | \$483,558      | \$449,766 |

A summary of certificate accounts by maturity is as follows:

|      | December 31, 2014 |                             | December 31, 2013 |                             |   |
|------|-------------------|-----------------------------|-------------------|-----------------------------|---|
|      | (In Thousands)    |                             |                   |                             |   |
|      | Amount            | Weighted<br>Average<br>Rate | Amount            | Weighted<br>Average<br>Rate |   |
| 2014 | \$—               | —                           | \$92,172          | 1.29                        | % |
| 2015 | 104,030           | 1.21                        | % 29,626          | 2.13                        | % |
| 2016 | 34,509            | 1.42                        | % 19,357          | 1.75                        | % |
| 2017 | 12,282            | 1.30                        | % 5,772           | 1.31                        | % |
| 2018 | 13,988            | 1.30                        | % 10,315          | 1.16                        | % |
| 2019 | 6,828             | 1.10                        | % —               | —                           |   |

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|       |           |      |   |           |      |   |
|-------|-----------|------|---|-----------|------|---|
| Total | \$171,637 | 1.26 | % | \$157,242 | 1.49 | % |
|-------|-----------|------|---|-----------|------|---|

Certificate accounts issued in amounts that meet or exceed the FDIC insurance limit of \$250,000 totaled \$53.1 million and \$46.5 million at December 31, 2014 and 2013, respectively.

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## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## 8. SECURITIES SOLD UNDER AGREEMENTS TO REPURCHASE

Securities sold under agreements to repurchase (“repurchase agreements”) are funds borrowed from customers on an overnight basis that are secured by securities and are summarized as follows:

|  | Years Ended December 31, |        |   |
|--|--------------------------|--------|---|
|  | 2014                     | 2013   |   |
|  | (In Thousands)           |        |   |
| Balance at end of year                                 | \$—                      | \$—    |   |
| Average amount outstanding during the year             | —                        | 7,243  |   |
| Interest expense incurred during the year              | —                        | 9      |   |
| Maximum amount outstanding at any month-end            | —                        | 15,312 |   |
| Weighted average interest rate during the year         | —                        | % 0.12 | % |
| Weighted average interest rate on end of year balances | —                        | % —    | % |

Repurchase agreements are no longer being offered by the Company as of October 1, 2013. The corresponding customer balances were transferred to demand deposit accounts.

## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## 9. ADVANCES FROM FEDERAL HOME LOAN BANK

Advances from the FHLB consist of the following:

|                                    |     | December 31, 2014 |                             | December 31, 2013 |                             |   |
|------------------------------------|-----|-------------------|-----------------------------|-------------------|-----------------------------|---|
|                                    |     | Amount            | Weighted<br>Average<br>Rate | Amount            | Weighted<br>Average<br>Rate |   |
|                                    |     | (In Thousands)    |                             |                   |                             |   |
| Fixed-rate FHLB advances maturing: |     |                   |                             |                   |                             |   |
| Due 2014                           | (a) | \$—               | —                           | % \$3,802         | 2.20                        | % |
| Due 2015                           | (a) | 16,891            | 0.59                        | % 9,001           | 1.47                        | % |
| Due 2016                           | (a) | 16,585            | 1.03                        | % 6,317           | 1.75                        | % |
| Due 2017                           | (a) | 6,217             | 2.01                        | % 5,872           | 2.19                        | % |
| Due 2018                           |     | 6,500             | 3.25                        | % 5,000           | 3.69                        | % |
| Due 2019                           | (a) | 13,274            | 1.52                        | % 9,000           | 1.33                        | % |
| Due 2020                           | (a) | 2,561             | 1.68                        | % 3,000           | 1.68                        | % |
| Due 2021                           | (a) | 4,047             | 2.01                        | % 3,000           | 2.00                        | % |
| Due 2024                           | (a) | 964               | 2.64                        | % —               | —                           | % |
| Total FHLB advances                |     | \$67,039          | 1.43                        | % \$44,992        | 1.93                        | % |

(a) Includes amortizing advances requiring monthly principal and interest payments.

FHLB advances are secured primarily by a blanket lien on qualified one- to four-family residential real estate, certain pledged commercial real estate loans and the Company's holding of FHLB stock. At December 31, 2014 and 2013, the Company was in compliance with the FHLB collateral requirements. At December 31, 2014, the Company pledged \$214.0 million of collateral to the FHLB.

At December 31, 2014, the Company had the ability to borrow an additional \$65.4 million based on the collateral pledged to the FHLB. In addition, the Company is able to pledge additional collateral to increase the advance availability with the FHLB.

The Company utilizes advances from the FHLB primarily in connection with funding growth in the balance sheet and to manage interest rate risk. At December 31, 2014, all of the Company's outstanding FHLB advances were at fixed interest rates ranging from 0.24% to 3.69%. At December 31, 2013, all of the Company's outstanding FHLB advances were at fixed interest rates ranging from 0.72% to 3.69%.

At December 31, 2014, the Company had an Ideal Way Line of Credit available with the FHLB of \$2.0 million and an unsecured line of credit of \$4.0 million with Banker's Bank Northeast. In addition, the Company's unused borrowing capacity with the Federal Reserve Bank of Boston was \$44.5 million at December 31, 2014. At December 31, 2014, there were no amounts outstanding under these lines of credit.

## 10. INCOME TAXES

Allocation of federal and state income taxes between current and deferred portions is as follows:

Years Ended December 31,

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|                                      | 2014           | 2013    | 2012   |
|--------------------------------------|----------------|---------|--------|
|                                      | (In Thousands) |         |        |
| Current tax (benefit) expense        |                |         |        |
| Federal                              | \$(440)        | ) \$367 | \$726  |
| State                                | (36)           | ) 124   | 230    |
| Total current tax (benefit) expense  | (476)          | ) 491   | 956    |
| Deferred tax (benefit) expense       |                |         |        |
| Federal                              | (548)          | ) 160   | (275)  |
| State                                | (27)           | ) 49    | (80)   |
| Total deferred tax (benefit) expense | (575)          | ) 209   | (355)  |
| Change in valuation reserve          | (54)           | ) (13)  | ) (20) |
|                                      | (629)          | ) 196   | (375)  |
| Income tax (benefit) expense         | \$(1,105)      | ) \$687 | \$581  |

The reasons for the differences between the statutory federal income tax rate and the effective tax rates are summarized as follows:

|   | Years Ended December 31, |    |        |    |        |    |
|---|--------------------------|----|--------|----|--------|----|
|   | 2014                     |    | 2013   |    | 2012   |    |
| Statutory rate                          | 34.0                     | %  | 34.0   | %  | 34.0   | %  |
| Increase (decrease) resulting from:     |                          |    |        |    |        |    |
| State taxes, net of federal tax benefit | 2.5                      | %  | 3.5    | %  | 3.2    | %  |
| Dividends received deduction            | 0.2                      | %  | (0.2)  | )% | (0.2)  | )% |
| Change in valuation allowance           | 3.2                      | %  | (0.4)  | )% | (0.7)  | )% |
| Tax-exempt interest                     | 29.6                     | %  | (16.1) | )% | (16.7) | )% |
| Bank owned life insurance               | 7.2                      | %  | (3.8)  | )% | (4.2)  | )% |
| Stock-based compensation                | (6.1)                    | )% | 3.4    | %  | 2.9    | %  |
| Expiration of contribution carryover    | (2.8)                    | )% | —      | %  | —      | %  |
| Other, net                              | (2.1)                    | )% | 0.8    | %  | 0.8    | %  |
| Effective tax rate                      | 65.7                     | %  | 21.2   | %  | 19.1   | %  |

## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The tax effects of each type of income and expense item that gave rise to deferred taxes are as follows:

|   | December 31,   |         |
|---|----------------|---------|
|   | 2014           | 2013    |
|   | (In Thousands) |         |
| Gross deferred tax assets:                          |                |         |
| Charitable contribution carryforward                | \$4            | \$—     |
| Capital loss carryforward                           | —              | 54      |
| Allowance for loan losses                           | 1,968          | 1,835   |
| Employee benefit and stock-based compensation plans | 904            | 912     |
| Nonaccrual interest                                 | 186            | 108     |
| OREO  | 67             | 161     |
| Alternative minimum tax credit                      | 940            | 540     |
| Net operating loss carryforward                     | 112            | —       |
| Other   | 115            | 139     |
| Gross deferred tax assets                           | 4,296          | 3,749   |
| Gross deferred tax liabilities                      |                |         |
| Deferred loan costs                                 | (357           | ) (369  |
| Mortgage servicing rights                           | (104           | ) (151  |
| Depreciation  | (136           | ) (105  |
| Unrealized gain on available-for-sale securities    | (16            | ) (28   |
| Gross deferred tax liabilities                      | (613           | ) (653  |
| Net deferred tax asset                              | 3,683          | 3,096   |
| Valuation allowance                                 | —              | (54     |
| Net deferred tax asset                              | \$3,683        | \$3,042 |

The change in the valuation reserve applicable to the net deferred tax asset is as follows:

|   | Years Ended December 31, |       |       |
|---|--------------------------|-------|-------|
|   | 2014                     | 2013  | 2012  |
|   | (In Thousands)           |       |       |
| Balance at beginning of year:                 | \$54                     | \$67  | \$87  |
| Change generated by current year's operations | (54                      | ) (13 | ) (20 |
| Balance at end of year                        | \$—                      | \$54  | \$67  |

The federal income tax reserve for loan losses at the Bank's base year is \$3.9 million. If any portion of the reserve is used for purposes other than to absorb loan losses, approximately 150% of the amount actually used, limited to the amount of the reserve, would be subject to taxation in the fiscal year in which used. As the Bank intends to use the reserve solely to absorb loan losses, a deferred tax liability of approximately \$1.4 million has not been provided.

The Company's income tax returns for the years ended December 31, 2011, 2012, 2013 and 2014 are open to audit under the statute of limitations by the Internal Revenue Service. The Company's policy is to record interest and penalties related to uncertain tax positions as part of its income tax expense. The Company has no penalties and interest recorded for the years ended December 31, 2014, 2013 and 2012.



## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## 11. OFF-BALANCE-SHEET ACTIVITIES

## Credit-related financial instruments

The Company 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, standby letters of credit, and various financial instruments with off-balance-sheet risk. Such commitments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the consolidated balance sheets.

The Company's exposure to credit loss is represented by the contractual amount of these commitments. The Company follows the same credit policies in making commitments as it does for on-balance-sheet instruments.

The following financial instruments were outstanding whose contract amounts represent credit risk:

|   | December 31,   |          |
|---|----------------|----------|
|   | 2014           | 2013     |
|   | (In Thousands) |          |
| Commitments to grant loans                  | \$35,418       | \$17,904 |
| Unfunded commitments for construction loans | 17,210         | 29,339   |
| Unfunded commitments under lines of credit  | 79,092         | 79,306   |
| Standby letters of credit                   | 904            | 1,311    |

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. The commitments for equity lines of credit may expire without being drawn upon. Therefore, the total commitment amounts do not necessarily represent future cash requirements. The amount of collateral obtained, if it is deemed necessary by the Company, is based on management's credit evaluation of the customer. Collateral held varies but may include cash, securities, accounts receivable, inventory, property, plant and equipment, and real estate.

Unfunded commitments under commercial lines of credit, revolving credit lines and overdraft protection agreements are commitments for possible future extensions of credit to existing customers. These lines of credit are uncollateralized, usually do not contain a specified maturity date, and may not be drawn upon to the total extent to which the Company is committed.

Disclosures and liability recognition are required for the fair value of certain guarantees at issuance. The Company does not issue any guarantees that would require liability recognition or disclosure, other than its standby letters of credit. The Company has issued conditional commitments in the form of standby letters of credit to guarantee payment on behalf of a customer and guarantee the performance of a customer to a third party. Standby letters of credit generally arise in connection with lending relationships. The credit risk involved in issuing these instruments is essentially the same as that involved in extending loans to customers. Contingent obligations under standby letters of credit totaled \$904,000 and \$1.3 million at December 31, 2014 and 2013, respectively and represent the maximum potential future payments the Company could be required to make. Typically, these instruments have terms of 12 months or less and expire unused; therefore, the total amounts do not necessarily represent future cash requirements. Each customer is evaluated individually for creditworthiness under the same underwriting standards used for commitments to extend credit and on-balance sheet instruments. The Company's policies governing loan collateral

apply to standby letters of credit at the time of credit extension. Loan-to-value ratios are generally consistent with loan-to-value requirements for other commercial loans secured by similar types of collateral. The fair value of the Company's standby letters of credit at December 31, 2014 and 2013 was not material.

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## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## Lease commitments

Pursuant to the terms of non-cancelable lease agreements in effect at December 31, 2014, future minimum operating lease commitments pertaining to banking premises are as follows:

|            | (In Thousands) |
|------------|----------------|
| 2015       | \$476          |
| 2016       | 470            |
| 2017       | 461            |
| 2018       | 420            |
| 2019       | 441            |
| Thereafter | 2,746          |
| Total      | \$5,014        |

The leases contain options to extend for periods from one to five years. Total rent expense, including common area charges, for the years ended December 31, 2014, 2013 and 2012 approximated \$527,000, \$496,000, and \$484,000, respectively.

## 12. OTHER COMMITMENTS AND CONTINGENCIES

## Employment and change in control agreements

Chicopee Bancorp, Inc. has three-year employment agreements with its President and Chief Executive Officer and Executive Vice President of Lending and three-year change of control agreements with certain other executives. These agreements generally provide for a base salary and the continuation of certain benefits currently received. The Company employment agreements renew on a daily and annual basis, respectively. Under certain specified circumstances, the employment agreements require certain payments to be made for certain reasons other than cause, including a "change in control" as defined in the agreement. However, such employment may be terminated for cause, as defined, without incurring any continuing obligations.

## Legal claims

Various legal claims arise from time to time in the ordinary course of business. In the opinion of management, the claims that existed at December 31, 2014 will have no material effect on the Company's consolidated financial statements.

## 13. MINIMUM REGULATORY CAPITAL REQUIREMENTS

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



Quantitative measures established by regulation to ensure capital adequacy require the Company to maintain minimum amounts and ratios (set forth in the following table) of total and Tier 1 capital (as defined in the regulations) to risk-weighted assets (as defined) and of Tier 1 capital (as defined) to average assets (as defined). Management believes, as of December 31, 2014 and 2013, that the Company and its bank subsidiary met all capital adequacy requirements to which they are subject.

As of December 31, 2014, the most recent notification from the Federal Deposit Insurance Corporation categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, an institution must maintain minimum total risk-based, Tier 1 risk-based and Tier 1 leverage ratios as set forth in the following tables. There are no conditions or events since the notification that management believes have changed the Bank's category. Prompt corrective action provisions are not applicable to the Company.

## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The Company's and Bank's actual capital amounts and ratios as of December 31, 2014 and 2013 are presented below.

|   | Actual<br>Amount | Ratio |   | Minimum for Capital<br>Adequacy Purposes<br>Amount | Ratio | Minimum<br>to be Well<br>Capitalized Under<br>Prompt Corrective<br>Action Provisions<br>Amount | Ratio    |        |
|---|------------------|-------|---|--|-------|--|----------|--------|
| (Dollars In Thousands)                  |                  |       |   |  |       |  |          |        |
| As of December 31, 2014:                |                  |       |   |  |       |  |          |        |
| Total Capital to Risk Weighted Assets:  |                  |       |   |  |       |  |          |        |
| Company                                 | \$91,331         | 17.5  | % | \$41,808   | 8.0   | %  | N/A      | N/A    |
| Bank                                    | \$78,337         | 15.0  | % | \$41,677   | 8.0   | %  | \$52,096 | 10.0 % |
| Tier 1 Capital to Risk Weighted Assets: |                  |       |   |  |       |  |          |        |
| Company                                 | \$86,384         | 16.5  | % | \$20,904   | 4.0   | %  | N/A      | N/A    |
| Bank                                    | \$73,390         | 14.1  | % | \$20,838   | 4.0   | %  | \$31,257 | 6.0 %  |
| Tier 1 Capital to Average Assets:       |                  |       |   |  |       |  |          |        |
| Company                                 | \$86,384         | 13.8  | % | \$24,956   | 4.0   | %  | N/A      | N/A    |
| Bank                                    | \$73,390         | 11.8  | % | \$24,871   | 4.0   | %  | \$31,088 | 5.0 %  |
| As of December 31, 2013:                |                  |       |   |  |       |  |          |        |
| Total Capital to Risk Weighted Assets:  |                  |       |   |  |       |  |          |        |
| Company                                 | \$96,446         | 19.6  | % | \$39,424   | 8.0   | %  | N/A      | N/A    |
| Bank                                    | \$85,931         | 17.5  | % | \$39,339   | 8.0   | %  | \$49,173 | 10.0 % |
| Tier 1 Capital to Risk Weighted Assets: |                  |       |   |  |       |  |          |        |
| Company                                 | \$91,814         | 18.6  | % | \$19,712   | 4.0   | %  | N/A      | N/A    |
| Bank                                    | \$81,299         | 16.5  | % | \$19,669   | 4.0   | %  | \$29,504 | 6.0 %  |
| Tier 1 Capital to Average Assets:       |                  |       |   |  |       |  |          |        |
| Company                                 | \$91,814         | 15.8  | % | \$23,210   | 4.0   | %  | N/A      | N/A    |
| Bank                                    | \$81,299         | 14.0  | % | \$23,172   | 4.0   | %  | \$28,965 | 5.0 %  |

In July 2013, the Federal Deposit Insurance Corporation and the other federal bank regulatory agencies issued a final rule that will revise their leverage and risk-based capital requirements and the method for calculating risk-weighted assets to make them consistent with agreements that were reached by the Basel Committee on Banking Supervision and certain provisions of the Dodd-Frank Act. Among other things, the rule establishes a new common equity Tier 1 minimum capital requirement (4.5% of risk-weighted assets), increases the minimum Tier 1 capital to risk-based assets requirement (from 4% to 6% of risk-weighted assets) and assigns a higher risk weight (150%) to exposures that are more than 90 days past due or are on nonaccrual status and to certain commercial real estate facilities that finance the acquisition, development or construction of real property. The final rule also requires unrealized gains and losses on certain "available-for-sale" securities holdings to be included for purposes of calculating regulatory capital unless a one-time opt-out is exercised. The rule limits a banking organization's capital distributions and certain discretionary bonus payments if the banking organization does not hold a "capital conservation buffer" consisting of 2.5% of common equity Tier 1 capital to risk-weighted assets in addition to the amount necessary to meet its minimum risk-based

capital requirements. The final rule becomes effective for the Company and the Bank on January 1, 2015. The capital conservation buffer requirement will be phased in beginning January 1, 2016 and ending January 1, 2019, when the full capital conservation buffer requirement will be effective.

## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following is a reconciliation of the Company's stockholders' equity as disclosed in the consolidated balance sheets under GAAP to regulatory capital as disclosed in the table above.

|   | December 31,   |          |
|---|----------------|----------|
|   | 2014           | 2013     |
|   | (In Thousands) |          |
| Total equity determined under GAAP                                  | \$88,134       | \$92,230 |
| Net unrealized gain on available-for-sale securities, net of tax    | (29)           | (52)     |
| Disallowed mortgage servicing rights                                | (27)           | (38)     |
| Disallowed deferred tax assets                                      | (1,694)        | (326)    |
| Tier 1 Capital  | 86,384         | 91,814   |
| Allowable allowance for loan losses                                 | 4,927          | 4,596    |
| Unrealized gain on available-for-sale equity securities, net of tax | 20             | 36       |
| Total regulatory capital  | \$91,331       | \$96,446 |

## 14. COMMON STOCK REPURCHASE PROGRAM

On June 1, 2012, the Company announced that the Board of Directors authorized the Seventh Stock Repurchase Program for the purchase of up to 272,000 shares, or approximately 5% of the Company's outstanding common stock. As of December 31, 2014, under the Seventh Stock Repurchase Program, the Company has purchased 211,269 shares at an average price per share of \$16.21. As of December 31, 2014, the Company repurchased a total of 2.2 million shares of common stock at a total cost of \$29.4 million, or an average price per share of \$13.49.

The following table summarizes the Stock Repurchase plans as of the dates indicated:

| Repurchase Plan | Approval Date      | Completion Date   | No. of Shares Approved | No. of Shares Purchased | Average Price per Share | Total Cost of the Plan |
|-----------------|--------------------|-------------------|------------------------|-------------------------|-------------------------|------------------------|
| Initial Plan    | August 16, 2007    | March 3, 2008     | 371,968                | 371,968                 | \$13.21                 | \$4.9 million          |
| Second Plan     | March 4, 2008      | August 8, 2008    | 353,370                | 353,370                 | \$13.26                 | \$4.7 million          |
| Third Plan      | August 8, 2008     | November 25, 2009 | 335,000                | 335,000                 | \$12.98                 | \$4.3 million          |
| Fourth Plan     | February 26, 2010  | November 23, 2010 | 318,952                | 318,952                 | \$11.75                 | \$3.7 million          |
| Fifth Plan      | November 19, 2010  | November 3, 2011  | 303,004                | 303,004                 | \$13.84                 | \$4.2 million          |
| Sixth Plan      | September 30, 2011 | October 11, 2012  | 287,000                | 287,000                 | \$14.26                 | \$4.1 million          |
| Seventh Plan    | June 1, 2012       | —                 | 272,000                | 211,269                 | \$16.21                 | \$3.4 million          |

## 15. EMPLOYEE BENEFIT PLANS

The Company provides a 401(k) defined contribution plan (the "Plan") for eligible employees. Each employee reaching the age of 21 and one year of service automatically becomes a participant in the Plan. Employees may defer from 1%-75% of compensation subject to current federal tax laws. For participating employees, the Company makes matching contributions equal to 50% of a participant's contribution up to 2% of compensation. The Company also provides a guaranteed non-elective 3% Safe Harbor contribution to all eligible employees. The Company's total expense under the Plan for the years ended December 31, 2014, 2013 and 2012 amounted to \$302,000, \$284,000 and \$259,000, respectively. The Company provides supplemental life insurance benefits to key officers. Amounts charged to expense for these benefits were \$59,000, \$55,000 and \$233,000 for the years ended December 31, 2014, 2013 and 2012, respectively.

16. EMPLOYEE STOCK OWNERSHIP PLAN

The Company has established an ESOP for the benefit of each employee that has reached the age of 21 and has completed at least 1,000 hours of service in the previous twelve-month period. As part of the Bank's conversion from mutual to stock ownership, the Company invested in a subsidiary, Chicopee Funding Corporation. During 2007, Chicopee Funding Corporation used the proceeds from the investment to fund a loan to the Chicopee Savings Bank Employee Stock Ownership Plan Trust (the "Trust"), which used the proceeds from the loan to purchase 8%, or 595,149 shares, of the Company's outstanding stock as part of the

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## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

conversion from mutual to stock. The loan bears interest equal to 8.25% and provides for annual payments of principal and interest. Under the ESOP's change in control provision, the Trust would be instructed to use proceeds from the sale of stock to pay off the outstanding ESOP loan balance and to distribute the remaining plan assets to current participants.

At December 31, 2014, the remaining principal balance is payable as follows:

Years Ending  
December 31,  
(In Thousands)

|            |         |
|------------|---------|
| 2015       | \$247   |
| 2016       | 268     |
| 2017       | 290     |
| 2018       | 314     |
| 2019       | 340     |
| Thereafter | 2,714   |
| Total      | \$4,173 |

The Company has committed to make contributions to the ESOP sufficient to support the debt service of the loan. The loan is secured by the shares purchased by the Trust, which are held in a suspense account for allocation among the participants as the loan is paid. Shares released are allocated to each eligible participant based on the ratio of each participant's compensation, as defined in the ESOP, to the total compensation of all eligible plan participants. Total compensation expense applicable to the ESOP amounted to \$491,000, \$509,000, and \$430,000 for the years ended December 31, 2014, 2013, and 2012, respectively.

Shares held by the ESOP include the following:

|                                      | December 31,<br>2014 | 2013    | 2012    |
|--------------------------------------|----------------------|---------|---------|
| Number of shares:                    |                      |         |         |
| Allocated                            | 221,841              | 201,566 | 181,107 |
| Unallocated                          | 327,333              | 357,090 | 386,847 |
| Total                                | 549,174              | 558,656 | 567,954 |
| Fair value of shares (In Thousands): |                      |         |         |
| Allocated                            | \$3,700              | \$3,500 | \$2,900 |
| Unallocated                          | 5,500                | 6,200   | 6,100   |
| Total                                | \$9,200              | \$9,700 | \$9,000 |

## 17. EQUITY INCENTIVE PLAN

## Stock Options

Under the Company's 2007 Equity Incentive Plan ("the Plan"), approved by the Company's stockholders at the annual meeting of the Company stockholders on May 30, 2007, the Company may grant options to directors, officers and employees for up to 743,936 shares of common stock. Both incentive stock options and non-qualified stock options may be granted under the Plan. The exercise price for each option is equal to the market price of the Company's stock

on the date of grant and the maximum term of each option is ten years. The stock options vest over five years in five equal installments on each anniversary of the date of grant.

The Company recognizes compensation expense over the vesting period, based on the grant-date fair value of the options granted. The fair value of each option granted is estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions for options granted during the year ended December 31, 2013.

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## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

|                         |                         |   |
|-------------------------|-------------------------|---|
|                         | Year Ended December 31, |   |
|                         | 2013                    |   |
| Expected dividend yield | 1.39                    | % |
| Expected term           | 6.5 years               |   |
| Expected volatility     | 24.06                   | % |
| Risk-free interest rate | 1.25                    | % |

There were no stock options granted during the year ended December 31, 2014.

The expected volatility is based on historical volatility of the Company's stock and other factors. The risk-free interest rate for the periods within the contractual life of the options is based on the U.S. Treasury yield curve in effect at the time of grant. The expected life of 6.5 years is based on the simplified method calculations allowed for "plain-vanilla" share options granted. The dividend yield assumption is based on the Company's expectation of dividend payouts. A summary of options under the Plan as of December 31, 2014, and changes during the year then ended is as follows:

|                                  | Shares  | Weighted<br>Average<br>Exercise Price | Weighted<br>Average<br>Remaining<br>Contractual<br>Term<br>(in years) | Aggregate<br>Intrinsic<br>Value (000's) |
|----------------------------------|---------|---------------------------------------|---|---|
| Outstanding at December 31, 2012 | 595,198 | \$14.24                               | 5.15  | \$983                                   |
| Outstanding at December 31, 2013 | 668,598 | 14.58                                 | 4.86  | \$1,894                                 |
| Exercised                        | (9,700) | ) 14.51                               | 3.69  | —                                       |
| Forfeited or expired             | (5,800) | ) 15.82                               | 7.76  | —                                       |
| Outstanding at December 31, 2014 | 653,098 | \$14.57                               | 3.83  | \$1,425                                 |
| Exercisable at December 31, 2014 | 541,497 | \$14.33                               | 3.03  | \$1,313                                 |
| Exercisable at December 31, 2013 | 515,698 | \$14.26                               | 3.74  | \$1,627                                 |
| Exercisable at December 31, 2012 | 519,998 | \$14.26                               | 4.62  | \$846                                   |

The weighted-average grant-date fair value of options granted during 2013 was \$3.59. The weighted average grant-date fair value of the options outstanding and exercisable at December 31, 2014 was \$3.81 and \$3.87, respectively. For the years ended December 31, 2014, 2013 and 2012 share based compensation expense applicable to options granted under the Plan was \$121,000, \$118,000 and \$278,000 respectively. During the year ended December 31, 2014, 1,200 stock options with an exercise price of \$14.21 per share, 1,000 stock options with an exercise price of \$16.55, and 7,500 stock options with an exercise price of \$14.29 per share were exercised. As of December 31, 2014, unrecognized stock-based compensation expense related to non-vested options amounted to \$284,000. This amount is expected to be recognized over a period of 2.64 years.

#### Stock Awards

Under the Plan, the Company may grant stock awards to its directors, officers and employees for up to 297,574 shares of common stock. The stock awards vest 20% per year beginning on the first anniversary of the date of grant. The fair market value of the stock awards, based on the market price at the date of grant, is recorded as unearned compensation. Unearned compensation is amortized over the applicable vesting period. The weighted-average grant-date fair value of all stock awards as of December 31, 2014 is \$14.08. The Company recorded compensation cost related to stock awards of approximately \$5,000 for the year ended December 31, 2014, \$6,000 for the year ended



December 31, 2013, and \$496,000 for the year ended December 31, 2012. There were no stock awards granted prior to July 1, 2007. There were no stock awards granted by the Company during the year ended December 31, 2014. Stock awards with a fair value of \$7,000, \$7,000 and \$854,000 have vested during the years ended December 31, 2014, 2013 and 2012, respectively. As of December 31, 2014, unrecognized stock-based compensation expense related to non-vested restricted stock awards of \$7,000 is expected to be recognized over a period of 1.19 years.

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## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

A summary of the status of the Company's stock awards as of December 31, 2014, and changes during the year then ended is as follows:

|                                   | Shares | Weighted<br>Average<br>Grant-Date<br>Fair Value |
|-----------------------------------|--------|---|
| Nonvested Shares                  |        |   |
| Outstanding at December 31, 2013: | 1,200  | \$14.08   |
| Vested                            | 400    | 14.08   |
| Outstanding at December 31, 2014  | 800    | \$14.08   |

## 18. LONG-TERM INCENTIVE PLAN

On March 13, 2012, the Company adopted the Chicopee Bancorp, Inc. 2012 Phantom Stock Unit Award and Long-Term Incentive Plan (the "Plan"), effective January 1, 2012. The Plan was established to promote the long-term financial success of the Company and its subsidiaries by providing a means to attract, retain and reward individuals who contribute to such success and to further align their interest with those of the Company's stockholders.

A total of 150,000 phantom stock units will be available for awards under the Plan. The only awards that may be granted under the Plan are Phantom Stock Units. A Phantom Stock Unit represents the right to receive a cash payment on the determination date equal to the book value of a share of the Company's stock on the determination date. The settlement of a Phantom Stock Unit on the determination date shall be in cash. The Plan year shall be January 1 to December 31. Unless the Compensation Committee of the Board of Directors of the Company determines otherwise, the required period of service for full vesting will be three years. The Company's total expense under the Plan for the years ended December 31, 2014, 2013 and 2012 was \$44,000, \$39,000 and \$0, respectively. During the years ended December 31, 2014 and 2013, 2,942 and 4,074 phantom stock units were granted, respectively.

## 19. RELATED PARTY TRANSACTIONS

In the ordinary course of business, the Company has granted loans to officers, directors and their affiliates. An analysis of the activity of these loans is as follows:

|                                | Years Ended<br>December 31, |         |
|--------------------------------|-----------------------------|---------|
|                                | 2014                        | 2013    |
|                                | (In Thousands)              |         |
| Balance at beginning of year:  | \$1,108                     | \$1,210 |
| Additions                      | —                           | 12      |
| Repayments                     | (45                         | ) (56   |
| Change in related party status | (592                        | ) (58   |
| Balance at end of year         | \$471                       | \$1,108 |

Deposits from related parties held by the Company at December 31, 2014 and 2013 amounted to \$3.3 million and \$3.0 million, respectively.

## 20. RESTRICTIONS ON DIVIDENDS

Chicopee Bancorp, Inc. is subject to Massachusetts law, which prohibits distributions to stockholders if, after giving effect to the distribution, the corporation would not be able to pay its debts as they become due in the usual course of business or the corporation's total assets would be less than the sum of its total liabilities plus the amount that would be needed, if the corporation were to be dissolved at the time of the distribution, to satisfy the preferential rights upon dissolution of stockholders whose preferential rights are superior to those receiving the distribution. In addition, the Federal Reserve Board has issued a policy statement regarding the payment of dividends by bank holding companies. In general, the Federal Reserve Board's policies provide that dividends should be paid only out of current earnings and only if the prospective rate of earnings retention by the bank holding company appears consistent with the organization's capital needs, asset quality and overall financial condition. The Federal Reserve Board's

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CHICOPEE BANCORP, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

policies also require that a bank holding company serve as a source of financial strength to its subsidiary banks by standing ready to use available resources to provide adequate capital funds to those banks during periods of financial stress or adversity and by maintaining the financial flexibility and capital-raising capacity to obtain additional resources for assisting its subsidiary banks where necessary. Under the prompt corrective action laws, the ability of a bank holding company to pay dividends may be restricted if a subsidiary bank becomes undercapitalized. These regulatory policies could affect the ability of Chicopee Bancorp to pay dividends or otherwise engage in capital distributions.

Dividends from Chicopee Bancorp, Inc. may depend, in part, upon receipt of dividends from the Bank. The subsidiary may pay dividends to its parent out of so much of its net income as the Bank's directors deem appropriate, subject to the limitation that the total of all dividends declared by the Bank in any calendar year may not exceed the total of its net income of that year combined with its retained net income of the preceding two years and subject to minimum regulatory capital requirements. The approval of the Massachusetts Commissioner of Banks is required if the total of all dividends declared in any calendar year exceeds the total of its net profits for that year combined with its retained net profits of the preceding two years. Net profits for this purpose means the remainder of all earnings from current operations plus actual recoveries on loans and investments and other assets after deducting from the total thereof all current operating expenses, actual losses, accrued dividends on preferred stock, if any and all federal and state taxes. The payment of dividends from the Bank to the Company may be additionally restricted if the payment of such dividends resulted in the Bank failing to meet regulatory capital requirements. Capital of the Company and the Bank at December 31, 2014 was sufficient to meet the requirements of regulatory authorities.

During the years ended December 31, 2014, 2013 and 2012, a total of \$5.0 million, \$2.5 million and \$1.6 million, respectively, in dividends were declared from the Bank to the Company. During the years ended December 31, 2014, 2013 and 2012, a total of \$700,000, \$660,000 and \$2.0 million, respectively, in dividends were declared from Chicopee Funding Corporation ("CFC") to the Company.

During the years ended December 31, 2014 and 2013, cash dividends of \$1.4 million, or \$0.28 per share, and \$1.0 million, or \$0.20 per share, respectively, were paid to the Company's stockholders. There were no cash dividends paid to the Company's stockholders prior to 2013.

21. FAIR VALUE

Certain assets and liabilities are recorded at fair value to provide additional insight into the Company's quality of earnings. Some of these assets and liabilities are measured on a recurring basis while others are measured on a nonrecurring basis, with the determination based upon applicable existing accounting pronouncements. For example, available-for-sale securities are recorded at fair value on a recurring basis. Other assets, such as, mortgage servicing rights, loans held for sale, and impaired loans, are recorded at fair value on a nonrecurring basis using the lower of cost or market methodology to determine impairment of individual assets. The Company groups assets and liabilities which are recorded at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. Levels within the fair value hierarchy are based on the lowest level of input that is significant to the fair value measurement (with Level 1 considered highest and Level 3 considered lowest). A brief description of each level follows.

Level 1 - Valuation is based upon quoted prices for identical instruments in active markets.

Level 2 - Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market.

Level 3 - Valuation is generated from model-based techniques that use at least one significant assumption not observable in the market. These unobservable assumptions reflect estimates that market participants would use in pricing the asset or liability. Valuation includes use of discounted cash flow models and similar techniques.

The fair value methods and assumptions are set forth below.

Cash and cash equivalents. The carrying amounts of cash and cash equivalents approximate their relative fair values. As such, the Company classifies these financial instruments as Level 1.

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CHICOPEE BANCORP, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Held-to-maturity and non-marketable securities. The fair values of held-to-maturity securities are estimated by independent providers. In obtaining such valuation information from third parties, the Company has evaluated their valuation methodologies used to develop the fair values in order to determine whether the valuations are representative of an exit price in the Company's principal markets. The Company's principal markets for its securities portfolios are the secondary institutional markets, with an exit price that is predominately reflective of bid level pricing in those markets. Fair values are calculated based on the value of one unit without regard to any premium or discount that may result from concentrations of ownership of a financial instrument, possible tax ramifications, or estimated transaction costs. If these considerations had been incorporated into the fair value estimates, the aggregate fair value could have been changed. The carrying values of non-marketable securities approximate fair values. As such, the Company classifies held-to-maturity and non-marketable securities as Level 2.

Available-for-sale securities. Fair value of securities are primarily measured using unadjusted information from an independent pricing service. The securities measured at fair value in Level 1 are based on quoted market prices in an active exchange market. These securities include marketable equity securities.

Loans. Fair values are estimated for portfolios of loans with similar financial characteristics. The fair values of performing loans are calculated by discounting scheduled cash flows through the estimated maturity using estimated market discount rates that reflect the credit and interest risk inherent in the loan. The estimates of maturity are based on the Company's historical experience with repayments for each loan classification, modified, as required, by an estimate of the effect of current economic and lending conditions, and the effects of estimated prepayments. Assumptions regarding risk, cash flows, and discount rates are judgmentally determined using available market information and specific borrower information. Management has made estimates of fair value presented above would be indicative of the value negotiated in an actual sale. As such, the Company classifies loans as Level 3. Fair values of impaired loans are based on estimated cash flows and are discounted using a rate commensurate with the risk associated with the estimated cash flows, or if collateral dependent, discounted to the appraised value of the collateral, less costs to sell.

Loans held for sale. Loans held for sale are recorded at the lower of carrying value or fair value. The fair value of mortgage loans held for sale is based on what secondary markets are currently offering for portfolios with similar characteristics. As such, the Company classifies loans held for sale as nonrecurring Level 2.

OREO. Real estate acquired through foreclosure is recorded at fair value. The fair value of OREO is based on property appraisals and an analysis of similar properties currently available. As such, the Company records OREO as nonrecurring Level 2.

Mortgage servicing rights. Mortgage servicing rights represent the value associated with servicing residential mortgage loans. Servicing assets and servicing liabilities are reported using the amortization method. In evaluating the carrying values of the mortgage servicing rights, the Company obtains third party valuations based on loan level data including note rate, type and term of the underlying loans. As such, the Company classifies mortgage servicing rights as nonrecurring Level 2.

Accrued interest receivable. The fair value estimate of this financial instrument approximates the carrying value as this financial instrument has a short maturity. It is the Company's policy to stop accruing interest on loans for which it is probable that the interest is not collectable. Therefore, this financial instrument has been adjusted for estimated credit loss. As such, the Company classifies accrued interest receivable as Level 2.

Deposits. The fair value of deposits is based on the discounted value of contractual cash flows. The discount rate is estimated using the rates currently offered for deposits of similar remaining maturities. The fair value estimates do not include the benefit that results from the low-cost funding provided by the deposits compared to the cost of borrowing funds in the market. If that value were considered, the fair value of the Company's net assets could increase. As such, the Company classifies deposits as Level 2.

Borrowed funds. The fair value of borrowed funds is based on the discounted value of contractual cash flows. The discount rate is estimated using the rates currently available for borrowings of similar remaining maturities. As such, the Company classifies borrowed funds as Level 2.

Accrued interest payable. The fair value estimate approximates the carrying amount as this financial instrument has a short maturity. As such, the Company classifies accrued interest payable as Level 2.

Off-balance-sheet instruments. Off-balance-sheet instruments include loan commitments. Fair values for loan commitments have not been presented as the future revenue derived from such financial instruments is not significant.

## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Limitations. Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial instrument. These values do not reflect any premium or discount that could result from offering for sale at one time the Company's entire holdings of a particular financial instrument. Because no market exists for a significant portion of the Company's financial instruments, fair value estimates are based on Management's judgments regarding future expected loss experience, current economic conditions, risk characteristics of various financial instruments, and other factors. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect these estimates. Fair value estimates are based on existing on- and off-balance-sheet financial instruments without attempting to estimate the value of anticipated future business and the value of assets and liabilities that are not considered financial instruments. Other significant assets and liabilities that are not considered financial instruments include the deferred tax asset and, premises and equipment. In addition, tax ramifications related to the realization of the unrealized gains and losses can have a significant effect on fair value estimates and have not been considered in any of these estimates.

Assets measured at fair value as of December 31, 2014 and 2013 on a recurring basis are summarized below:

|                                     | December 31,<br>2014   | Fair Value Measurements Using                      |  |                                    |
|-------------------------------------|------------------------|--|--|------------------------------------|
|                                     |                        | Readily<br>Available<br>Market Prices<br>(Level 1) | Observable<br>Market Data<br>(Level 2) | Determined Fair<br>Value (Level 3) |
| Assets (market approach)            | (Dollars In Thousands) |  |  |                                    |
| Available-for-sale securities:      |                        |  |  |                                    |
| Equity securities by industry type: |                        |  |  |                                    |
| Financial                           | \$414                  | \$414  | \$—                                    | \$—                                |
| Total equity securities             | \$414                  | \$414  | \$—                                    | \$—                                |

|                                     | December 31,<br>2013   | Fair Value Measurements Using                      |  |                                    |
|-------------------------------------|------------------------|--|--|------------------------------------|
|                                     |                        | Readily<br>Available<br>Market Prices<br>(Level 1) | Observable<br>Market Data<br>(Level 2) | Determined Fair<br>Value (Level 3) |
| Assets (market approach)            | (Dollars In Thousands) |  |  |                                    |
| Available-for-sale securities:      |                        |  |  |                                    |
| Equity securities by industry type: |                        |  |  |                                    |
| Financial                           | \$602                  | \$602  | \$—                                    | \$—                                |
| Total equity securities             | \$602                  | \$602  | \$—                                    | \$—                                |



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## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Assets measured at fair value on a nonrecurring basis as of December 31, 2014 and 2013 are summarized below:

|                           | December 31,<br>2014 | Fair Value Measurements Using                   |  |                                       |
|---------------------------|----------------------|---|--|---------------------------------------|
|                           |                      | Readily<br>Available Market<br>Prices (Level 1) | Observable<br>Market Data<br>(Level 2) | Determined<br>Fair Value<br>(Level 3) |
| (Dollars In Thousands)    |                      |   |  |                                       |
| Assets:                   |                      |   |  |                                       |
| Impaired loans            | \$5,184              | \$—   | \$—                                    | \$5,184                               |
| OREO                      | 1,050                | —   | 1,050                                  | —                                     |
| Mortgage servicing rights | 622                  | —   | 622                                    | —                                     |

|                           | December 31,<br>2013 | Fair Value Measurements Using                   |  |                                       |
|---------------------------|----------------------|---|--|---------------------------------------|
|                           |                      | Readily<br>Available Market<br>Prices (Level 1) | Observable<br>Market Data<br>(Level 2) | Determined<br>Fair Value<br>(Level 3) |
| (Dollars In Thousands)    |                      |   |  |                                       |
| Assets:                   |                      |   |  |                                       |
| Impaired loans            | \$1,869              | \$—   | \$—                                    | \$1,869                               |
| OREO                      | 407                  | —   | 407                                    | —                                     |
| Loans held for sale       | 70                   | —   | 70                                     | —                                     |
| Mortgage servicing rights | 831                  | —   | 831                                    | —                                     |

Impaired loans are presented net of their related specific reserve of \$73,000 and \$279,000 as of December 31, 2014 and 2013, respectively.

## Fair Value of Financial Instruments.

FASB ASC Topic 825, "Financial Instruments", requires disclosures of fair value information about financial instruments, whether or not recognized in the balance sheet, if the fair values can be reasonably determined. Fair value is best determined based upon quoted market prices. However, in many instances, there are no quoted market prices for the Company's various financial instruments. In cases where quoted prices are not available, fair values are based on estimates using present value or other valuation techniques using observable inputs when available. 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 instrument. FASB ASC Topic 825 excludes certain financial instruments and all non-financial instruments from its disclosure requirements. Accordingly, the aggregate fair value amounts presented may not necessarily represent the underlying fair value of the Company.

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## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The fair values of the Company's financial instruments are as follows:

|                               | Carrying<br>Amount at<br>December 31,<br>2014<br>(Dollars In Thousands) | Fair Value Measurements Using                      |  |                                       |
|-------------------------------|---|--|--|---------------------------------------|
|                               |   | Readily<br>Available<br>Market Prices<br>(Level 1) | Observable<br>Market Data<br>(Level 2) | Determined<br>Fair Value<br>(Level 3) |
| Financial assets:             |   |  |  |                                       |
| Cash and cash equivalents     | \$49,769  | \$49,769   | \$—                                    | \$—                                   |
| Available-for-sale securities | 414   | 414  | —                                      | —                                     |
| Held-to-maturity securities   | 33,747  | —  | 34,229                                 | —                                     |
| FHLB stock                    | 3,914   | —  | 3,914                                  | —                                     |
| Loans:                        |   |  |  |                                       |
| Residential real estate       | 118,837   | —  | —                                      | 121,296                               |
| Residential construction      | 8,022   | —  | —                                      | 8,008                                 |
| Commercial real estate        | 247,246   | —  | —                                      | 248,316                               |
| Commercial construction       | 35,218  | —  | —                                      | 35,463                                |
| Commercial and industrial     | 73,452  | —  | —                                      | 73,668                                |
| Consumer                      | 2,627   | —  | —                                      | 2,804                                 |
| Home equity                   | 34,355  | —  | —                                      | 34,453                                |
| Net loans                     | 519,757   | —  | —                                      | 524,008                               |
| Accrued interest receivable   | 1,591   | —  | 1,591                                  | —                                     |
| Mortgage servicing rights     | 269   | —  | 622                                    | —                                     |
| Financial liabilities:        |   |  |  |                                       |
| Deposits                      | \$483,558   | \$—  | \$484,423                              | \$—                                   |
| FHLB long-term advances       | 67,039  | —  | 67,644                                 | —                                     |
| Accrued interest payable      | 82  | —  | 82                                     | —                                     |

## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

|                               | Carrying<br>Amount at<br>December 31,<br>2013<br>(Dollars In Thousands) | Fair Value Measurements Using<br>Readily<br>Available<br>Market Prices<br>(Level 1) | Observable<br>Market Data<br>(Level 2) | Determined<br>Fair Value<br>(Level 3) |
|-------------------------------|---|---|--|---------------------------------------|
| Financial assets:             |   |   |  |                                       |
| Cash and cash equivalents     | \$ 18,915   | \$ 18,915   | \$—                                    | \$—                                   |
| Available-for-sale securities | 602   | 602   | —                                      | —                                     |
| Held-to-maturity securities   | 48,606  | —   | 49,338                                 | —                                     |
| FHLB stock                    | 3,914   | —   | 3,914                                  | —                                     |
| Loans:                        |   |   |  |                                       |
| Residential real estate       | 112,551   | —   | —                                      | 116,049                               |
| Residential construction      | 6,036   | —   | —                                      | 6,028                                 |
| Commercial real estate        | 209,286   | —   | —                                      | 212,228                               |
| Commercial construction       | 38,006  | —   | —                                      | 36,432                                |
| Commercial and industrial     | 85,430  | —   | —                                      | 85,511                                |
| Consumer                      | 2,370   | —   | —                                      | 2,530                                 |
| Home equity                   | 31,940  | —   | —                                      | 32,183                                |
| Net loans                     | 485,619   | —   | —                                      | 490,961                               |
| Accrued interest receivable   | 1,609   | —   | 1,609                                  | —                                     |
| Mortgage servicing rights     | 381   | —   | 831                                    | —                                     |
| Financial liabilities:        |   |   |  |                                       |
| Deposits                      | \$ 449,766  | \$—   | \$ 451,245                             | \$—                                   |
| FHLB long-term advances       | 44,992  | —   | 45,699                                 | —                                     |
| Accrued interest payable      | 59  | —   | 59                                     | —                                     |

## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## 22. QUARTERLY CONSOLIDATED FINANCIAL INFORMATION (UNAUDITED)

Following is the quarterly financial information of the Company for 2014 and 2013:

|  | 2014             |                   |                  |                   | 2013             |                   |                  |                   |
|--|------------------|-------------------|------------------|-------------------|------------------|-------------------|------------------|-------------------|
|  | First<br>Quarter | Second<br>Quarter | Third<br>Quarter | Fourth<br>Quarter | First<br>Quarter | Second<br>Quarter | Third<br>Quarter | Fourth<br>Quarter |
|  | (In Thousands)   |                   |                  |                   |                  |                   |                  |                   |
| Interest and dividend income                       | \$5,623          | \$5,784           | \$5,934          | \$6,013           | \$5,894          | \$5,792           | \$5,710          | \$5,673           |
| Interest expense                                   | 927              | 921               | 913              | 922               | 1,150            | 1,149             | 1,069            | 981               |
| Net interest income                                | 4,696            | 4,863             | 5,021            | 5,091             | 4,744            | 4,643             | 4,641            | 4,692             |
| (Reduction of ) provision for loan losses          | 2,201            | 2,774             | 227              | 69                | (70 )            | 127               | 212              | 156               |
| Net gain on sales of available-for-sale securities | 34               | —                 | —                | —                 | —                | —                 | —                | 37                |
| Non-interest income                                | 555              | 711               | 899              | 618               | 842              | 788               | 764              | 669               |
| Non-interest expenses                              | 4,618            | 4,694             | 4,737            | 4,851             | 4,634            | 4,655             | 4,505            | 4,361             |
| Income (loss) before income tax                    | (1,534 )         | (1,894 )          | 956              | 789               | 1,022            | 649               | 688              | 881               |
| Income tax expense                                 | (175 )           | (1,854 )          | 434              | 490               | 225              | 136               | 115              | 211               |
| Net income (loss)                                  | \$(1,359 )       | \$(40 )           | \$522            | \$299             | \$797            | \$513             | \$573            | \$670             |
| Earnings (loss) per share:                         |                  |                   |                  |                   |                  |                   |                  |                   |
| Basic  | \$(0.27 )        | \$(0.01 )         | \$0.10           | \$0.06            | \$0.16           | \$0.10            | \$0.11           | \$0.14            |
| Diluted  | \$(0.27 )        | \$(0.01 )         | \$0.10           | \$0.06            | \$0.16           | \$0.10            | \$0.11           | \$0.14            |

## 23. CONDENSED FINANCIAL STATEMENTS OF PARENT COMPANY

Financial information pertaining to Chicopee Bancorp, Inc. is as follows:

| BALANCE SHEETS   | December 31,   |          |
|--|----------------|----------|
|  | 2014           | 2013     |
|  | (In Thousands) |          |
| Assets:  |                |          |
| Cash and cash equivalents                                  | \$6,852        | \$4,387  |
| Investment in common stock of Chicopee Savings Bank        | 75,140         | 81,715   |
| Investment in common stock of Chicopee Funding Corporation | 4,192          | 4,429    |
| Other assets   | 1,985          | 1,701    |
| Total assets   | \$88,169       | \$92,232 |
| Liabilities and Stockholders' Equity:                      |                |          |
| Total liabilities  | \$35           | \$2      |
| Stockholders' equity                                       | 88,134         | 92,230   |
| Total liabilities and stockholders' equity                 | \$88,169       | \$92,232 |

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## CHICOPEE BANCORP, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

| STATEMENTS OF INCOME   | Years Ended December 31, |         |         |
|--|--------------------------|---------|---------|
|  | 2014                     | 2013    | 2012    |
|  | (In Thousands)           |         |         |
| Interest income  | \$9                      | \$11    | \$2,043 |
| Dividend income from subsidiaries  | 7,373                    | 3,124   | 1,565   |
| Operating expenses   | 814                      | 750     | 704     |
| Income before income taxes and equity in undistributed net income (loss) of subsidiaries | 6,568                    | 2,385   | 2,904   |
| Applicable income tax benefit  | (279)                    | (57)    | (44)    |
| Income before equity in undistributed net income (loss) of subsidiaries                  | 6,847                    | 2,442   | 2,948   |
| Equity in undistributed net income (loss) of Chicopee Savings Bank                       | (7,188)                  | 390     | 1,157   |
| Equity in undistributed net loss of Chicopee Funding Corporation                         | (237)                    | (279)   | (1,640) |
| Net income (loss)  | \$(578)                  | \$2,553 | \$2,465 |
|  | Years Ended December 31, |         |         |
|  | 2014                     | 2013    | 2012    |
|  | (In Thousands)           |         |         |
| Cash flows from operating activities:  |                          |         |         |
| Net income (loss)  | \$(578)                  | \$2,553 | \$2,465 |
| Adjustments to reconcile net income (loss) to net cash provided by operating activities: |                          |         |         |
| Equity in undistributed net (income) loss of Chicopee Savings Bank                       | 7,188                    | (390)   | (1,157) |
| Equity in undistributed net loss of Chicopee Funding Corporation                         | 237                      | 203     | 1,640   |
| Increase in other assets   | (284)                    | (212)   | (391)   |
| Increase (decrease) in other liabilities   | 33                       | 2       | (50)    |
| Stock option expense   | 140                      | 118     | 278     |
| Change in unearned compensation  | 496                      | 515     | 813     |
| Net cash provided by operating activities  | 7,232                    | 2,789   | 3,598   |
| Cash flows from investing activities:  |                          |         |         |
| Investment in Chicopee Savings Bank  | (636)                    | (633)   | (1,091) |
| Net cash used in investing activities  | (636)                    | (633)   | (1,091) |
| Cash flows from financing activities:  |                          |         |         |
| Treasury stock purchased   | (2,862)                  | (242)   | (4,377) |
| Adjustment to treasury shares  | —                        | —       | 32      |
| Cash dividends paid on common stock  | (1,410)                  | (1,008) | —       |
| Exercise of stock options  | 141                      | 299     | (53)    |
| Net cash used in financing activities  | (4,131)                  | (951)   | (4,398) |
| Net increase (decrease) in cash and cash equivalents                                     | 2,465                    | 1,205   | (1,891) |
| Cash and cash equivalents at beginning of year   | 4,387                    | 3,182   | 5,073   |
| Cash and cash equivalents at end of year   | \$6,852                  | \$4,387 | \$3,182 |

## 24. SUBSEQUENT EVENTS



Subsequent Events represent events or transactions occurring after the balance sheet date but before the financial statements are issued or are available to be issued. Financial statements are considered “issued” when they are widely distributed to stockholders and others for general use and reliance in a form and format that complies with GAAP. Financial statements are considered “available to be issued” when they are complete in form and format that complies with GAAP and all approvals necessary for their issuance have been obtained.

Specifically, there are two types of subsequent events:

Those comprising events or transactions providing additional evidence about conditions that existed at the balance sheet date, including estimates inherent in the financial statement preparation process (referred to as recognized subsequent events).

Those comprising events that provide evidence about conditions not existing at the balance sheet date but, rather, that arose after such date (referred to as non-recognized subsequent events).

The Company is a Securities and Exchange Commission filer and management has evaluated subsequent events through the date that the financial statements were issued.

On January 26, 2015, the Company announced a cash dividend of \$0.07 per share of its common stock to stockholders of record as of the close of business on February 6, 2015, payable on or about February 20, 2015.