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SALISBURY BANCORP INC
Form 10KSB
March 28, 2002

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-KSB

(Mark One)

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

For the fiscal year ended December 31, 2001

OR

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

For the transition period from _____ to _____

Commission file number 0-24751

SALISBURY BANCORP, INC.
(Name of Small Business Issuer in its charter)

Connecticut 06-1514263

(State or Other Jurisdiction of (I.R.S. Employer
Incorporation or Organization) Identification No.)

5 Bissell Street, Lakeville, CT 06039

(Address of Principal Executive Offices) (Zip Code)

(860) 435-9801

(Issuer's telephone number, including area code)

Securities registered under Section 12 (b) of the Exchange Act:

| Title of Each Class ----- | Name of Each Exchange on Which Registered ----- |
|---|---|
| Common stock par value \$.10 per share ----- | American Stock Exchange ----- |

Securities registered under Section 12 (g) of the Exchange Act:

None

(Title of Class)

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

Yes No

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Check if there is no disclosure of delinquent filers in response to Item 405 of Regulation S-B is not contained in this form, and no disclosure will 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-KSB or any amendment to this Form 10-KSB. [X]

The revenues for the issuer's fiscal year ended December 31, 2001 are \$19,476,528

State the aggregate market value of the voting and non-voting common equity held by non-affiliates computed by reference to the price at which the common equity was sold, or the average bid and asked price of such common equity, as of a specified date within the past 60 days. (See definition of affiliate in Rule 12b-2 of the Exchange Act). On February 4, 2002: \$28,179,255

Note. If determining whether a person is an affiliate will involve an unreasonable effort and expense, the issuer may calculate the aggregate market value of the common equity held by non-affiliates on the basis of reasonable assumptions, if the assumptions are stated.

Check whether the issuer has filed all documents and reports required to be filed by Section 12, 13 or 15 (d) of the Exchange Act after the distribution of securities under a plan confirmed by a court.

Yes [X] No []

APPLICABLE ONLY TO CORPORATE REGISTRANTS

The Company had 1,422,358 shares outstanding as of March 8, 2002.
Transitional Small Business Disclosure Format (check one): Yes [] No [X]
Documents Incorporated by Reference: None

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PART I

ITEM 1. DESCRIPTION OF BUSINESS

(a) General Development of the Business

Salisbury Bancorp, Inc. (AMEX:SAL) (the "Company") is a Connecticut corporation that was formed in 1998. Its primary activity is to act as the holding company for its sole subsidiary, the Salisbury Bank and Trust Company (the "Bank") which accounts for most of the Company"s net income. The Bank assumed its present name in 1925 following the acquisition by the Robbins Burrall Trust Company of the Salisbury Savings Society. The Robbins Burrall Trust Company was incorporated in 1909 as the successor to a private banking firm established in 1874. The Salisbury Savings Society was incorporated in 1848. The Bank is chartered as a state bank and trust company by the State of Connecticut and its deposits are insured by the Federal Deposit Insurance Corporation in accordance with the Federal Deposit Insurance Act. The Bank"s main office is at 5 Bissell Street, Lakeville, Connecticut 06039. Its telephone number is (860) 435-9801.

The Bank serves its customers from its four (4) offices which are located in Canaan, Lakeville, Salisbury and Sharon, Connecticut. Substantially all of the Bank"s customers reside in or maintain their principal offices in Litchfield County, Connecticut or in Dutchess County or Columbia County, New York or in Berkshire County, Massachusetts.

The Company's products and services are all of the nature of a commercial bank and trust company.

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Lending

Lending is the principal business of the Bank and loans represent the largest portion of the Bank's assets. The portfolio consists of many types of loans. These include residential mortgages, home equity lines of credit, monthly installment loans for consumers as well as commercial loans which include lines of credit, short term loans, Small Business Administration ("SBA") loans and real estate loans for business customers.

The primary lending activity has been the origination of first mortgage loans for the purchase, refinance or construction of residential properties in the Bank's market area. The Bank has also increased its lending activity through home equity loans. Loans secured by mortgages on a borrower's principal residence are generally viewed as the least vulnerable to major economic changes and at the same time provide a significant yet relatively stable source of interest income. Presently, loans are maintained in the Bank's portfolio and are completely serviced by the Bank.

The Bank also originates a variety of other loans for consumer and business purposes. Although these loans represent a smaller percentage of the total loan portfolio, the Bank is in a position of being a full service retail lender to its consumers and a full service commercial lender to its business customers.

Investments

The Company's securities portfolio is also an important component of the balance sheet. It provides a source of earnings in the form of interest and dividends. It also plays a role in the interest rate risk management of the Company and it provides a source of liquidity.

The portfolio is comprised primarily of U.S. Government sponsored agencies, U.S. Treasury and mortgage-backed securities. At December 31, 2001, it totaled \$105,593,000 which represents approximately 37.23% of total assets.

Deposits and Borrowings

The Bank's primary sources of funds are deposits, borrowings and principal payments on loans. Although competition for funds from non-banking institutions remains aggressive, the Bank continues its efforts to build multiple account relationships with its customers. As a result, average daily deposits increased 9.51% to \$176,540,000 during 2001.

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The Bank is a member of the Federal Home Loan Bank of Boston. Borrowings totaled \$53,003,746 at December 31, 2001 as compared with \$47,357,293 at December 31, 2000.

For additional information relating to the asset, deposit and borrowing components of the Company, see Item 6, Management's Discussion and Analysis and the accompanying Consolidated Financial Statements.

Fiduciary

The Bank provides trust, investment and financial planning services to its customers.

The Bank has a full service Trust Department. Among the services offered are: custody and agency accounts, estate planning and estate settlement. Another service is that of serving as Guardian or Conservator of estates and managing

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the financial position of Guardianships or Conservatorships. Self directed IRAs and Pension plans are also offered.

All Others

The Company also offers safe deposit rentals, foreign exchange, a full menu of electronic fund transfer services and other ancillary services to businesses and individuals.

(b) Narrative Description of Business

Salisbury Bancorp, Inc. is a bank holding company, which as described above, has one subsidiary, Salisbury Bank and Trust Company (the "Bank").

The Bank is a full-service commercial bank and its activities encompass a broad range of services which includes a complete menu of deposit services, multiple mortgage products and various other types of loans for both business and personal needs. Full trust services are also available. The Bank owns and operates one subsidiary, SBT Realty, Inc. which is incorporated under the laws of the State of New York. SBT Realty, Inc. holds and manages bank owned real estate situated in New York State.

Competition

The Company and the Bank encounter competition in all phases of their business. Several competitive financial institutions have offices in the Salisbury, Connecticut Banking Market. In addition, the Bank competes with banking institutions located in Massachusetts and New York, as well as proximate areas of Connecticut.

The banking business in the area served by the Bank is very competitive. Based on information published by the Federal Reserve Bank of Boston, the Salisbury, Connecticut Banking market is served by seven (7) commercial banks and savings banks. As reflected below, the Bank has a 51.43% market share of deposits in such Salisbury Banking Market.

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SALISBURY, CONNECTICUT ALL INSTITUTIONS, BY TOTAL DEPOSITS

| | City | State | Market Deposits | Market Share |
|--|-------------|-------|---------------------------|-----------------|
| 1. Salisbury Bancorp, Inc. (Salisbury Bank & Trust Company) | Lakeville | CT | \$ 183,320 (\$183,320) | 51.43% --- |
| 2. Canaan National Bancorp, Inc. (Canaan National Bank) | Canaan | CT | \$ 52,310 (\$ 52,310) | 14.67% --- |
| 3. Iron Bancshares, Inc. (National Iron Bank) | Salisbury | CT | \$ 34,060 (\$ 34,060) | 9.56% --- |
| 4. NewMil Bancorp, Inc. (NewMil Bank) | New Milford | CT | \$ 32,990 (\$ 32,990) | 9.26% --- |
| 5. Torrington Savings Bank | Torrington | CT | \$ 26,800 | 7.52% |
| 6. Union Savings Bank | Danbury | CT | \$ 14,370 | 4.03% |
| 7. Connecticut Mutual Holding Company | Winsted | CT | \$ 12,590 ----- | 3.53% ----- |

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(Litchfield Bancorp)

\$ 356,440
=====

100.00%
=====

Herfindahl-Hirschman Index: 3,123

Note: The table is based on June 30, 2000 FDIC and OTS Summary of Deposits data (dollars in millions). It reflects all mergers and bank holding company acquisitions completed by January 2, 2002. Holding companies with at least one commercial bank subsidiary are always considered commercial banking organizations, even in markets where only their thrift(s) operate.

While the Bank enjoys a large market share of the Salisbury Connecticut Banking Market, the Bank's share of the total deposits throughout all of Litchfield County would represent approximately 6% of such market, and would make the Bank the 8th largest of 20 institutions within Litchfield County.

Banks compete on the basis of price, including rates paid on deposits and charged on borrowings, convenience and quality of service. Savings and loan associations are able to compete aggressively with commercial banks in the important area of consumer lending. Credit unions and small loan companies are each significant factors in the consumer market. Insurance companies, investment firms, credit and mortgage companies, brokerage firms cash management accounts, money-market funds and retailers are all significant competitors for various types of business. Insurance companies, investment counseling firms and other businesses and individuals actively compete with the Bank for personal and corporate trust services and investment counseling services. Many non-bank competitors are not subject to the extensive regulation described below under "LEGISLATION, REGULATION AND SUPERVISION" and in certain respects may have a competitive advantage over banks in providing certain services.

In marketing its services, the Bank emphasizes its position as a hometown bank with personal service, flexibility and prompt responsiveness to the needs of its customers. Moreover, the Bank competes for both deposits and loans by offering competitive rates and convenient business hours. In addition to providing banking services to customers in its primary service areas, the Bank is a member of the automatic teller machine networks and offers internet banking services, which allow the Bank to deliver certain financial services to customers regardless of their proximity to the primary service area of the Bank.

Connecticut has enacted legislation which liberalized banking powers for thrift institutions thereby improving their competitive position with other banks. In addition, the Connecticut Interstate Banking Act permits acquisitions of and mergers with Connecticut banks and bank holding companies with banks and bank holding companies in other states. Accordingly, it is possible for large super-regional organizations to enter many new markets including the market served by the Bank. Certain of these competitors, by virtue of their size and resources, may enjoy certain efficiencies and competitive advantages over the Bank in the pricing, delivery, and marketing of their products and services. It is possible that such legislative authority will increase the number or the size of financial institutions competing with the Bank for deposits and loans in its market place, although it is impossible to predict the effect upon competition of such legislation.

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Legislation, Regulation and Supervision

General

Virtually every aspect of the business of banking is subject to regulation including such matters as the amount of reserves that must be established

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against various deposits, the establishment of branches, mergers, non-banking activities and other operations. Numerous laws and regulations also set forth special restrictions and procedural requirements with respect to the extension of credit, credit practices, the disclosure of credit terms and discrimination in credit transactions.

The descriptions of the statutory provisions and regulations applicable to banks set forth below do not purport to be a complete description of such statutes and regulations and their effects on the Bank. Proposals to change the laws and regulations governing the banking industry are frequently introduced in Congress, in the state legislatures and before the various bank regulatory agencies. The likelihood and timing of any changes and the impact such changes might have on the Bank's future business and earnings are difficult to determine.

Federal Reserve Board Regulation

The Company is a registered bank holding company under the Bank Holding Company Act of 1956, as amended (the "BHCA"). It is subject to the supervision and examination of the Board of Governors of the Federal Reserve System (the "Federal Reserve Board") and files with the Federal Reserve Board the reports as required under the BHCA.

The BHCA generally requires prior approval by the Federal Reserve Board of the acquisition by the Company of substantially all of the assets or more than five percent (5%) of the voting stock of any bank. The BHCA also allows the Federal Reserve Board to determine (by order or by regulation) what activities are so closely related to banking as to be a proper incident of banking, and thus, whether the Company can engage in such activities. The BHCA prohibits the Company and the Bank from engaging in certain tie-in arrangements in connection with any extension of credit, sale of property or furnishing of services.

Federal legislation permits adequately capitalized bank holding companies to venture across state lines to offer banking services through bank subsidiaries to a wide geographic market. It is possible for large super-regional organizations to enter many new markets including the market served by the Bank, although it is impossible to assess what impact this will have on the Company or the Bank.

The Federal Reserve Act imposes certain restrictions on loans by the Bank to the Company and certain other activities, on investments, in their stock or securities, and on the taking by the Bank of such stock or securities as collateral security for loans to any borrower.

Under the BHCA and the regulations of the Federal Reserve System promulgated thereunder ("Regulation Y"), no corporation may become a bank holding company as defined therein, without prior approval of the Federal Reserve Board. The Company received the approval to become a bank holding company on June 18, 1998. The Company will also have to secure prior approval of the Federal Reserve Board if it wishes to acquire voting shares of any other bank, if after such acquisition it would own or control more than five percent (5%) of the voting share of such bank. The BHCA imposes limitations upon the Company as to the types of business in which it may engage.

Regulation Y requires bank holding companies to provide the Federal Reserve Board with written notice before purchasing or redeeming equity securities if the gross consideration for the purchase or redemption, when aggregated with the net consideration paid by the Company for all such purchases or redemptions during the preceding twelve (12) months, is equal to ten percent (10%) or more of the Company's consolidated net worth. For purposes of Regulation Y, "net consideration" is the gross consideration paid by a company for all of its equity securities purchased or redeemed during the period, minus the gross

consideration received for all of its equity securities sold during the period other than as part of a new issue. However, a bank holding company need not obtain Federal Reserve Board approval of any equity security redemption when: (i) the bank holding company's capital ratios exceed the threshold established for "well-capitalized" state member banks before and immediately after the redemption; (ii) the bank holding company is well-managed; and (iii) the bank holding company is not the subject of any unresolved supervisory issues. The Gramm-Leach-Bliley Financial Services Modernization Act of 1999 (S.900) (the "GLBA"), provides bank holding companies, banks, securities firms, insurance companies, and investment management firms the option of engaging in a broad range of financial and related activities by opting to become a "financial holding company." These holding companies will be subject to oversight by the Federal Reserve Board, in addition to other regulatory agencies. Under the financial holding company structure, bank holding companies have greater ability to purchase or establish nonbank subsidiaries which are financial in nature or which engage in activities which are incidental or complementary to a financial activity. Additionally, for the first time, securities and insurance firms will be permitted to purchase full-service banks.

While the GLBA Act facilitates the ability of financial institutions to offer a wide range of financial services, large financial institutions would appear to be the beneficiaries as a result of this Act because many community banks are less able to devote the capital and management resources needed to facilitate broad expansion of financial services. The Company qualified and registered as a financial holding company in May 3, 2000.

Connecticut Regulation

The Company is incorporated in the State of Connecticut and is subject to the Connecticut Business Corporation Act and the Connecticut Bank Holding Company Statutes.

As a state-chartered bank and member of the Federal Deposit Insurance Corporation ("FDIC"), the Bank is subject to regulation both by the Connecticut Banking Commissioner and by the FDIC. Applicable laws and regulations impose restrictions and requirements in many areas, including capital requirements, maintenance of reserves, establishment of new branch offices, mergers, making of loans and investments, consumer protection, employment practices and other matters. Any new regulations or amendments to existing regulations may materially affect the services offered, expenses incurred and/or income generated by the Bank.

The Connecticut Banking Commissioner regulates the Bank's internal organization as well as its deposit, lending and investment activities. The approval of the Connecticut Banking Commissioner is required, among other things, to open branch offices and to consummate merger transactions and other business combinations. The Connecticut Banking Commissioner conducts periodic examinations of the Bank. The Connecticut banking statutes also restrict the ability of the Bank to declare cash dividends to its shareholders.

Subject to certain limited exceptions, loans made to any one obligor may not exceed fifteen percent (15%) of the Bank's capital, surplus, undivided profits and loan reserves. In addition, under Connecticut law, the beneficial ownership of more than ten percent (10%) of any class of voting securities of a bank may not be acquired by any person or groups of persons acting in concert without the approval of the Connecticut Banking Commissioner.

FDIC Regulation

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The FDIC insures the Bank's deposit accounts in an amount up to \$100,000 for each insured depositor. FDIC insurance of deposits may be terminated by the FDIC, after notice and a hearing, upon a finding by the FDIC that the insured institution has engaged in unsafe or unsound practices, or is in an unsafe or unsound condition to continue operations, or has violated any applicable law, regulation, rule or order of, or condition imposed by, the FDIC. A bank's failure to meet the minimum capital and risk-based capital guidelines discussed below, would be considered to be unsafe and unsound banking practices. The Bank, as a Connecticut-chartered FDIC-insured bank, is regulated by the FDIC in many of the areas also regulated by the Connecticut Banking Commissioner. The FDIC also conducts its own periodic examinations of the Bank, and the Bank is required to submit financial and other reports to the FDIC on a quarterly and annual basis, or as otherwise required by the FDIC.

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FDIC insured banks, such as the Bank, pay premiums to the FDIC for the insurance of deposits.

Under FDIC regulations, FDIC-insured, state-chartered banks which are not members of the Federal Reserve System must meet certain minimum capital requirements, including a leverage capital ratio and a risk-based capital ratio. See "MANAGEMENT'S DISCUSSION AND ANALYSIS".

The Community Reinvestment Act ("CRA") requires lenders to identify the communities served by the institution's offices and to identify the types of credit the institution is prepared to extend within such communities. The FDIC conducts examinations of insured institutions' CRA compliance and rates such institutions as "Outstanding", "Satisfactory", "Needs to Improve" and "Substantial Noncompliance". As of its last CRA examination, the Bank received a rating of "Outstanding". Failure to receive at least a "Satisfactory" rating may inhibit an institution from undertaking certain activities, including acquisitions of other financial institutions, which require regulatory approval based, in part, on CRA compliance considerations. Similarly, failure of a bank to maintain a CRA rating of "Satisfactory" or better would preclude it or its holding company from engaging in any new financial activities pursuant to the Gramm-Leach-Bliley Act.

Employees

The Company's current workforce at January 31, 2002 was 79 employees of whom 66 were full time and 13 were part time. The employees are not represented by a collective bargaining unit.

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STATISTICAL DISCLOSURE REQUIRED PURSUANT TO SECURITIES EXCHANGE ACT, INDUSTRY GUIDE 3

The statistical disclosures required pursuant to Industry Guide 3, not contained in Management's Discussion and Analysis of Financial Condition and Results of Operations-contained herein, are presented on the following pages of this Report on Form 10-KSB.

Page(s) of

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Investment Portfolio

As of December 1994, Salisbury Bank and Trust Company adopted Statement of Financial Accounting Standard No. 115 (SFAS 115), "Accounting for Certain Investments in Debt and Equity Securities". SFAS 115 provides for the categorization of investments into three (3) groups and further provides for the accounting and reporting treatment of each group. Investments may be classified as held-to-maturity, available-for-sale, or trading. The Bank does not purchase or hold any investment securities for the purpose of trading such investments. The following table sets forth the carrying amounts of the investment securities as of December 31:

(dollars in thousands)

| | 2001 ----- | 2000 ----- |
|--|---------------|---------------|
| Available-for-sale securities: (at fair value) | | |
| Equity securities | \$ 135 | \$ 179 |
| U.S. Treasury securities and other | | |
| U.S. government corporations and agencies | 38,701 | 46,761 |
| Obligations of states and political subdivisions | 30,273 | 14,170 |
| Mortgage-backed securities | 33,139 | 27,472 |
| | ----- | ----- |
| | \$102,248 | \$ 88,582 |
| | ===== | ===== |
| Held-to-maturity securities (at amortized cost) | | |
| U.S. Treasury securities and other | | |
| U.S. government corporations and agencies | \$ 0 | \$ 0 |
| Obligations of states and political subdivisions | 400 | 410 |
| Mortgage-backed securities | \$ 400 | \$ 410 |
| | ----- | ----- |
| Federal Home Loan Bank stock | \$ 2,945 | \$ 2,930 |
| | ===== | ===== |

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For the following table, yields are not calculated and presented on a fully taxable-equivalent ("FTE") basis.

The scheduled maturities of held-to-maturity securities and available-for-sale securities (other than equity securities) were as follows as of December 31, 2001:

(dollars in thousands)

| | Under 1 Year Yield ----- | 1-5 Years ----- | Yield ----- | 5-10 Years ----- | Yield ----- |
|--|--------------------------------|-----------------------|----------------|------------------------|----------------|
| Held-to-maturity ----- securities ----- (at amortized cost) | | | | | |
| U.S. Treasury securities and other U.S. government corporations and agencies | \$ 0 | \$ 0 | | \$ 0 | |
| Obligations of state and political subdivisions | | | | | |
| Mortgage-backed securities | | | | | |
| Available-for-sale ----- securities ----- (at fair value) | | | | | |
| U.S. Treasury securities and other U.S. government corporations and agencies | \$ 0 | \$ 1,038 | 5.38% | \$ 3,034 | 6.70% |
| Obligations of state and political subdivisions \$30,273 | \$ 0 | \$ 451 | 4.76% | \$ 3,370 | 4.98% |
| Mortgage-backed securities | \$ 0 | \$ 1,473 | 7.16% | \$ 1,053 | 6.00% |

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Loan Portfolio Analysis by Category
(dollars in thousands)

| | 2001 ----- | 2000 ----- | December 31 1999 ----- | 1998 ----- |
|---|---------------|---------------|------------------------------|---------------|
| Commercial, financial and agricultural | \$ 10,797 | \$ 8,592 | \$ 9,025 | \$ 10,692 |

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| | | | | |
|---|------------|-----------|-----------|------------|
| Real Estate-construction and land development | 3,935 | 6,275 | 3,382 | 3,392 |
| Real Estate - residential | 102,201 | 98,312 | 86,680 | 80,451 |
| Real Estate-commercial | 17,423 | 15,463 | 15,324 | 14,909 |
| Consumer 10,030 | 10,673 | 10,698 | 10,430 | 10,805 |
| Other | 125 | 247 | 364 | 535 |
| | ----- | ----- | ----- | ----- |
| | 144,511 | 139,562 | 125,473 | 120,409 |
| Allowance for possible loan losses | (1,445) | (1,292) | (1,160) | (1,260) |
| Unearned income | 0 | (0) | (0) | (6) |
| | ----- | ----- | ----- | ----- |
| Net loans | \$ 143,066 | \$138,270 | \$124,313 | \$ 119.143 |
| | ===== | ===== | ===== | ===== |

There are no industry concentrations in the Bank"s loan portfolio.

The following table shows the maturity of commercial, financial and agricultural loans, real estate commercial loans and real estate-construction loans outstanding as of December 31, 2001. Also provided are the amounts due after one (1) year classified according to the sensitivity to changes in interest rates.

| | Due in one year or less ----- | Due after one year to five years ----- | Due af five y ----- |
|---|-------------------------------------|---|---------------------------|
| Commercial, financial, agricultural and real estate commercial | \$19,074 | \$ 3,029 | \$ 6,1 |
| Real estate-construction and land development | 3,957 | 0 | |
| | ----- | ----- | ----- |
| | \$23,031 | \$ 3,029 | \$ 6,1 |
| | ===== | ===== | ===== |
| Maturities after One Year with: | | | |
| Fixed interest rates | | \$ 2,266 | \$ 6,1 |
| Variable interest rates | | 763 | |
| | | ----- | ----- |
| | | \$ 3,029 | \$ 6,1 |
| | | ===== | ===== |

Return on Equity and Assests

The following table summarizes various financial ratios of the Company for each of the last three (3) years:

| | Year ended December 31, ----- | | |
|--|----------------------------------|--------------|--------------|
| | 2001 ---- | 2000 ---- | 1999 ---- |
| Return on average total assets (net income divided by average total assets) | 1.14% | 1.23% | 1.25% |

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| | | | |
|---|--------|--------|--------|
| Return on average shareholders' equity (net income divided by average shareholders' equity) | 12.25% | 13.64% | 12.96% |
| Dividend payout ratio (total declared dividends divided by net income) | 41.38% | 39.72% | 39.16% |
| Equity to assets ratio (average shareholders' equity as a percentage of average total assets) | 9.27% | 8.98% | 9.67% |
| Nonaccrual, Past Due and Restructured Loans | | | |

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At December 31, 2001, there were two (2) nonaccrual loans in the Bank's portfolio. They were secured by 1-4 family residential properties. There were three (3) real estate loans 90 days past due and still accruing. They are scheduled to be brought current during 2002. When a mortgage loan becomes 90 days past due, and there is not sufficient collateral to cover the principal and accrued interest, the Bank generally stops accruing interest unless there are unusual circumstances which warrant an exception. Generally the only loan types that the Bank reclassifies to nonaccrual are those secured by real estate. Other types of loans are generally charged off if they become 90 days or more delinquent. However, exception is warranted with the \$44,000 in loans that are presently 90 days past due and still accruing.

Nonaccrual, Past Due and Restructured Loans
(dollars in thousands)

| | 2001 | 2000 | December 31 1999 | 1998 | 1997 |
|--|---------|---------|---------------------|---------|---------|
| | ----- | ----- | ----- | ----- | ----- |
| Nonaccrual | \$ 372 | \$ 186 | \$ 473 | \$1,208 | \$1,328 |
| 90 days or more past due | 215 | 323 | 10 | 109 | 279 |
| Restructured loans | 0 | 12 | 12 | 547 | 764 |
| | ----- | ----- | ----- | ----- | ----- |
| Total nonperforming loans | \$ 587 | \$ 521 | \$ 495 | \$1,864 | \$2,371 |
| | ===== | ===== | ===== | ===== | ===== |
| Total nonperforming loans as per- centage of the total loan portfolio | 0.41% | 0.37% | 0.39% | 1.55% | 2.01% |
| Allowance for loan losses as a per- centage of nonperforming loans | 246.17% | 247.99% | 234.34% | 67.60% | 51.71% |

Information with respect to non-accrual and restructured loans at December 31, 2001, 2000 and 1999 is as follows:

(dollars in thousands)

Year Ended December

| | |
|-------|-------|
| 2001 | 2000 |
| ----- | ----- |

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| | | |
|--|-------|-------|
| Interest income that would have been recorded under original terms | \$ 38 | \$ 12 |
| Gross interest recorded | 28 | 1 |
| | ----- | ----- |
| Foregone interest | \$ 10 | \$ 11 |
| | ===== | ===== |

Summary of Loan Loss Experience
(dollars in thousands)

| | Year Ended December 31 | | | |
|---|------------------------|----------|----------|----------|
| | 2001 | 2000 | 1999 | 1998 |
| | ----- | ----- | ----- | ----- |
| Balance of the allowance for loan losses at beginning of year | \$ 1,292 | \$ 1,160 | \$ 1,260 | \$ 1,226 |
| | ----- | ----- | ----- | ----- |
| Charge-offs: | | | | |
| Commercial, financial and agricultural | 0 | 0 | 1 | 0 |
| Real estate mortgage | 13 | 21 | 243 | 53 |
| Consumer | 88 | 50 | 25 | 52 |
| | ----- | ----- | ----- | ----- |
| Total charge-offs | 101 | 71 | 269 | 112 |
| | ----- | ----- | ----- | ----- |
| Recoveries: | | | | |
| Commercial, financial and agricultural | 0 | 0 | 0 | 0 |
| Real estate mortgage | 87 | 6 | 19 | 13 |
| Consumer | 17 | 17 | 30 | 13 |
| | ----- | ----- | ----- | ----- |
| Total recoveries | 104 | 23 | 49 | 26 |
| | ----- | ----- | ----- | ----- |
| Net charge-offs | (3) | 48 | 220 | 86 |
| Provisions charges to operations | 150 | 180 | 120 | 120 |
| | ----- | ----- | ----- | ----- |
| Balance at end of year | \$ 1,445 | \$ 1,292 | \$ 1,160 | \$ 1,260 |
| | ===== | ===== | ===== | ===== |
| Ratio of net charge-offs to average loans outstanding | (.002%) | .04% | .18% | .07% |
| Ratio of allowance for loan losses to year end loans | 1.01% | .93% | .93% | 1.05% |

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Allocation of the Allowance for Loan Losses
(dollars in thousands)

| | 2001 | | 2000 | | Years Ended December 31 1999 | | |
|---|--------|---------|--------|---------|------------------------------|---------|--------|
| | Amount | Percent | Amount | Percent | Amount | Percent | Amount |
| | ----- | ----- | ----- | ----- | ----- | ----- | ----- |
| Commercial, financial and agricultural | \$ 120 | 7.47% | \$ 160 | 6.16% | \$ 160 | 7.19% | \$ 1 |
| Real estate construction and land development | 24 | 2.72% | 0 | 4.50% | 0 | 2.70% | |
| Real estate mortgage | 1,200 | 82.78% | 1,066 | 81.51% | 941 | 81.30% | 9 |

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| | | | | | | | |
|-------------|---------|---------|---------|---------|---------|---------|-------|
| Consumer | 100 | 6.94% | 65 | 7.65% | 58 | 8.52% | |
| Other loans | 1 | .09% | 1 | .18% | 1 | .29% | |
| | ----- | ----- | ----- | ----- | ----- | ----- | ----- |
| | \$1,445 | 100.00% | \$1,292 | 100.00% | \$1,160 | 100.00% | \$1,2 |
| | ===== | ===== | ===== | ===== | ===== | ===== | ===== |

Provisions to the allowance for possible loan losses are charged to operating expenses and are based on past experience, current economic conditions and management's judgement of the amount necessary to cover possible losses on the collection of loans. The Bank records provisions for estimated loan losses, which are charged against earnings, in the period they are established.

Short-Term Borrowings
(dollars in thousands)

| | December 31 | | |
|--|-------------|----------|----------|
| | 2001 | 2000 | 1999 |
| | ---- | ---- | ---- |
| Federal Home Loan Bank Advances | | | |
| Average interest rate | | | |
| At year end | 5.95% | 5.93% | 5.19% |
| For the year | 5.62% | 5.81% | 5.19% |
| Average amount outstanding during the year | \$53,407 | \$49,291 | \$35,954 |
| Maximum amount outstanding at any month | \$56,766 | \$58,605 | \$42,038 |
| Amount outstanding at year end | \$53,004 | \$47,357 | \$39,712 |

ITEM 2. DESCRIPTION OF PROPERTIES

The Company is not the owner or lessee of any properties. The Bank does not lease any properties. The properties described below are owned by the Bank.

The Bank serves its customers from its four (4) offices which are located in Canaan, Lakeville, Salisbury and Sharon, Connecticut. The Bank's trust department is located in a separate building adjacent to the main office of the Bank.

The following table includes all property owned by the Bank, but does not include Other Real Estate Owned.

| OFFICES | LOCATION | STATUS |
|------------------|---|--------|
| Main Office | 5 Bissell Street Lakeville, Connecticut | Owned |
| Trust Department | 19 Bissell Street Lakeville, Connecticut | Owned |
| Salisbury Office | 18 Main Street Salisbury, Connecticut | Owned |
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| Sharon Office | 29 Low Road Sharon, Connecticut | Owned |
| Canaan Office | 94 Main Street Canaan, Connecticut | Owned |

ITEM 3. LEGAL PROCEEDINGS

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Other than routine litigation incidental to its business, there are no material legal proceedings pending to which the Company, Bank, or their properties are subject.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

No matters were submitted to a vote of security holders during the fourth quarter of the Company's 2001 fiscal year.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

(a) Market Information

The Company's common stock is traded on The American Stock Exchange under the symbol "SAL". The following table presents the high and low sales prices of the Company's common stock.

| | 2001 Quarters | | | | 2000 | |
|------------------------|---------------|---------|---------|---------|---------|---------|
| | 4th | 3rd | 2nd | 1st | 4th | 3rd |
| Range of Stock prices: | | | | | | |
| High | \$23.60 | \$24.25 | \$20.00 | \$19.00 | \$18.50 | \$17.50 |
| Low | \$20.79 | \$19.70 | \$19.00 | \$18.00 | \$17.25 | \$17.00 |

(b) Holders

There were approximately 519 holders of stock as of March 8, 2002. This number includes brokerage firms and other financial institutions which hold stock in their name but which is actually owned by third parties. The Company is not provided with the number or identities of these parties.

(c) Dividends

Dividends are currently declared four (4) times a year, and the Company expects to follow such practices in the future. During the year 2001, Salisbury Bancorp, Inc. declared a cash dividend each quarter of \$.21 per share. Dividends for the year 2001 totaled \$.84 per share which compared to total dividends of \$.77 that were declared in the year 2000. At their February 25, 2002 meeting, the Directors of Salisbury Bancorp, Inc. declared a cash dividend of \$.22 per share for the first quarter of 2002. The dividend will be paid on April 26, 2002 to shareholders of record as of March 29, 2002. Payment of all dividends are dependent upon the condition and earnings of the Company. The Company's ability to pay dividends is limited by the prudent banking principles applicable to all bank holding companies and by the provisions of Connecticut Corporate law, which provide that no distribution may be made by a company if, after giving it effect: (1) the company would not be able to pay its debts as they become due in the usual course of business or (2) the company's total assets would be less than the sum of its total liabilities plus amounts needed to satisfy any preferred stock rights. The following table presents cash dividends declared per share for the last two (2) years:

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| | 2001 Quarters | | | | 2000 | |
|----------------------------|---------------|--------|--------|--------|--------|--------|
| | 4th | 3rd | 2nd | 1st | 4th | 3rd |
| Cash dividends declared | \$0.21 | \$0.21 | \$0.21 | \$0.21 | \$0.38 | \$0.13 |

The dividends paid to shareholders of the Company are funded primarily from dividends received by the Company from the Bank. Reference should be made to Note 12 of the Consolidated Financial Statements for a description of restrictions on the ability of the Bank to pay dividends to the Company.

ITEM 6. MANAGEMENT'S DISCUSSION AND ANALYSIS Salisbury Bancorp, Inc. And Subsidiary

OVERVIEW

The following provides management's comments on the financial condition and results of operations of Salisbury Bancorp, Inc. (the "Company"), a Connecticut corporation which is the holding company for Salisbury Bank and Trust Company, (the "Bank"). The Company's sole subsidiary is the Bank, which has four (4) full service offices including a Trust Department located in the towns of Canaan, Lakeville, Salisbury and Sharon, Connecticut. The Company and the Bank were formed in 1998 and 1848, respectively. This discussion should be read in conjunction with the Company's consolidated financial statements and the notes to the consolidated financial statements that are presented as part of this Annual Report.

In order to provide a strong foundation for building shareholder value and to serve its customers, the Company remains committed to investing in the technological and human resources necessary to implement new personalized financial products and to deliver them with the highest quality of service. To that end, in 2001, the Bank launched a new internet banking product called "SBTNET" and acquired a branch in Canaan, Connecticut. This new branch has added banking convenience for our Canaan area customers and, with deposits of \$26,811,000 as of December 31, 2001, offers a solid base for expanding the Bank's operation in that area.

Earnings for the Company amounted to \$2,901,000 in 2001, a 1.83% increase over year 2000 earnings of \$2,849,000. Earnings per diluted share increased 5.73% to \$2.03 per share for 2001 compared to a \$1.92 for 2000.

The growth in net income and earnings per share during 2001 reflect an increase in average earning assets and noninterest income, the continuing efforts of management to control operating expenses, and the reduced number of shares outstanding as a result of stock repurchases.

The Company's risk-based capital ratios at December 31, 2001, which includes the risk-weighted assets and capital of the Salisbury Bank and Trust Company were 15.09% for Tier 1 capital and 16.21% for total capital. The Company's leverage ratio was 7.61% at December 31, 2001.

As a result of the Company's financial performance, the Board of Directors increased the dividends declared on the Company's common stock to \$.84 per share in 2001, compared to \$.77 per share in 2000.

FINANCIAL CONDITION

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COMPARISON OF DECEMBER 31, 2001 AND 2000

Total assets at December 31, 2001 were \$283,602,000 compared to \$249,054,000 at December 31, 2000, an increase of \$34,548,000 or 13.87%. This growth is primarily attributable to the Bank's purchase of People's Bank Canaan branch office that was completed during September 2001. In connection with this transaction, the Bank assumed approximately \$26,000,000 in deposits, received approximately \$120,000 in loans and \$272,000 in fixed assets.

SECURITIES PORTFOLIO

As of December 31, 2001, the securities portfolio, including Federal Home Loan Bank of Boston stock, totaled \$105,593,000. This represents an increase of \$13,671,000 or 14.87% when compared to \$91,922,000 at year-end 2000. The Company manages the securities portfolio in accordance with the investment policy adopted by the Board of Directors. The primary objectives are to earn interest and dividend income, provide liquidity to meet cash flow needs and to manage

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interest rate risk and asset-quality diversification to the Company's assets. The securities portfolio also acts as collateral for deposits of public agencies. The Company continues to use arbitrage strategy by borrowing funds and investing them at a rate of return higher than the borrowing cost in order to generate additional interest income. This strategy contributes to the growth in the portfolio. The growth in the securities portfolio however, is primarily the result of increased investing activities resulting from the cash received from the purchase of the Canaan branch.

The primary component of the total portfolio is U.S. Government sponsored agencies, which account for 34.72% of the portfolio at December 31, 2001 compared to 48.70% at December 31, 2000. This decrease from year-end 2000 is the result of Management's efforts to increase after tax earnings by increasing investment activity in tax-exempt municipal investments. The remaining portion of the portfolio primarily consists of mortgage-backed securities. At December 31, 2001, securities totaling \$102,248,000 were classified as available-for-sale and securities totaling \$400,000 were classified as held-to-maturity.

As of January 1994, the Company adopted Statement of Financial Accounting Standards No. 115, "Accounting for Certain Investments in Debt and Equity Securities." This resulted in new classifications of the securities in the portfolio; Securities-Available-for-Sale, and Securities-Held-to-Maturity. The securities reported as available-for-sale are stated at fair value in the financial statements of the Company. Unrealized holding losses and gains (accumulated other comprehensive income/loss) are not included in earnings, but are reported as a net amount (less expected tax) in a separate component of capital until realized. At December 31, 2001, the unrealized loss net of tax was \$279,000 compared to an unrealized loss net of tax of \$171,000 at December 31, 2000. The securities reported as securities-held-to-maturity are stated at amortized cost.

FEDERAL FUNDS SOLD

The balance of federal funds sold totaled \$18,150,000 at December 31, 2001. This compares to \$5,125,000 at December 31, 2000. This increase is primarily the result of the cash received with the acquisition of the new Canaan branch. Although this total is somewhat higher than the Bank's normal operating range of funds for daily cash needs, some of the funds are being invested in the securities portfolio while others will fund loans.

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LENDING

Loans receivable, net of allowance for loan losses increased \$4,796,000 to \$143,066,000 at December 31, 2001 or 3.47% compared to \$138,270,000 at December 31, 2000. The Company's credit function is designed to insure adherence to prudent credit standards despite competition for loans in the Company's market area. The Company offers a wide variety of loan types and terms along with competitive pricing to customers, although the largest dollar volumes of loan growth continue to be in the residential mortgage area. For the year ending December 31, 2001, residential mortgages increased \$3,889,000 or 3.96% to \$102,201,000. This compares to residential mortgages that totaled \$98,312,000 at December 31, 2000. This increase is primarily the result of continuing efforts to develop new personalized financial products and services designed to meet the needs of our customers.

PROVISIONS AND ALLOWANCE FOR LOAN LOSSES

Total loans at December 31, 2001 were \$144,511,000, which compares to total loans of \$139,562,000 at December 31, 2000. This is an increase of \$4,949,000 or 3.55%. While the Bank's loan portfolio continues to grow, the Bank monitors the quality of the portfolio to ensure that loan quality will not be sacrificed for growth or otherwise compromise the Company's objectives. At December 31, 2001 approximately 86% of the Bank's loan portfolio was related to real estate products and although the portfolio increased during the year 2001, the concentration remained consistent as approximately 86% of the portfolio was related to real estate at December 31, 2001. There were no material changes in the composition of the loan portfolio during this period.

Credit risk is inherent in the business of extending loans. The Company maintains an allowance or reserve for credit losses through charges to earnings. The loan loss provision for the year 2001 was \$150,000 as compared to \$180,000 for the year ended December 31, 2000.

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The Bank evaluates the adequacy of the allowance on a monthly basis. No material changes have been made in the estimation methods or assumptions that the Bank uses in making this determination during the year ended December 31, 2001. Such evaluations are based on assessments of credit quality and "risk rating" of loans by senior management, which is submitted to the Board of Directors for approval. Loans are initially risk rated when originated. If there is deterioration in the credit, the risk rating is adjusted accordingly.

The allowance also includes a component resulting from the application of the measurement criteria of Statements of Financial Accounting Standards No. 114, Accounting by Creditors for Impairment of a Loan ("SFAS114"). Impaired loans receive individual evaluation of the allowance necessary on a monthly basis. Impaired loans are defined in the Bank's Loan Policy as residential real estate mortgages with balances of \$300,000 or more and commercial loans of \$100,000 or more when it is probable that the Bank will not be able to collect all principal and interest due according to the terms of the note. Any such commercial loans and residential mortgages will be considered impaired under any of the following circumstances:

1. Non-accrual status;
2. Loans over 90 days delinquent;
3. Troubled debt restructures consummated after December 31, 1994; or
4. Loans classified as "doubtful", meaning that they have weaknesses, which make collection or liquidation in full, on the basis of currently

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existing facts, conditions, and values, highly questionable and improbable.

The individual allowance for any impaired loan is based upon the present value of expected future cash flows discounted at the loan's effective interest rate or the fair value of the collateral if the loan is collateral dependent. Specifically identifiable and quantifiable losses are immediately charged off against the allowance.

In addition, a risk of loss factor is applied in evaluating categories of loans generally as part of the periodic analysis of the Allowance for Loan Losses. This analysis reviews the allocations of the different categories of loans within the portfolio and it considers historical loan losses and delinquency figures as well as any recent delinquency trends.

The credit card delinquency and loss history is separately evaluated and given a special loan loss factor because management recognizes the higher risk involved in such loans. Concentrations of credit and local economic factors are also evaluated on a periodic basis. Historical average net losses by loan type are examined as well as trends by type. The Bank's loan mix over the same period of time is also analyzed. A loan loss allocation is made for each type of loan multiplied by the loan mix percentage for each loan type to produce a weighted average factor. There have been no reallocations within the allowance during the year ended December 31, 2001.

At December 31, 2001, the allowance for loan losses totaled \$1,445,000, representing 246.17% of nonperforming loans, which totaled \$587,000, and 1.00% of total loans of \$144,511,000. This compared to \$1,292,000 representing 247.99% of nonperforming loans, which totaled \$521,000 and .93% of total loans of \$139,562,000 at December 31, 2000. Management does not believe that the increase of \$66,000 in nonperforming loans represents any trend towards increased delinquency of loans, which would be likely to have an effect on the adequacy of the allowance for loan losses. While a total of \$101,000 loans were charged off during the year 2001, as compared to \$71,000 during 2000, a total of \$104,000 of previously charged off loans was recovered during the year ended December 31, 2001. Recoveries for the year 2000 totaled \$23,000. When comparing the two years, net charge-offs were \$48,000 for the year 2000 and during the year 2001 net recoveries exceeded charge offs by \$3,000. The \$51,000 difference in net recoveries more than compensated for the \$30,000 reduction in provisions during 2001. Management believes that the allowance for loan losses is adequate. While management estimates loan losses using the best available information, no assurances can be given that future additions to the allowance will not be necessary based on changes in economic and real estate market conditions, further information obtained regarding problem loans, identification of additional problem loans or other factors. Additionally, with expectations of the Company to grow its existing portfolio, future additions to the allowance may be necessary to maintain adequate coverage ratios.

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DEPOSITS

The Company offers a variety of deposit accounts with a range of interest rates and terms. Deposits at year-end 2001 totaled \$201,351,000 compared to \$166,436,000 at year-end 2000. This increase of \$34,915,000 or 20.98% can be primarily attributed to the acquisition of the Canaan branch as previously mentioned where the Company acquired approximately \$26,000,000 in deposits as part of that transaction. Ongoing efforts of the Company to develop and maintain relationship banking with its customers coupled with competitively priced products has also been a contributing factor in the growth of deposits. The flow

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of deposits is influenced significantly by general economic conditions, changes in money market rates, prevailing interest rates and the aggressive competition from nonbanking entities. During the year, there was an increase in savings and money market accounts which are lower cost core deposits.

The average daily amount of deposits by category and the average rates paid on such deposits are summarized in the following table:

(dollars in thousands)

| | Year ended December 31 | | | | | |
|--------------|------------------------|-------|--------------------|-------|--------------------|-------|
| | 2001 | | 2000 | | 1999 | |
| | Average Balance | Rate | Average Balance | Rate | Average Balance | Rate |
| | ----- | ---- | ----- | ---- | ----- | ---- |
| Demand | \$ 31,497 | | \$ 31,522 | | \$ 30,024 | |
| NOW | 17,185 | 1.07% | 16,246 | 1.06% | 16,400 | 2.03% |
| Money Market | 50,331 | 3.41% | 43,975 | 4.71% | 36,782 | 3.67% |
| Savings | 16,674 | 2.37% | 15,691 | 2.43% | 15,315 | 2.43% |
| Time | 60,854 | 4.94% | 53,781 | 5.20% | 58,933 | 4.99% |
| | ----- | | ----- | | ----- | |
| | \$176,541 | 3.00% | \$161,215 | 3.36% | \$157,454 | 3.07% |
| | ===== | | ===== | | ===== | |

Maturities of time certificates of deposits of \$100,000 or more outstanding for the years ended December 31 are summarized as follows:

(dollars in thousands)

| | Year Ended December 31 | | |
|--------------------------------------|------------------------|----------|----------|
| | 2001 | 2000 | 1999 |
| | ----- | ----- | ----- |
| Three months or less | \$ 3,895 | \$ 3,355 | \$ 2,296 |
| Over three months through six months | 4,161 | 4,351 | 4,120 |
| Over six months through one year | 4,398 | 7,105 | 5,194 |
| Over one year | 5,708 | 2,088 | 3,294 |
| | ----- | ----- | ----- |
| Total | \$18,162 | \$16,899 | \$14,904 |
| | ===== | ===== | ===== |

BORROWINGS

As part of its operating strategy, the Company utilizes advances from the Federal Home Loan Bank to supplement deposit growth and fund its asset growth, a strategy which is designed to increase interest income. These advances are made pursuant to various credit programs, each of which has its own interest rate and range of maturities. At December 31, 2001, the Company had \$53,004,000 in outstanding advances from the Federal Home Loan Bank compared to \$47,357,000 at December 31, 2000. Management expects that it will continue this strategy of supplementing deposit growth with advances from the Federal Home Loan Bank of Boston.

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INTEREST RATE RISK

Interest rate risk is the most significant market risk affecting the Company. Interest rate risk is defined as an exposure to a movement in interest rates that could have an adverse effect on net interest income. Net interest income is sensitive to interest rate risk to the degree that interest bearing liabilities mature or reprice on a different basis than earning assets.

In an attempt to manage its exposure to changes in interest rates, the Bank's assets and liabilities are managed in accordance with policies established and reviewed by the Bank's Board of Directors. The Bank's Asset/Liability Management Committee monitors asset and deposit levels, developments and trends in interest rates, liquidity and capital. One of the primary financial objectives is to manage interest rate risk and control the sensitivity of earnings to changes in interest rates in order to prudently improve net interest income and manage the maturities and interest rate sensitivities of assets and liabilities.

To quantify the extent of these risks both in its current position and in actions it might take in the future, interest rate risk is monitored using gap analysis which identifies the differences between assets and liabilities which mature or reprice during specific time frames and model simulation which is used to "rate shock" the Company's assets and liability balances to measure how much of the Company's net interest income is "at risk" from sudden rate changes.

At December 31, 2001 the Company was slightly asset sensitive, however, the level of interest rate risk is within the limits approved by the Board of Directors.

LIQUIDITY

Liquidity is the ability to raise funds on a timely basis at an acceptable cost in order to meet cash needs. Adequate liquidity is necessary to handle fluctuation in deposit levels, to provide for customers' credit needs, and to take advantage of investment opportunities as they are presented. The Company manages liquidity primarily with readily marketable investment securities, deposits and loan repayments. The Company's subsidiary, Salisbury Bank and Trust Company is a member of the Federal Home Loan Bank of Boston. This enhances the liquidity position by providing a source of available borrowings.

At December 31, 2001, the Company had approximately \$27,232,000 in loan commitments outstanding. Management believes that the current level of liquidity is ample to meet the Company's needs for both the present and foreseeable future.

CAPITAL

At December 31, 2001, the Company had \$23,363,000 in shareholder equity compared to \$22,460,000 at December 31, 2000. This represents an increase of \$903,000 or 4.02%. Several components contributed to the change since December 2000. Earnings for the year totaled \$2,901,000. Market conditions have resulted in a negative adjustment to unrealized comprehensive income of \$108,000. The Company declared dividends in 2001 resulting in a decrease in capital of \$1,199,000. During 2001, the Company repurchased 36,008 shares of stock which reduced capital in the amount of \$691,000. Under current regulatory definitions, the Company and the Bank are considered to be "well capitalized" for capital adequacy purposes. As a result, the Bank pays the lowest federal deposit insurance deposit premiums possible. One primary measure of capital adequacy for

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regulatory purposes is based on the ratio of risk-based capital to risk weighted assets. This method of measuring capital adequacy helps to establish capital requirements that are more sensitive to the differences in risk associated with various assets. It takes in account off-balance sheet exposure in assessing capital adequacy and it minimizes disincentives to holding liquid, low risk assets. At year-end 2001, the Company had a risk-based capital ratio of 16.21% compared to 20.05% at December 31, 2000. The decrease is the result of the activity in the Company's stock buy back program during the year as well as the impact on the risk-based capital resulting from the acquisition of the Canaan branch as mentioned previously. Despite the decrease from the prior year end, the Company's ratio of total capital to risk rated assets of 16.21% substantially exceeds all applicable requirements for "well capitalized" institutions.

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Maintaining strong capital is essential to bank safety and soundness. However, the effective management of capital resources requires generating attractive returns on equity to build value for shareholders while maintaining appropriate levels of capital to fund growth, meeting regulatory requirements and being consistent with prudent industry practices. Management believes that the capital ratios of the Company and Bank are adequate to continue to meet the foreseeable capital needs of the institution.

RESULTS OF OPERATIONS COMPARISON BETWEEN 2001 AND 2000

NET INTEREST INCOME

The Company earns income from two basic sources. The primary source is through the management of its financial assets and liabilities and the second is by charging fees for services provided. The first involves functioning as a financial intermediary. The Company accepts funds from depositors or borrows funds and then either lends the funds to borrowers or invests those funds in various types of securities. The second is fee income, which is discussed in the noninterest income section of this analysis. Net interest income is the difference between the interest and fees earned on loans and securities (the Company's earning assets) and the interest expense paid on deposits and borrowed funds, primarily in the form of advances from the Federal Home Loan Bank. The amount by which interest income will exceed interest expense depends on two factors: (1) the volume or balance of earning assets compared to the volume or balance of interest-bearing deposits and borrowed funds and (2) the interest rate earned on those interest earning assets compared with the interest rate paid on those interest-bearing deposits and borrowed funds. For this discussion, net interest income is presented on a fully taxable-equivalent ("FTE") basis. FTE interest income restates reported interest income on tax exempt loans and securities as if such interest were taxed at the applicable State and Federal income tax rates for all periods presented.

| (dollars in thousands) | 2001 | December 31 2000 | 1999 |
|---|-----------|---------------------|-----------|
| | ----- | ----- | ----- |
| Interest Income (financial statements) | \$ 17,089 | \$ 16,510 | \$ 14,524 |
| Tax Equivalent Adjustment | 504 | 335 | 295 |

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| | | | |
|-------------------------|----------|----------|----------|
| Interest Expense | (8,300) | (8,284) | (6,683) |
| | ----- | ----- | ----- |
| Net Interest Income-FTE | \$ 9,293 | \$ 8,561 | \$ 8,136 |
| | ===== | ===== | ===== |

The Company's 2001 interest income-FTE of \$17,089,000 was \$579,000 or 3.51% greater than 2000. This is primarily the result of an increase in average earning assets of \$19,444,000 or 8.61% during 2001. Interest expense increased \$16,000 to \$8,300,000 in 2001. Although average deposits increased \$15,441,000 or 11.91% and average advances from the Federal Home Loan Bank increased \$4,116,000 or 8.35%, an environment of generally lower rates resulted in the minimal increase in interest expense for the year 2001. Overall, net interest income-FTE increased 8.55% to \$9,293,000 in 2001 compared to \$8,561,000 in 2000.

Net interest margin is net interest income expressed as a percentage of average earning assets. It is used to measure the difference between the average rate of interest earned on assets and the average rate of interest that must be paid to support those assets. To maintain its net interest margin, the Company must manage the relationship between interest earned and paid. The Company's 2001 net interest margin (FTE) of 3.79% was the same as that in 2000. Although interest margins continue to be pressured by aggressive competition, increased volumes of deposits and borrowings have resulted in the increase in net interest and dividend income on a fully taxable equivalent basis.

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YIELD ANALYSIS

Average Balances, Interest Earned and Rates Paid

| (dollars in thousands) | 2001 | | | Year Ended December 31 2000 | | |
|--|--------------------|------------------------------|----------------|--------------------------------|------------------------------|----------------|
| | AVERAGE BALANCE | INTEREST EARNED/ PAID* | YIELD RATE* | AVERAGE BALANCE | INTEREST EARNED/ PAID* | YIELD RATE* |
| | ----- | ----- | ----- | ----- | ----- | ----- |
| ASSETS | | | | | | |
| Interest earning assets: | | | | | | |
| Loans | \$145,502 | \$11,344 | 7.80% | \$129,972 | \$10,494 | 8.07% |
| Taxable Securities | \$68,921 | \$4,422 | 6.42% | \$73,958 | \$4,810 | 6.50% |
| Tax-Exempt securities | \$20,030 | \$1,481 | 7.39% | \$13,160 | \$987 | 7.50% |
| Federal Funds | \$9,986 | \$310 | 3.10% | \$8,382 | \$533 | 6.36% |
| Other Interest Income | \$809 | \$36 | 4.45% | \$332 | \$21 | 6.33% |
| | ----- | ----- | ----- | ----- | ----- | ----- |
| Total interest earning | \$245,248 | \$17,593 | 7.17% | \$225,804 | \$16,845 | 7.46% |
| | | ===== | | | ===== | |
| assets | | | | | | |
| Allowance for loan losses | (\$1,412) | | | (\$1,187) | | |
| Cash & due from Banks | \$5,138 | | | \$5,040 | | |
| Premise, Equipment | \$2,676 | | | \$2,425 | | |
| Net unrealized gain/loss on AFS Securities | \$500 | | | (\$2,803) | | |

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| | | |
|----------------------|-----------|-----------|
| Other Assets | \$3,312 | \$3,281 |
| | ----- | ----- |
| Total Average Assets | \$255,462 | \$232,560 |
| | ===== | ===== |

LIABILITIES AND
SHAREHOLDERS'
EQUITY

Interest Bearing
Liabilities:

Now/Money Market

| | | | | | | |
|------------------|----------|---------|-------|----------|---------|-------|
| Deposits | \$67,516 | \$1,901 | 2.82% | \$60,221 | \$2,245 | 3.73% |
| Savings Deposits | \$16,674 | \$396 | 2.37% | \$15,691 | \$382 | 2.43% |
| Time Deposits | \$60,854 | \$3,004 | 4.94% | \$53,781 | \$2,794 | 5.20% |
| Borrowed Funds | \$53,407 | \$2,999 | 5.62% | \$49,291 | \$2,863 | 5.81% |
| | ----- | ----- | ---- | ----- | ----- | ---- |

Total Interest Bearing
Liabilities

| | | | | | |
|-----------|---------|-------|-----------|---------|-------|
| \$198,451 | \$8,300 | 4.18% | \$178,984 | \$8,284 | 4.63% |
| | ----- | | ----- | | |

Demand Deposits

| | |
|----------|----------|
| \$31,497 | \$31,522 |
|----------|----------|

Other Liabilities

| | |
|---------|---------|
| \$1,829 | \$1,167 |
|---------|---------|

Shareholders' Equity

| | |
|----------|----------|
| \$23,685 | \$20,887 |
| ----- | ----- |

Total Liabilities and
Equity

| | |
|-----------|-----------|
| \$255,462 | \$232,560 |
| ===== | ===== |

Net Interest Income

| | |
|---------|---------|
| \$9,293 | \$8,561 |
| ===== | ===== |

Net Interest Spread

| | |
|-------|-------|
| 2.99% | 2.83% |
|-------|-------|

Net Interest Margin

| | |
|-------|-------|
| 3.79% | 3.79% |
|-------|-------|

* Annualized

Consolidated

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Volume and Rate Variance Analysis of Net Interest Income
(Taxable equivalent basis)

(dollars in thousands)

| | 2001 over 2000 | | | 2000 over | |
|----------------------------------|----------------|----------|----------|-----------|-------|
| | Volume | Rate | Total | Volume | Rat |
| | ----- | ----- | ----- | ----- | ----- |
| Increase (decrease) in: | | | | | |
| Interest income on: | | | | | |
| Loans | \$ 1,253 | \$ (403) | \$ 850 | \$ 531 | \$ 3 |
| Taxable investment securities | (327) | (61) | (388) | 525 | 2 |
| Tax-exempt investment securities | 515 | (21) | 494 | 116 | |
| Other interest income | 132 | (340) | (208) | 101 | 1 |
| Total interest income | \$ 1,573 | \$ (825) | \$ 748 | \$ 1,273 | \$ 7 |
| | ----- | ----- | ----- | ----- | ----- |
| Interest expense on: | | | | | |
| NOW/Money Market deposits | \$ 272 | \$ (616) | \$ (344) | \$ 202 | \$ 5 |
| Savings deposits | 24 | (10) | 14 | 9 | |

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| | | | | | |
|------------------------|--------|----------|--------|--------|-------|
| Time deposits | 368 | (158) | 210 | (258) | 1 |
| Borrowed funds | 239 | (103) | 136 | 711 | 3 |
| | ----- | ----- | ----- | ----- | ----- |
| Total interest expense | \$ 903 | \$ (887) | \$ 16 | \$ 664 | \$ 9 |
| | ----- | ----- | ----- | ----- | ----- |
| Net interest margin | \$ 670 | \$ 62 | \$ 732 | \$ 609 | \$ (1 |
| | ===== | ===== | ===== | ===== | ===== |

NONINTEREST INCOME

Fees earned by the Trust Department remain the largest component of noninterest income and amounted to \$1,070,000 in 2001. This compares to \$1,108,000 for the corresponding period in 2000. A significant portion of trust fee income is based upon the value of assets under management, and, as such, the calculation of fees is influenced by the value of the markets at the time of assessment. During the year 2001, as a result of this decline in stock market values, trust fee income decreased from year 2000 levels. Estate settlement fees also contribute to trust department income. Although the timing of the receipt of the fee is difficult to predict, the overall volume of business for 2001 and 2000 was very comparable. Other noninterest income increased \$467,000 to \$1,317,000 for the year ended compared to \$850,000 for the same period in 2000. Service charges on deposit accounts increased \$78,000 or 23.08% to \$416,000 compared to \$338,000 for the same period in 2001. Growth in demand deposit and NOW accounts generated an increase in transaction volumes resulting in increased fees. As a result of investment activities in the securities portfolio during the year the Company recorded gains on sales of available-for-sale securities of \$130,000. This compared to recorded losses of (\$64,000) for the year ended December 31, 2000. This represents an increase of \$194,000 when comparing the two years. An economic environment of generally lower interest rates resulted in significant activity in mortgage refinancing and was the primary result of the increase in fees generated from the sale of loans held-for-sale to \$184,000 for the year ended December 31, 2001. This is an increase of \$111,000 or 152.05% over a total of \$73,000 earned for the year ended December 31, 2000. Other noninterest income increased \$84,000 or 16.70% to \$587,000 from \$503,000 for the year ended December 31, 2001 as compared to the same period in 2000. The Company's VISA credit card program and Master Money Debit Card program grew during 2001, resulting in increased transaction fees. The Company continues to seek to increase noninterest income due to its importance as a potential contributor to profitability.

NONINTEREST EXPENSE

Noninterest expense totaled \$6,755,000 in 2001. This is an increase of \$958,000 when compared to total noninterest expense of \$5,797,000 in 2000. However, as a percentage of total average earning assets, these expenses have remained generally consistent at 2.75% in 2001 and 2.57% in 2000. Salaries and employee benefits increased \$439,000 or 12.92%. This is primarily the result of the additional staff hired to service the increase in new business coupled with annual pay increases and increasing costs of employee benefits. Occupancy and equipment expenses increased 12.54% to \$733,000 from \$651,000. The increases in these expenses were costs primarily associated with the acquisition of the new Canaan branch as mentioned previously. During 2001 data processing expenses decreased 14.34% to \$247,000 from \$288,000 as a result of the renegotiation of various data processing agreements with vendors. Insurance expenses for the year 2001, which do not include insurance benefits associated with employees, decreased \$14,000 or 13.21% to \$92,000 from \$106,000, as a result of the Company's claim experience and management's renegotiation of various renewal

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premiums on policies. Printing and stationery costs increased \$29,000 or 19.33% to \$179,000 for the year ended December 31, 2001 compared to \$150,000 for the year 2000. This is the result of the need for new forms and documentation relating primarily to either new regulatory requirements or the new office in Canaan. Amortization of intangible assets from branch acquisitions is a new expense to the Company that is associated with the Canaan branch acquisition. For the year ended December 31, 2001 the expense totaled \$48,000. Other operating expenses increased \$423,000 or 37.07% to \$1,564,000 from \$1,141,000 when comparing the two years. This is primarily the result of additional costs related to the Canaan branch.

INCOME TAXES

In 2001, the Company's tax expense was \$1,370,000, an effective tax rate of 32.08%. This compares to income tax expense of \$1,357,000 in 2000, reflecting an effective tax rate of 32.26%. This is primarily the result of the impact of an increase in tax-exempt interest income earned from the securities portfolio.

NET INCOME

Overall, net income totaled \$2,901,000 for the year ended December 31, 2001, compared to net income of \$2,849,000 for the year 2000. This was an increase of \$52,000 or 1.83% and reflects earnings of \$2.03 per diluted share for the year, compared to earnings per diluted share of \$1.92 for the same period in 2000.

IMPACT OF INFLATION AND CHANGING PRICES

The Company's consolidated financial statements are prepared in conformity with generally accepted accounting principles which require the measurement of financial condition and operating results in terms of historical dollars without considering changes in the relative purchasing power of money, over time, due to inflation. Unlike most industrial companies, virtually all of the assets and liabilities of the Company are monetary and as a result, interest rates have a greater impact on the Company's performance than do the effects of general levels of inflation; although they do not necessarily move in the same direction or with the same magnitude as the prices of goods and services. Although not an influence in recent years, inflation could impact earnings in future periods.

FORWARD LOOKING STATEMENTS

This form 10-KSB and future filings made by the Company with the Securities and Exchange Commission, as well as other filings, reports and press releases made or issued by the Company and the Bank, and oral statements made by executive officers of the Company and Bank, may include forward-looking statements relating to such matters as (a) assumptions concerning future economic and business conditions and their effect on the economy in general and on the markets in which the Company and the Bank do business and (b) expectations for revenues and earnings for the Company and Bank through growth resulting from attraction of new deposit and loan customers and the introduction of new products and services. Such forward-looking statements are based on assumptions rather than historical or current facts and, therefore, are inherently uncertain and subject to risk. For those statements, the Company claims the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995.

The Company notes that a variety of factors could cause the actual results or experience to differ materially from the anticipated results or other expectations described or implied by such forward-looking statements. The risks and uncertainties that may affect the operations, performance, development and results of the Company's and Bank's business include the following: (a) the risk of adverse changes in business conditions in the banking industry generally and

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in the specific markets in which the Bank operates; (b) changes in legislative and regulatory environment that negatively impact the Company and Bank through increased operating expenses; (c) increased competition from other financial and non-financial institutions; (d) the impact of technological advances; and (e) other risks detailed from time to time in the Company's filings with the Securities and Exchange Commission.

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STATEMENT OF MANAGEMENT'S RESPONSIBILITY

Management is responsible for the integrity and objectivity of the financial statements and other information appearing in this Annual Report. The financial statements were prepared in accordance with generally accepted accounting principles applying estimates and Management's best judgement as required. To fulfill their responsibilities, Management establishes and maintains accounting systems and practices adequately supported by internal accounting controls. These controls include the selection and training of management and supervisory personnel; an organization structure providing for delegation of authority and establishment of responsibilities; communication of requirements for compliance with approved accounting, control and business practices throughout the organization; business planning and review; and a program of internal audit. Management believes the internal accounting controls in use provide reasonable assurance that assets are safeguarded, that transactions are executed in accordance with Management's authorization and that financial records are reliable for the purpose of preparing financial statements.

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ITEM 7. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

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Salisbury Bancorp, Inc. (parent company only)

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To the Board of Directors
Salisbury Bancorp, Inc.
Lakeville, Connecticut

INDEPENDENT AUDITORS' REPORT

We have audited the accompanying consolidated balance sheets of Salisbury Bancorp, Inc. and Subsidiary as of December 31, 2001 and 2000 and the related consolidated statements of income, changes in stockholders' equity and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Salisbury Bancorp, Inc. and Subsidiary as of December 31, 2001 and 2000, and the consolidated results of their operations and their cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

/s/SHATSWELL, MacLEOD & COMPANY, P.C.

SHATSWELL, MacLEOD & COMPANY, P.C.

West Peabody, Massachusetts
January 28, 2002

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SALISBURY BANCORP, INC. AND SUBSIDIARY

CONSOLIDATED BALANCE SHEETS

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December 31, 2001 and 2000

| ASSETS | 2001 |
|--|----------------|
| Cash and due from banks | \$ 7,184,123 |
| Interest bearing demand deposits with other banks | 258,097 |
| Money market mutual funds | 617,461 |
| Federal funds sold | 18,150,000 |
| | ----- |
| Cash and cash equivalents | 26,209,681 |
| Investments in available-for-sale securities (at fair value) | 102,248,029 |
| Investments in held-to-maturity securities (fair values of \$401,403 as of December 31, 2001 and \$408,188 as of December 31, 2000) | 399,989 |
| Federal Home Loan Bank stock, at cost | 2,945,200 |
| Loans, net | 143,066,109 |
| Investment in real estate | 75,000 |
| Premises and equipment | 2,683,487 |
| Intangible assets on branch acquisition | 3,226,554 |
| Accrued interest receivable | 1,681,268 |
| Other assets | 1,067,143 |
| | ----- |
| Total assets | \$ 283,602,460 |
| | ===== |
| LIABILITIES AND STOCKHOLDERS' EQUITY | |
| Deposits: | |
| Noninterest-bearing | \$ 37,702,153 |
| Interest-bearing | 163,649,335 |
| | ----- |
| Total deposits | 201,351,488 |
| Federal Home Loan Bank advances | 53,003,746 |
| Due to broker 4,203,808 | 11,004,451 |
| Other liabilities | 1,680,272 |
| | ----- |
| Total liabilities | 260,239,314 |
| | ----- |
| Stockholders' equity: | |
| Common stock, par value \$.10 per share; authorized 3,000,000 shares; issued and outstanding, 1,422,358 shares in 2001 and 1,458,366 shares in 2000 | 142,236 |
| Paid-in capital | 2,281,415 |
| Retained earnings | 21,218,155 |
| Accumulated other comprehensive loss | (278,660) |
| | ----- |
| Total stockholders' equity | 23,363,146 |
| | ----- |
| Total liabilities and stockholders' equity | \$ 283,602,460 |
| | ===== |

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

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SALISBURY BANCORP, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF INCOME

Years Ended December 31, 2001 and 2000

| | 2001 | 2000 |
|---|---------------|---------------|
| | ----- | ----- |
| Interest and dividend income: | | |
| Interest and fees on loans | \$ 11,343,508 | \$ 10,494,188 |
| Interest and dividends on securities: | | |
| Taxable | 4,218,806 | 4,608,877 |
| Tax-exempt | 977,487 | 651,388 |
| Dividends on equity securities | 203,806 | 200,788 |
| Other interest | 345,784 | 554,511 |
| | ----- | ----- |
| Total interest and dividend income | 17,089,391 | 16,509,744 |
| | ----- | ----- |
| Interest expense: | | |
| Interest on deposits | 5,301,623 | 5,421,141 |
| Interest on Federal Home Loan Bank advances | 2,999,174 | 2,863,271 |
| | ----- | ----- |
| Total interest expense | 8,300,797 | 8,284,412 |
| | ----- | ----- |
| Net interest and dividend income | 8,788,594 | 8,225,322 |
| Provision for loan losses | 150,000 | 180,000 |
| | ----- | ----- |
| Net interest and dividend income after provision for loan losses | 8,638,594 | 8,045,322 |
| | ----- | ----- |
| Other income: | | |
| Trust department income | 1,070,017 | 1,108,241 |
| Service charges on deposit accounts | 416,060 | 337,700 |
| Gains (losses) on sales of available-for-sale securities, net | 130,117 | (63,971) |
| Gain on sale of loans held-for-sale | 183,618 | 72,711 |
| Other income | 587,325 | 502,991 |
| | ----- | ----- |
| Total other income | 2,387,137 | 1,957,691 |
| | ----- | ----- |
| Other expense: | | |
| Salaries and employee benefits | 3,833,838 | 3,395,161 |
| Occupancy expense | 246,549 | 233,100 |
| Equipment expense | 486,393 | 418,141 |
| Data processing | 247,061 | 288,421 |
| Insurance | 92,323 | 105,611 |
| Net cost of operation of other real estate owned | 1,559 | 1,761 |
| Printing and stationery | 178,624 | 149,981 |
| Legal expense | 56,286 | 64,191 |
| Amortization of intangible assets from branch acquisitions | 47,767 | |
| Other expense | 1,564,454 | 1,140,601 |
| | ----- | ----- |
| Total other expense | 6,754,854 | 5,796,991 |
| | ----- | ----- |
| Income before income taxes | 4,270,877 | 4,206,011 |
| Income taxes | 1,369,674 | 1,356,991 |

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| | | |
|---------------------------|--------------|-------------|
| Net income | \$ 2,901,203 | \$ 2,849,02 |
| Earnings per common share | \$ 2.03 | \$ 1.9 |

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

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SALISBURY BANCORP, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

Years Ended December 31, 2001 and 2000

| | Number of Shares Issued | Common Stock | Paid-in Capital | Retained Earnings | Treasury Stock |
|---|----------------------------------|-----------------|--------------------|----------------------|-------------------|
| Balance, December 31, 1999 | 1,504,171 | \$150,417 | \$3,780,376 | \$17,798,981 | \$ |
| Comprehensive income: | | | | 2,849,02 | |
| Net income | | | | | |
| Net change in unrealized holding loss on available-for-sale securities, net of tax effect | | | | | |
| Comprehensive income | | | | | |
| Repurchase of common stock | | | | | (8 |
| Transfer treasury stock to reduce shares issued | (45,805) | (4,580) | (811,482) | | 8 |
| Dividends declared (\$.77 per share) | | | | (1,131,591) | |
| Balance, December 31, 2000 | 1,458,366 | 145,837 | 2,968,894 | 19,516,414 | |
| Comprehensive income: | | | | 2,901,203 | |
| Net income | | | | | |
| Net change in unrealized holding loss on available-for-sale securities, net of tax effect | | | | | |
| Comprehensive income | | | | | |
| Repurchase of common stock | | | | | (6 |
| Transfer treasury stock to reduce shares issued | (36,008) | (3,601) | (687,479) | | 6 |
| Dividends declared (\$.84 per share) | | | | (1,199,462) | |
| Balance, December 31, 2001 | 1,422,358 | \$142,236 | \$2,281,415 | \$21,218,155 | \$ |

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Reclassification disclosure for the years ended December 31:

| | 2001 | 2000 |
|---|--------------|----------|
| | ----- | ----- |
| Net unrealized gains (losses) on available-for-sale securities | \$ (46,411) | \$ 2,666 |
| Reclassification adjustment for realized (gains) losses in net income | (130,117) | 6 |
| | ----- | ----- |
| Other comprehensive income (loss) before income tax effect | (176,528) | 2,722 |
| Income tax (expense) benefit | 68,757 | (1,066) |
| | ----- | ----- |
| Other comprehensive income (loss), net of tax | \$ (107,771) | \$ 1,666 |
| | ===== | ===== |

Accumulated other comprehensive loss as of December 31, 2001 and 2000 consists of net unrealized holding losses on available-for-sale securities, net of taxes.

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

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SALISBURY BANCORP, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS

Years Ended December 31, 2001 and 2000

| | 2001 | 2000 |
|---|--------------|--------------|
| | ----- | ----- |
| Cash flows from operating activities: | | |
| Net income | \$ 2,901,203 | \$ 2,849,666 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Accretion of securities, net | (49,133) | (65,000) |
| (Gain) loss on sales of available-for-sale securities, net | (130,117) | 63,000 |
| Provision for loan losses | 150,000 | 180,000 |
| Depreciation and amortization | 262,703 | 269,000 |
| Amortization of intangible assets from branch acquisition | 47,767 | |
| Accretion of fair value adjustment on deposits | (136,287) | |
| (Increase) decrease in interest receivable | 108,960 | (214,000) |
| Deferred tax benefit | (24,072) | (139,000) |
| Increase in prepaid expenses | (84,167) | (10,000) |
| Increase in cash surrender value of insurance policies | (29,192) | (26,000) |
| Increase in income tax receivable | (43,254) | |
| (Increase) decrease in other assets | (91,608) | 112,000 |
| Decrease in taxes payable | (8,081) | |

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| | | |
|---|--------------|----------|
| Increase in accrued expenses | 176,341 | 236, |
| Increase (decrease) in interest payable | (39,979) | 106, |
| Decrease in other liabilities | (7,275) | (1, |
| | ----- | ----- |
| Net cash provided by operating activities | 3,011,890 | 3,350, |
| | ----- | ----- |
| Cash flows from investing activities: | | |
| Purchases of Federal Home Loan Bank stock | (14,900) | (828, |
| Purchases of available-for-sale securities | (88,096,807) | (21,958, |
| Proceeds from sales of available-for-sale securities | 19,419,941 | 6,225, |
| Proceeds from maturities of available-for-sale securities | 48,212,964 | 16,036, |
| Proceeds from maturities of held-to-maturity securities | 10,032 | 78, |
| Loan purchases | (2,800,000) | (715, |
| Loan originations and principal collections, net | (2,128,114) | (13,444, |
| Recoveries of loans previously charged off | 103,658 | 22, |
| Capital expenditures | (152,711) | (541, |
| | ----- | ----- |
| Net cash used in investing activities | (25,445,937) | (15,124, |
| | ----- | ----- |

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SALISBURY BANCORP, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS

Years Ended December 31, 2001 and 2000

(continued)

| | 2001 | 2000 |
|--|---------------|---------------|
| | ----- | ----- |
| Cash flows from financing activities: | | |
| Net increase in demand deposits, NOW and savings accounts | 18,060,288 | 14,653,988 |
| Net decrease in time deposits | (9,573,854) | (2,576,311) |
| Assumption of net deposits on branch acquisitions | 22,897,443 | |
| Advances from Federal Home Loan Bank | 20,000,000 | 29,000,000 |
| Principal payments on advances from Federal Home Loan Bank | (14,353,547) | (21,354,686) |
| Dividends paid | (1,454,946) | (1,088,830) |
| Net repurchase of common stock | (691,080) | (816,062) |
| | ----- | ----- |
| Net cash provided by financing activities | 34,884,304 | 17,818,099 |
| | ----- | ----- |
| Net increase in cash and cash equivalents | 12,450,257 | 6,043,700 |
| Cash and cash equivalents at beginning of year | 13,759,424 | 7,715,724 |
| | ----- | ----- |
| Cash and cash equivalents at end of year | \$ 26,209,681 | \$ 13,759,424 |
| | ===== | ===== |

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Supplemental disclosures:

| | | |
|-------------------|--------------|--------------|
| Interest paid | \$ 8,340,776 | \$ 8,177,825 |
| Income taxes paid | 1,437,000 | 1,488,445 |

Branch office acquisition:

| | | |
|-------------------------|---------------|--|
| Deposits assumed | \$ 26,565,337 | |
| Loans acquired | (121,423) | |
| Fixed assets acquired | (272,150) | |
| | ----- | |
| Net liabilities assumed | 26,171,764 | |
| | | |
| Cash received | (22,897,443) | |
| | ----- | |
| Intangible assets | \$ 3,274,321 | |
| | ===== | |

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

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SALISBURY BANCORP, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Years Ended December 31, 2001 and 2000

NOTE 1 - NATURE OF OPERATIONS

Salisbury Bancorp, Inc. (Bancorp) is a Connecticut corporation that was organized on April 24, 1998 to become a holding company, under which Salisbury Bank & Trust Company (Bank) operates as its wholly-owned subsidiary. (Bancorp and the Bank are referred to together as the (Company)).

The Bank is a state chartered bank which was incorporated in 1874 and is headquartered in Lakeville, Connecticut. The Bank operates its business from four banking offices located in Connecticut. The Bank is engaged principally in the business of attracting deposits from the general public and investing those deposits in residential and commercial real estate, consumer and small business loans.

NOTE 2 - ACCOUNTING POLICIES

The accounting and reporting policies of the Company and its subsidiary conform to accounting policies generally accepted in the United States of America and predominant practices within the banking industry. The consolidated financial statements were prepared using the accrual basis of accounting. The significant accounting policies are summarized below to assist the reader in better understanding the consolidated financial statements and other data contained herein.

USE OF ESTIMATES:

The preparation of financial statements in conformity with accounting

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

BASIS OF PRESENTATION:

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary, the Bank, and the Bank's wholly-owned subsidiary, SBT Realty, Inc. SBT Realty, Inc. holds and manages bank owned real estate situated in New York state. All significant intercompany accounts and transactions have been eliminated in the consolidation.

CASH AND CASH EQUIVALENTS:

For purposes of reporting cash flows, cash and cash equivalents include cash on hand, cash items, due from banks, interest bearing demand deposits with other banks, money market mutual funds and federal funds sold.

Cash and due from banks as of December 31, 2001 includes \$1,294,000 which is subject to withdrawals and usage restrictions to satisfy the reserve requirements of the Federal Reserve Bank.

SECURITIES:

Investments in debt securities are adjusted for amortization of premiums and accretion of discounts. Gains or losses on sales of investment securities are computed on a specific identification basis.

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The Company classifies debt and equity securities into one of three categories: held-to-maturity, available-for-sale or trading. This security classification may be modified after acquisition only under certain specified conditions. In general, securities may be classified as held-to-maturity only if the Company has the positive intent and ability to hold them to maturity. Trading securities are defined as those bought and held principally for the purpose of selling them in the near term. All other securities must be classified as available-for-sale.

- Held-to-maturity securities are measured at amortized cost in the balance sheet. Unrealized holding gains and losses are not included in earnings or in a separate component of capital. They are merely disclosed in the notes to the consolidated financial statements.
- Available-for-sale securities are carried at fair value on the consolidated balance sheet. Unrealized holding gains and losses are not included in earnings but are reported as a net amount (less expected tax) in a separate component of capital until realized.
- Trading securities are carried at fair value on the consolidated balance sheet. Unrealized holding gains and

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losses for trading securities are included in earnings.

- Declines in the fair value of held-to-maturity and available-for-sale securities below their cost that are deemed to be other than temporary are reflected in earnings as realized losses.

LOANS:

Loans receivable that management has the intent and ability to hold until maturity or payoff, are reported at their outstanding principal balances reduced by any charge-offs, the allowance for loan losses and any deferred fees or costs on originated loans or unamortized premiums or discounts on purchased loans.

Interest on loans is recognized on a simple interest basis.

Loan origination, commitment fees and certain direct origination costs are deferred, and the net amount amortized as an adjustment of the related loan's yield. The Company is amortizing these amounts over the contractual life of the related loans.

Cash receipts of interest income on impaired loans is credited to principal to the extent necessary to eliminate doubt as to the collectibility of the net carrying amount of the loan. Some or all of the cash receipts of interest income on impaired loans is recognized as interest income if the remaining net carrying amount of the loan is deemed to be fully collectible. When recognition of interest income on an impaired loan on a cash basis is appropriate, the amount of income that is recognized is limited to that which would have been accrued on the net carrying amount of the loan at the contractual interest rate. Any cash interest payments received in excess of the limit and not applied to reduce the net carrying amount of the loan are recorded as recoveries of charge-offs until the charge-offs are fully recovered.

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.

The allowance for loan losses is evaluated on a regular basis by management and is based upon management's periodic review of the collectibility of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

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A loan is 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

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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 for commercial and construction loans 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 and residential loans for impairment disclosures.

PREMISES AND EQUIPMENT:

Premises and equipment are stated at cost, less accumulated depreciation and amortization. Cost and related allowances for depreciation and amortization of premises and equipment retired or otherwise disposed of are removed from the respective accounts with any gain or loss included in income or expense. Depreciation and amortization are calculated principally on the straight-line method over the estimated useful lives of the assets.

OTHER REAL ESTATE OWNED AND IN-SUBSTANCE FORECLOSURES:

Other real estate owned includes properties acquired through foreclosure and properties classified as in-substance foreclosures in accordance with Financial Accounting Standards Board Statement No. 15, "Accounting by Debtors and Creditors for Troubled Debt Restructuring." These properties are carried at the lower of cost or estimated fair value less estimated costs to sell. Any writedown from cost to estimated fair value required at the time of foreclosure or classification as in-substance foreclosure is charged to the allowance for loan losses. Expenses incurred in connection with maintaining these assets and subsequent writedowns are included in other expense.

In accordance with Statement of Financial Accounting Standards No. 114, "Accounting by Creditors for Impairment of a Loan," the Company classifies loans as in-substance repossessed or foreclosed if the Company receives physical possession of the debtor's assets regardless of whether formal foreclosure proceedings take place.

ADVERTISING:

The Company directly expenses costs associated with advertising as they are incurred.

INCOME TAXES:

The Company recognizes income taxes under the asset and liability method. Under this method, deferred tax assets and liabilities are established for the temporary differences between the accounting basis and the tax basis of the Company's assets and liabilities at enacted tax rates expected to be in effect when the amounts related to such temporary differences are realized or settled.

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FAIR VALUES OF FINANCIAL INSTRUMENTS:

Statement of Financial Accounting Standards No. 107, "Disclosures About Fair Value of Financial Instruments," requires that the Company disclose estimated fair value for its financial instruments. Fair value methods and assumptions used by the Company in estimating its fair value disclosures are as follows:

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Cash and cash equivalents: The carrying amounts reported in the balance sheet for cash and cash equivalents approximate those assets' fair values.

Securities (including mortgage-backed securities): Fair values for securities are based on quoted market prices, where available. If quoted market prices are not available, fair values are based on quoted market prices of comparable instruments.

Loans receivable: For variable-rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying values. The fair values for other loans are estimated using discounted cash flow analyses, using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality.

Accrued interest receivable: The carrying amount of accrued interest receivable approximates its fair value.

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

Federal Home Loan Bank Advances: Fair values for Federal Home Loan Bank advances are estimated using a discounted cash flow technique that applies interest rates currently being offered on advances to a schedule of aggregated expected monthly maturities on Federal Home Loan Bank advances.

Due to broker: The carrying amount of due to broker approximates its fair value.

Off-balance sheet instruments: The fair value of commitments to originate loans is estimated using the fees currently charged to enter similar agreements, taking into account the remaining terms of the agreements and the present creditworthiness of the counterparties. For fixed-rate loan commitments and the unadvanced portion of loans, fair value also considers the difference between current levels of interest rates and the committed rates. The fair value of letters of credit is based on fees currently charged for similar agreements or on the estimated cost to terminate them or otherwise settle the obligation with the counterparties at the reporting date.

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STOCK BASED COMPENSATION:

The Company recognizes stock-based compensation using the intrinsic value approach set forth in APB Opinion No. 25 rather than the fair value method introduced in SFAS No. 123. Entities electing to continue to follow the provisions of APB No. 25 must make pro forma disclosure of net income and earnings per share, as if the fair value method of accounting defined in SFAS No. 123 had been applied. The Company has made the pro forma disclosures required by SFAS No. 123. The Company had no stock options outstanding as of December 31, 2001 and 2000.

EARNINGS PER SHARE:

Basic EPS excludes dilution and is computed by dividing income available to common stockholders by the weighted-average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that then shared in the earnings of the entity.

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RECENT ACCOUNTING PRONOUNCEMENTS:

In June 1998, the FASB issued Statement No. 133, "Accounting for Derivative Instruments and Hedging Activities," effective for fiscal years beginning after June 15, 2000. This Statement establishes accounting and reporting standards for derivative instruments and hedging activities, including certain derivative instruments embedded in other contracts, and requires that an entity recognize all derivatives as assets or liabilities in the balance sheet and measure them at fair value. If certain conditions are met, an entity may elect to designate a derivative as follows: (a) a hedge of the exposure to changes in the fair value of a recognized asset or liability or an unrecognized firm commitment, (b) a hedge of the exposure to variable cash flows of a forecasted transaction, or (c) a hedge of the foreign currency exposure of an unrecognized firm commitment, an available-for-sale security, a foreign currency denominated forecasted transaction, or a net investment in a foreign operation. The Statement generally provides for matching the timing of the recognition of the gain or loss on derivatives designated as hedging instruments with the recognition of the changes in the fair value of the item being hedged. Depending on the type of hedge, such recognition will be in either net income or other comprehensive income. For a derivative not designated as a hedging instrument, changes in fair value will be recognized in net income in the period of change. The adoption of this Statement did not have a material impact on the consolidated financial statements. The Company had no derivative instruments as of December 31, 2001 and 2000.

FASB has issued SFAS No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities". This Statement replaces SFAS No. 125, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities" and rescinds SFAS Statement No. 127, "Deferral of the Effective Date of Certain Provisions of FASB Statement No. 125". SFAS No. 140 provides accounting and reporting standards for transfers and servicing of financial assets and extinguishments of liabilities. This statement provides consistent

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standards for distinguishing transfers of financial assets that are sales from transfers that are secured borrowings. This statement is effective for transfers and servicing of financial assets and extinguishments of liabilities occurring after March 31, 2001; however, the disclosure provisions are effective for fiscal years ending after December 15, 2000. The adoption of this Statement did not have a material impact on its financial position or results of operations.

In June 2001, the FASB issued SFAS No. 141, "Business Combinations". This statement addresses financial accounting and reporting for business combinations and supercedes APB Opinion No. 16, "Business Combinations", and SFAS No. 38, "Accounting for Preacquisition Contingencies of Purchased Enterprises". Under Opinion 16, business combinations were accounted for using one of two methods, the pooling-of-interests method or the purchase method. All business combinations in the scope of SFAS No. 141 are to be accounted for using one method - the purchase method. The provisions of SFAS No. 141 apply to all business combinations initiated after June 30, 2001 and to all business combinations accounted for using the purchase method for which the date of acquisition is July 1, 2001, or later.

On September 14, 2001 the Company acquired a bank branch. The acquisition is described on the following page. The results of operations of the acquired bank branch are included in the income statement of the Company for the period from September 15, 2001 to December 31, 2001.

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In June 2001, the FASB issued SFAS No. 142, "Goodwill and Other Intangible Assets". This statement addresses financial accounting and reporting for required goodwill and other intangible assets and supercedes APB Opinion No. 17, "Intangible Assets". The initial recognition and measurement provisions of SFAS No. 142 apply to intangible assets which are defined as assets (not including financial assets) that lack physical substance. The term "intangible assets" is used in SFAS No. 142 to refer to intangible assets other than goodwill. The accounting for a recognized intangible asset is based on its useful life. An intangible asset with a finite useful life is amortized; an intangible asset with an indefinite useful life is not amortized. An intangible asset that is subject to amortization shall be reviewed for impairment in accordance with SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed of".

SFAS No. 142 provides that goodwill shall not be amortized. Goodwill is defined as the excess of the cost of an acquired entity over the net of the amounts assigned to assets acquired and liabilities assumed. SFAS No. 142 further provides that goodwill shall be tested for impairment at a level of reporting referred to as a reporting unit. Impairment is the condition that exists when the carrying amount of goodwill exceeds its implied fair value.

SFAS No. 142 is effective as follows:

All of the provisions of SFAS No. 142 shall be applied in fiscal years beginning after December 15, 2001, to all goodwill and intangible assets recognized in an entity's statement of financial position at the beginning of that fiscal year, regardless of when

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those previously recognized assets were initially recognized.

The Company has intangible assets as of December 31, 2001 in the amount of \$3,226,554 that arose from the Company's purchase of certain assets and its assumption of certain liabilities of a bank branch in Canaan, Connecticut on September 14, 2001. The fair value of the liabilities assumed exceeded the fair value of the assets acquired. Included in the intangible assets acquired was an identified intangible asset (a core deposit intangible) in the amount of \$888,606 which is being amortized to expense over 13 years on the straight line method. The Company classified the remainder of the intangible assets acquired, in the amount of \$2,385,715, as an unidentifiable intangible asset and is amortizing it to expense over 25 years on the straight-line method. Accumulated amortization of the intangible assets was \$47,767. Estimated amortization expense in each of the five years in the period from January 1, 2002 to December 31, 2006 is \$163,783. This accounting is in accordance with SFAS No. 72, "Accounting for Certain Acquisitions of Banking or Thrift Institutions" and will not change because SFAS No. 142 did not change the essential parts of SFAS No. 72. However, the intangible asset will be subject to the impairment review requirements of SFAS No. 121.

On October 10, 2001 the Financial Accounting Standards Board (Board) affirmed that paragraph 5 of FASB Statement No. 72, Accounting for Certain Acquisitions of Banking or Thrift Institutions, applies to all acquisitions of financial institutions (or branches thereof) whether "troubled" or not, in which the fair value of the liabilities assumed exceeds the fair value of tangible and intangible assets acquired. The Board decided to reconsider the guidance in paragraphs 5-7 of Statement 72 as part of its consideration of combinations of mutual enterprises within the scope of the project on combinations of not-for-profit organizations.

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NOTE 3 - INVESTMENTS IN SECURITIES

Debt and equity securities have been classified in the consolidated balance sheets according to management's intent. The carrying amount of securities and their approximate fair values are as follows as of December 31:

| | Amortized Cost Basis ----- | Gains In Accumulated Other Comprehensive Income ----- | Los Accum O Compre ----- |
|---|-------------------------------------|--|--------------------------------------|
| Available-for-sale securities: | | | |
| December 31, 2001: | | | |
| Equity securities | \$ 3,031 | \$ 131,978 | \$ |
| Debt securities issued by the U.S. Treasury and other U.S. government corporations and agencies | 38,459,596 | 278,375 | |
| Debt securities issued by states of the United States and political subdivisions of the states | 30,927,212 | 151,015 | (|

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| | | | |
|--|----------------|------------|--------|
| Money market mutual funds | 617,461 | 617,461 | |
| Mortgage-backed securities | 33,314,635 | 171,006 | (|
| | ----- | ----- | |
| | 103,321,935 | 732,374 | (1, |
| Money market mutual funds included in cash and cash equivalents | (617,461) | | |
| | ----- | ----- | |
| | \$ 102,704,474 | \$ 732,374 | \$ (1, |
| | ===== | ===== | ===== |
| December 31, 2000: | | | |
| Equity securities | \$ 11,830 | \$ 166,735 | |
| Debt securities issued by the U.S. Treasury and other U. S. government corporations and agencies | 46,925,648 | 35,087 | (|
| Debt securities issued by states of the United States and political subdivisions of the states | 14,134,594 | 209,400 | (|
| Money market mutual funds | 1,161,416 | | |
| Mortgage-backed securities | 27,789,473 | 63,523 | (|
| | ----- | ----- | |
| | 90,022,961 | 474,745 | (|
| Money market mutual funds included in cash and cash equivalents | (1,161,416) | | |
| | ----- | ----- | |
| | \$ 88,861,545 | \$ 474,745 | \$ (|
| | ===== | ===== | ===== |

| | Net Carrying Amount | Gross Unrecognized Holding Gains | Gross Unrecognized Holding Loss | Fair Value |
|------------------------------|---------------------------|---|--|---------------|
| | ----- | ----- | ----- | ----- |
| Held-to-maturity securities: | | | | |
| December 31, 2001: | | | | |
| Mortgage-backed securities | \$399,989 | \$ 1,414 | \$ | \$401,403 |
| | ===== | ===== | ===== | ===== |
| December 31, 2000: | | | | |
| Mortgage-backed securities | \$410,441 | \$ | \$ (2,253) | \$408,188 |
| | ===== | ===== | ===== | ===== |

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The scheduled maturities of securities (other than equity securities) were as follows as of December 31, 2001:

| | Available-For-Sale Fair Value | Held-To-Maturity Net Carrying Amount |
|---------------------|-------------------------------------|--|
| | ----- | ----- |
| Due within one year | \$ | \$ |

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| | | |
|--|---------------|------------|
| Due after one year through five years | 1,489,496 | |
| Due after five years through ten years | 6,404,004 | |
| Due after ten years | 61,080,975 | |
| Mortgage-backed securities | 33,138,545 | 399,989 |
| | ----- | ----- |
| | \$102,113,020 | \$ 399,989 |
| | ===== | ===== |

During 2001, proceeds from sales of available-for-sale securities amounted to \$19,419,941. Gross realized gains on those sales amounted to \$130,117. During 2000, proceeds from sales of available-for-sale securities amounted to \$6,225,720. Gross realized gains and gross realized losses on those sales amounted to \$145 and \$64,121, respectively. The tax (expense) benefit applicable to these net realized gains and losses amounted to \$(50,681) and \$24,919, respectively.

There were no issuers of securities whose carrying amount exceeded 10% of stockholders' equity as of December 31, 2001.

Total carrying amounts of \$6,199,068 and \$7,073,366 of debt securities were pledged to secure public deposits and for other purposes as required by law as of December 31, 2001 and 2000, respectively.

NOTE 4 - LOANS

Loans consisted of the following as of December 31:

| | 2001 | 2000 |
|---|----------------|------------|
| | ----- | ----- |
| | (in thousands) | |
| Commercial, financial and agricultural | \$ 10,797 | \$ 8,592 |
| Real estate - construction and land development | 3,935 | 6,275 |
| Real estate - residential | 102,201 | 98,312 |
| Real estate - commercial | 17,423 | 15,463 |
| Consumer | 10,030 | 10,673 |
| Other | 125 | 247 |
| | ----- | ----- |
| | 144,511 | 139,562 |
| Allowance for loan losses | (1,445) | (1,292) |
| | ----- | ----- |
| Net loans | \$ 143,066 | \$ 138,270 |
| | ===== | ===== |

Certain directors and executive officers of the Company and companies in which they have significant ownership interest were customers of the Bank during 2001. Total loans to such persons and their companies amounted to \$1,336,893 as of December 31, 2001. During 2001 advances of \$178,014 were made and repayments totaled \$342,922.

Changes in the allowance for loan losses were as follows for the years ended December 31:

| | 2001 | 2000 |
|--|-------------|-------------|
| | ----- | ----- |
| Balance at beginning of period | \$1,291,502 | \$1,159,537 |
| Provision for loan losses | 150,000 | 180,000 |
| Recoveries of loans previously charged off | 103,658 | 22,543 |
| Loans charged off | (100,656) | (70,578) |
| | ----- | ----- |
| Balance at end of period | \$1,444,504 | \$1,291,502 |

=====

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Information about loans that meet the definition of an impaired loan in Statement of Financial Accounting Standards No. 114 is as follows as of December 31:

| | 2001 | | |
|---|---------------------------------------|-------------------------------------|-------|
| | Recorded Investment In Impaired Loans | Related Allowance For Credit Losses | |
| | ----- | ----- | ----- |
| Loans for which there is a related allowance for credit losses | \$0 | \$0 | \$ |
| Loans for which there is no related allowance for credit losses | 0 | | |
| | --- | --- | --- |
| Totals | \$0 | \$0 | \$ |
| | == | == | == |
| Average recorded investment in impaired loans during the year ended December 31 | \$0 | | |
| | == | | |
| Related amount of interest income recognized during the time, in the year ended December 31, that the loans were impaired | | | |
| Total recognized | \$0 | | \$ |
| | == | | == |
| Amount recognized using a cash-basis method of accounting | \$0 | | \$ |
| | == | | == |

NOTE 5 - PREMISES AND EQUIPMENT

The following is a summary of premises and equipment as of December 31:

| | 2001 | 2000 |
|---|--------------|--------------|
| | ----- | ----- |
| Land | \$ 350,644 | \$ 324,194 |
| Buildings | 2,514,603 | 2,231,783 |
| Furniture and equipment | 1,884,112 | 1,768,521 |
| | ----- | ----- |
| | 4,749,359 | 4,324,498 |
| Accumulated depreciation and amortization | (2,065,872) | (1,803,169) |
| | ----- | ----- |
| | \$ 2,683,487 | \$ 2,521,329 |
| | ===== | ===== |

NOTE 6 - DEPOSITS

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 The aggregate amount of time deposit accounts in denominations of \$100,000 or more as of December 31, 2001 and 2000 was \$18,161,373 and \$16,899,009, respectively.

For time deposits as of December 31, 2001, the scheduled maturities for years ended December 31 are:

| | |
|------|--------------|
| 2002 | \$49,355,011 |
| 2003 | 7,726,724 |
| 2004 | 819,561 |
| 2005 | 3,033,450 |
| 2006 | 5,383,084 |
| | ----- |
| | \$66,317,830 |
| | ===== |

Certain directors and executive officers of the Company and companies in which they have a significant ownership interest were customers of the Bank. Total deposits to such persons and their companies amounted to \$727,850 as of December 31, 2001 and \$663,517 as of December 31, 2001.

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NOTE 7 - FEDERAL HOME LOAN BANK ADVANCES

Advances consist of funds borrowed from the Federal Home Loan Bank of Boston (FHLB).

Maturities of advances from the FHLB for the five fiscal years ending after December 31, 2001 and thereafter are summarized as follows:

| | |
|------------|--------------|
| | AMOUNT |
| | ----- |
| 2002 | \$ 1,113,139 |
| 2003 | 10,993,295 |
| 2004 | 766,823 |
| 2005 | 263,339 |
| 2006 | 188,605 |
| Thereafter | 39,678,545 |
| | ----- |
| | \$53,003,746 |
| | ===== |

The advances due after 2006 include three advances that are redeemable at par at the option of the FHLB. An advance of \$19,000,000 is redeemable on January 25, 2002, an advance of \$10,000,000 is redeemable on December 15, 2003 and an advance of \$10,000,000 is redeemable on February 26, 2004.

Amortizing advances are being repaid in equal monthly payments and are being amortized from the date of the advance to the maturity date on a direct reduction basis.

Advances are secured by the Company's stock in that institution, its residential real estate mortgage portfolio and the remaining U.S. government and agency obligations not otherwise pledged.

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At December 31, 2001, the interest rates on FHLB advances ranged from 4.81 percent to 6.58 percent. At December 31, 2000, the weighted average interest rate on FHLB advances was 5.39 percent.

NOTE 8 - EMPLOYEE BENEFITS

The Company has an insured noncontributory defined benefit retirement plan available to all employees eligible as to age and length of service. Benefits are based on a covered employee's final average compensation, primary social security benefit and credited service. The Company makes annual contributions which meet the Employee Retirement Income Security Act minimum funding requirements.

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The following tables set forth information about the plan as of December 31 and the years then ended:

| | 2001 | 2000 |
|---|--------------|--------------|
| | ----- | ----- |
| Change in projected benefit obligation: | | |
| Benefit obligation at beginning of year | \$ 2,174,561 | \$ 2,004,633 |
| Actuarial (gain) loss | (1,540) | 191,408 |
| Service cost | 141,721 | 131,006 |
| Interest cost | 168,343 | 163,061 |
| Benefits paid | (137,467) | (315,547) |
| | ----- | ----- |
| Benefit obligation at end of year | 2,345,618 | 2,174,561 |
| | ----- | ----- |
| Change in plan assets: | | |
| Plan assets at estimated fair value at beginning of year | 2,296,344 | 2,567,234 |
| Actual return on plan assets | (45,501) | 44,657 |
| Contributions | 57,817 | |
| Benefits paid | (137,467) | (315,547) |
| | ----- | ----- |
| Fair value of plan assets at end of year | 2,171,193 | 2,296,344 |
| | ----- | ----- |
| Funded status (174,425) | 121,783 | |
| Unrecognized net gain from actuarial experience | (301,286) | (516,865) |
| Unrecognized prior service cost | 95,436 | 96,328 |
| Unamortized net asset existing at date of adoption of SFAS No. 87 | 58,364 | 58,364 |
| | ----- | ----- |
| Accrued benefit cost included in other liabilities | \$ (321,911) | \$ (240,390) |
| | ===== | ===== |

The weighted-average discount rate and rate of increase in future compensation levels used in determining the actuarial present value of the projected benefit obligation were 8.0% and 6.0% for 2001 and 2000, respectively. The weighted-average expected long-term rate of return on assets was 8.0% for 2001 and 2000.

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Components of net periodic cost:

| | 2001 | 2000 |
|-------------------------------------|------------|------------|
| | ----- | ----- |
| Service cost | \$ 141,721 | \$ 131,006 |
| Interest cost on benefit obligation | 168,343 | 163,061 |
| Expected return on assets | (180,290) | (192,757) |
| Amortization of prior service cost | 9,564 | 9,564 |
| | ----- | ----- |
| Net periodic cost | \$ 139,338 | \$ 110,874 |
| | ===== | ===== |

The Company adopted a 401(k) Plan effective in 2000. Under the Plan eligible participants may contribute up to fifteen percent of their pay. The Company may make discretionary contributions to the Plan. The Company's contribution in the years ended December 31, 2001 and 2000 amounted to \$48,000 and \$44,000, respectively. Discretionary contributions vest in full after five years.

Five of the Company's executives have a change in control agreement (agreement) with the Company. Under the agreements, if the executive officer's employment is terminated within twelve months subsequent to a change in control as defined in the agreements, then the officer is entitled to a lump sum amount equal to the executive's annual compensation, as defined in the agreements, less amounts previously paid the executive from the date of the change in control.

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NOTE 9 - INCOME TAXES

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

| | 2001 | 2000 |
|--------------------------|--------------|--------------|
| | ----- | ----- |
| Current: | | |
| Federal | \$ 1,073,942 | \$ 1,172,814 |
| State | 319,804 | 323,712 |
| | ----- | ----- |
| | 1,393,746 | 1,496,526 |
| Deferred: | | |
| Federal | (19,437) | (113,530) |
| State | (4,635) | (26,002) |
| | ----- | ----- |
| | (24,072) | (139,532) |
| | ----- | ----- |
| Total income tax expense | \$ 1,369,674 | \$ 1,356,994 |
| | ===== | ===== |

The reasons for the differences between the statutory federal income tax rates and the effective tax rates are summarized as follows for the years ended December 31:

| | 2001 | 2000 |
|--|--------|--------|
| | ----- | ----- |
| | % of | % of |
| | Income | Income |
| Federal income tax at statutory rate | 34.0% | 34.0% |
| Increase (decrease) in tax resulting from: | | |

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| | | |
|---------------------------------------|-------|-------|
| Tax-exempt income | (7.8) | (5.3) |
| Other items | 1.0 | (1.0) |
| State tax, net of federal tax benefit | 4.9 | 4.6 |
| | ---- | ---- |
| Effective tax rates | 32.1% | 32.3% |
| | ==== | ==== |

The Company had gross deferred tax assets and gross deferred tax liabilities as follows as of December 31:

| | 2001 | 2000 |
|--|------------|------------|
| | ----- | ----- |
| Deferred tax assets: | | |
| Allowance for loan losses | \$ 365,020 | \$ 306,595 |
| Interest on non-performing loans | 10,283 | 6,244 |
| Accrued deferred compensation | 20,602 | 22,361 |
| Post retirement benefits | 19,475 | 14,801 |
| Other real estate owned property writedown | 25,317 | 25,317 |
| Deferred organization costs | 2,193 | 3,386 |
| Accrued pensions | 125,385 | 110,771 |
| Net unrealized holding loss on available-for-sale securities | 177,785 | 109,028 |
| | ----- | ----- |
| Gross deferred tax assets | 746,060 | 598,503 |
| | ----- | ----- |
| Deferred tax liabilities: | | |
| Core deposit intangible asset | (60,672) | |
| Accelerated depreciation | (323,737) | (335,378) |
| Discount accretion | (13,569) | (7,872) |
| | ----- | ----- |
| Gross deferred tax liabilities | (397,978) | (343,250) |
| | ----- | ----- |
| Net deferred tax assets | \$ 348,082 | \$ 255,253 |
| | ===== | ===== |

Deferred tax assets as of December 31, 2001 and 2000 have not been reduced by a valuation allowance because management believes that it is more likely than not that the full amount of deferred tax assets will be realized.

As of December 31, 2001, the Company had no operating loss and tax credit carryovers for tax purposes.

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NOTE 10 - FINANCIAL INSTRUMENTS

The Company is a party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financial needs of its customers. These financial instruments include commitments to originate loans, standby letters of credit and unadvanced funds on loans. The instruments involve, to varying degrees, elements of credit risk in excess of the amount recognized in the balance sheets. The contract amounts of those instruments reflect the extent of involvement the Company has in particular classes of financial instruments.

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

Commitments to originate loans are agreements to lend to a customer provided 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. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Company evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Company upon extension of credit, is based on management's credit evaluation of the borrower. Collateral held varies, but may include secured interests in mortgages, accounts receivable, inventory, property, plant and equipment and income producing properties.

The estimated fair values of the Company's financial instruments, all of which are held or issued for purposes other than trading, are as follows as of December 31:

| | 2001 | | 2000 |
|-------------------------------|--------------------|---------------|-------------------|
| | Carrying Amount | Fair Value | Carrying Value |
| Financial assets: | | | |
| Cash and cash equivalents | \$ 26,209,681 | \$ 26,209,681 | \$ 13,759,424 |
| Available-for-sale securities | 102,248,029 | 102,248,029 | 88,581,628 |
| Held-to-maturity securities | 399,989 | 401,403 | 410,441 |
| Federal Home Loan Bank stock | 2,945,200 | 2,945,200 | 2,930,300 |
| Loans | 143,066,109 | 143,680,000 | 138,270,230 |
| Accrued interest receivable | 1,681,268 | 1,681,268 | 1,790,228 |
| Financial liabilities: | | | |
| Deposits | 201,351,488 | 201,601,000 | 166,436,004 |
| FHLB advances | 53,003,746 | 53,974,000 | 47,357,293 |
| Due to broker | 4,203,808 | 4,203,808 | 11,004,451 |

The carrying amounts of financial instruments shown in the above table are included in the consolidated balance sheets under the indicated captions. Accounting policies related to financial instruments are described in Note 2.

The amounts of financial instrument liabilities with off-balance sheet credit risk are as follows as of December 31:

| | 2001 | 2000 |
|--------------------------------------|--------------|--------------|
| Commitments to originate loans | \$ 6,692,798 | \$ 7,462,000 |
| Standby letters of credit | 20,000 | 20,000 |
| Unadvanced portions of loans: | | |
| Home equity | 8,631,632 | 7,355,736 |
| Commercial lines of credit | 5,260,748 | 6,653,389 |
| Construction | 881,951 | 3,792,995 |
| Consumer | 5,744,632 | 4,976,987 |

\$27,231,761

\$30,261,107

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There is no material difference between the notional amounts and the estimated fair values of the off-balance sheet liabilities.

Commitments to purchase when issued investment securities at December 31, 2001 totaled \$3,140,546.

The Company has no derivative financial instruments subject to the provisions of SFAS No. 119 "Disclosure About Derivative Financial Instruments and Fair Value of Financial Instruments."

NOTE 11 - SIGNIFICANT GROUP CONCENTRATIONS OF CREDIT RISK

Most of the Bank's business activity is with customers located in northwestern Connecticut and bordering New York and Massachusetts towns. There are no concentrations of credit to borrowers that have similar economic characteristics. The majority of the Bank's loan portfolio is comprised of loans collateralized by real estate located in northwestern Connecticut and bordering New York and Massachusetts towns.

NOTE 12 - REGULATORY MATTERS

The Company and its subsidiary the Bank are subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory - and possibly additional discretionary - actions by regulators that, if undertaken, could have a direct material effect on the Company's and the Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of their assets, liabilities and certain off-balance-sheet items as calculated under regulatory accounting practices. Their 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 and the Bank to maintain minimum amounts and ratios (set forth in the table below) 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, 2001, that the Company and the Bank meet all capital adequacy requirements to which they are subject.

As of December 31, 2001, 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 the Bank must maintain minimum total risk-based, Tier 1 risk-based and Tier 1 leverage ratios as set forth in the table. There are no conditions or events since that notification that management believes have changed the Bank's category.

The Company and the Bank's actual capital amounts and ratios are also presented in the table.

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| | Actual | | For Capital Adequacy Purposes: | |
|--|----------|--------|--------------------------------|-------|
| | Amount | Ratio | Amount | Ratio |
| (Dollar amounts in thousand) | | | | |
| As of December 31, 2001: | | | | |
| Total Capital (to Risk Weighted Assets) | | | | |
| Consolidated | \$21,919 | 16.21% | \$10,820 | >8.0% |
| Salisbury Bank & Trust Company | 21,739 | 16.09 | 10,812 | >8.0 |
| Tier 1 Capital (to Risk Weighted Assets) | | | | |
| Consolidated | 20,415 | 15.09 | 5,410 | >4.0 |
| Salisbury Bank & Trust Company | 20,235 | 14.97 | 5,406 | >4.0 |
| Tier 1 Capital (to Average Assets) | | | | |
| Consolidated | 20,415 | 7.61 | 10,730 | >4.0 |
| Salisbury Bank & Trust Company | 20,235 | 7.56 | 10,713 | >4.0 |

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| | Actual | | For Capital Adequacy Purposes: | |
|--|----------|--------|--------------------------------|-------|
| | Amount | Ratio | Amount | Ratio |
| (Dollar amounts in thousand) | | | | |
| As of December 31, 2000: | | | | |
| Total Capital (to Risk Weighted Assets) | | | | |
| Consolidated | \$23,998 | 20.05% | \$9,573 | >8.0% |
| Salisbury Bank & Trust Company | 23,658 | 19.80 | 9,558 | >8.0 |
| Tier 1 Capital (to Risk Weighted Assets) | | | | |
| Consolidated | 22,631 | 18.91 | 4,787 | >4.0 |
| Salisbury Bank & Trust Company | 22,291 | 18.66 | 4,779 | >4.0 |
| Tier 1 Capital (to Average Assets) | | | | |
| Consolidated | 22,631 | 9.53 | 9,500 | >4.0 |
| Salisbury Bank & Trust Company | 22,291 | 9.42 | 9,468 | >4.0 |

The declaration of cash dividends is dependent on a number of factors, including regulatory limitations, and the Company's operating results and financial condition. The stockholders of the Company will be entitled to dividends only when, and if, declared by the Company's Board of Directors out of funds legally available therefore. The declaration of future dividends will be subject to favorable operating results, financial conditions, tax considerations, and other factors.

As of December 31, 2001 the Bank is restricted from declaring dividends to the Company in an amount greater than approximately \$9,393,000 as such declaration would decrease capital below the Bank's required minimum level of regulatory capital.

NOTE 13 - DIRECTORS STOCK RETAINER PLAN

At the 2001 annual meeting the stockholders of the Company voted to approve the "Directors Stock Retainer Plan of Salisbury Bancorp, Inc. (the Plan)." This plan provides non-employee directors of the Company with shares of restricted stock of the Company as a component of their compensation for services as directors. The maximum number of shares of stock that may be issued pursuant to the plan shall not exceed 15,000. The first grant date under this plan will precede the 2002 annual meeting of stockholders. Each director whose term of office begins with or continues after the date of the Plan was approved by the stockholders shall be issued an "annual stock retainer" consisting of 120 shares of common stock of the Company.

NOTE 14 - EARNINGS PER SHARE (EPS)

During the years ended December 31, 2001 and 2000 there were no dilutive potential common shares that could have been issued by the Company. Therefore, diluted earnings per share is not presented.

NOTE 15 - RECLASSIFICATION

Certain amounts in the prior years have been reclassified to be consistent with the current year's statement presentation.

NOTE 16 - PARENT COMPANY ONLY FINANCIAL STATEMENTS

The following condensed financial statements are for Salisbury Bancorp, Inc. (Parent Company Only) and should be read in conjunction with the Consolidated Financial Statements of Salisbury Bancorp, Inc. and Subsidiary.

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SALISBURY BANCORP, INC.

(Parent Company Only)

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BALANCE SHEETS

December 31, 2001 and 2000

| ASSETS | 2001 | 2000 |
|--|---------------|---------------|
| ----- | ----- | ----- |
| Checking account in Salisbury Bank & Trust Company | \$ 335 | \$ |
| Money market mutual funds | 470,905 | 661,312 |
| Investments in available-for-sale securities (at fair value) | 230,000 | |
| Investment in subsidiary | 23,182,570 | 22,120,121 |
| Other assets | 2,193 | 3,386 |
| | ----- | ----- |
| Total assets | \$ 23,656,003 | \$ 23,014,819 |
| | ===== | ===== |
| | | |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Dividends payable | \$ 298,695 | \$ 554,179 |
| Other liabilities | (5,838) | 384 |
| | ----- | ----- |
| Total liabilities | 292,857 | 554,563 |
| | ----- | ----- |
| Total stockholders' equity | 23,363,146 | 22,460,256 |
| | ----- | ----- |
| Total liabilities and stockholders' equity | \$ 23,656,003 | \$ 23,014,819 |
| | ===== | ===== |

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SALISBURY BANCORP, INC.

(Parent Company Only)

STATEMENTS OF INCOME

Years Ended December 31, 2001 and 2000

| | 2001 | 2000 |
|---------------------------------|--------------|--------------|
| | ----- | ----- |
| Dividend income from subsidiary | \$ 1,740,000 | \$ 1,330,000 |
| Taxable interest on securities | 14,442 | 44,555 |
| | ----- | ----- |
| | 1,754,442 | 1,374,555 |
| | ----- | ----- |
| | | |
| Legal expense | 8,596 | 9,906 |
| Supplies and printing | 6,211 | 12,828 |
| Other expense | 13,297 | 18,063 |
| | ----- | ----- |

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| | | |
|--|--------------|--------------|
| | 28,104 | 40,797 |
| | ----- | ----- |
| Income before income tax (benefit) expense | | |
| and equity in undistributed net income of subsidiary | 1,726,338 | 1,333,758 |
| Income tax (benefit) expense | (4,645) | 1,464 |
| | ----- | ----- |
| Income before equity in undistributed net income of subsidiary | 1,730,983 | 1,332,294 |
| Equity in undistributed net income of subsidiary | 1,170,220 | 1,516,730 |
| | ----- | ----- |
| Net income | \$ 2,901,203 | \$ 2,849,024 |
| | ===== | ===== |

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SALISBURY BANCORP, INC.

(Parent Company Only)

STATEMENTS OF CASH FLOWS

Years Ended December 31, 2001 and 2000

| | | |
|--|-------------|--------------|
| | 2001 | 2000 |
| | ----- | ----- |
| Cash flows from operating activities: | | |
| Net income | \$2,901,20 | \$ 2,849,024 |
| Adjustments to reconcile net income to net cash provided | | |
| by operating activities: | | |
| Undistributed income of subsidiary | (1,170,220) | (1,516,730) |
| Deferred tax expense | 1,193 | 1,080 |
| Accretion of securities | | (22,262) |
| (Decrease) increase in taxes payable | | (8,081) |
| Increase (decrease) in due to subsidiary | (6,222) | 384 |
| | ----- | ----- |
| Net cash provided by operating activities | 1,725,954 | 1,303,415 |
| | ----- | ----- |
| Cash flows from investing activities: | | |
| Proceeds from sales of available-for-sale securities | | 292,263 |
| Maturities of available-for-sale securities | 230,000 | |
| | ----- | ----- |
| Net cash provided by investing activities | 230,000 | 292,263 |
| | ----- | ----- |
| Cash flows from financing activities: | | |
| Net repurchase of common stock | (691,080) | (816,062) |
| Dividends paid | (1,454,946) | (1,088,830) |
| | ----- | ----- |

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| | | |
|--|-------------|-------------|
| Net cash used in financing activities | (2,146,026) | (1,904,892) |
| | ----- | ----- |
| Net increase (decrease) in cash and cash equivalents | (190,072) | (309,214) |
| Cash and cash equivalents at beginning of year | 661,312 | 970,526 |
| | ----- | ----- |
| Cash and cash equivalents at end of year | \$ 471,240 | \$ 661,312 |
| | ===== | ===== |

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ITEM 8. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

During the two (2) most recent fiscal years, the Company and the Bank have had no changes in or disagreements with their independent accountants on accounting and financial disclosure matters.

PART III

ITEM 9. DIRECTORS, EXECUTIVE OFFICERS, PROMOTERS AND CONTROL PERSONS; COMPLIANCE WITH SECTION 16 (a) OF THE EXCHANGE ACT.

MANAGEMENT OF THE COMPANY

The following table sets forth the name and age of each Executive Officer, his principal occupation for the last five (5) years and the year in which he was first appointed an Executive Officer of the Company.

| NAME | AGE | POSITION | EXECUTIVE OFFICER OF THE COMPANY SINCE: |
|-------------------------|-----|---------------------------------------|---|
| ---- | --- | ----- | ----- |
| John F. Perotti | 55 | President and Chief Executive Officer | 1998 (1) |
| Richard J. Cantele, Jr. | 42 | Secretary | 2001 (2) |
| John F. Foley | 51 | Chief Financial Officer | 1998 (3) |

(1) Mr. Perotti is also the President and Chief Executive Officer of the Bank and has been an Executive Officer of the Bank since 1982.

(2) Mr. Cantele is also the Executive Vice President, Treasurer and Chief Operating Officer of the Bank and has been an Executive Officer of the Bank since 1989.

(3) Mr. Foley is also the Senior Vice President, Comptroller and Principal Financial Officer of the Bank and has been an Executive Officer of the Bank since 1986.

Board of Directors

The Certificate of Incorporation and Bylaws of the Company provide for a Board of Directors of not less than seven (7) members, as determined from time to time by resolution of the Board of Directors. The Board of Directors of the Company is divided into three (3) classes. Classes of directors serve for staggered three (3) year terms. A successor class is to be elected at each annual meeting of shareholders. When the terms of office of the members of one class expire vacant directorships may be filled, until the expiration of the term of the

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vacated directorship, by the vote of a majority of the directors then in office. The Company does not have a nominating committee. Rather, the full Board of Directors performs that function.

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The following table sets forth certain information, as of March 8, 2002 with respect to the directors of the Company.

| NOMINEES FOR ELECTION | | | | | |
|------------------------|-----|-----------------------------------|------------------------|----------|--|
| Name | Age | Position Held with the Company | Director Term Since | Expiring | |
| ---- | --- | ----- | ----- | ----- | |
| John R. H. Blum | 72 | Chairman | 1998 | 2002 | |
| Louise F. Brown | 58 | Director | 1998 | 2002 | |
| Nancy F. Humphreys | 60 | Director | 2001 | 2002 | |
| CONTINUING DIRECTORS | | | | | |
| Gordon C. Johnson 67 | | Director | 1998 | 2003 | |
| Holly J. Nelson | 48 | Director | 1998 | 2003 | |
| Walter C. Shannon, Jr. | 66 | Director | 1998 | 2003 | |
| John F. Perotti | 55 | President, CEO, and Director | 1998 | 2004 | |
| Craig E. Toensing | 64 | Director | 1998 | 2004 | |
| Michael A. Varet | 59 | Director | 1998 | 2004 | |

Presented below is additional information concerning the directors of the Company. Unless otherwise stated, all directors have held the positions described for at least five (5) years.

John R. H. Blum is an attorney in private practice and former Commissioner of Agriculture for the State of Connecticut. He has been a director of the Bank since 1995 and was elected Chairman of the Board of Directors of the Company and the Bank in 1998.

Louise F. Brown has been a director of the Bank since 1992 and is a partner at the Sharon office in the law firm of Gager & Peterson, LLP.

Nancy F. Humphreys has been a director of the Bank since 2001. She retired from Citigroup New York, Citibank in February of 2000, as Managing Director and Treasurer of Global Corporate Investment Bank North America.

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Gordon C. Johnson has been a director of the Bank since 1994 and is a Doctor of Veterinary Medicine.

Holly J. Nelson has been a director of the Bank since 1995. She is a member of Horses North, LLC, a tour operator, and is a partner in Oblong Property Management, LLC.

John F. Perotti is President and Chief Executive Officer of the Company and the Bank. Prior to that he served as Executive Vice President and Chief Operating Office of the Bank and prior to that, he was Vice President and Treasurer of the Bank. He has been a director of the Bank since 1985.

Walter C. Shannon, Jr. is President Emeritus of Wagner McNeil, Inc. and President of William J. Cole Agency, Inc. He has been a director of the Bank since 1993.

Craig E. Toensing has been a director of the Bank since 1995 and retired in December 2001 as Senior Vice President and Trust Officer of the Bank.

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Michael A. Varet is a partner in the law firm of Piper Marbury Rudnick & Wolfe LLP. Mr. Varet has been a director of the Bank since 1997. Section 16(a) Beneficial Ownership Reporting Compliance

Section 16(a) of the Securities Exchange Act of 1934, as amended, requires the Company's executive officers, directors and persons who own more than ten percent (10%) of the Company's Common Stock, to file with the Securities and Exchange Commission (the "SEC") reports of ownership and changes in ownership of the Company's Common Stock. Executive officers, directors and any shareholders owning greater than ten percent (10%) of the Company's Common Stock are required by the SEC's regulations to furnish the Company with copies of all such reports that they file.

Based solely on a review of copies of reports filed with the SEC since January 1, 2001 and of written representations by certain executive officers and directors, all persons subject to the reporting requirements of Section 16(a) are believed by management to have filed the required reports on a timely basis.

ITEM 10. EXECUTIVE COMPENSATION

Fees

During 2001, each director received an annual retainer of \$2,000. In addition, directors received \$500 for each Board of Directors meeting attended and \$200 for each committee meeting attended. Directors' Perotti and Toensing received no additional compensation for their services as directors or members of any board committee during 2001.

The following table provides certain information regarding the compensation paid to certain executive officers of the Company and the Bank for services rendered in all capacities during the fiscal years ended December 31, 2001, 2000 and 1999. No other current executive officer of the Company or the Bank received cash compensation in excess of \$100,000 during the year ended December 31, 2001. All compensation expense was paid by the Bank.

Summary Compensation Table

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| Name and Principal Position ----- | Year ---- | Annual Compensation | | All Other Compensation (\$)(2) (3) ----- |
|---|--------------|------------------------|--------------------|---|
| | | Salary(\$)(1) ----- | Bonus(\$) ----- | |
| John F. Perotti President and Chief Executive Officer of the Company and the Bank | 2001 | \$179,920 | \$25,949 | \$3,400 |
| | 2000 | 172,992 | 38,515 | 3,400 |
| | 1999 | 163,200 | 30,243 | -- |
| Craig E. Toensing (4) Senior Vice President and Trust Officer of the Bank | 2001 | \$134,108 | \$19,530 | \$2,985 |
| | 2000 | 130,200 | 30,825 | \$3,221 |
| | 1999 | 122,808 | 24,641 | --- |
| Richard J. Cantele, Jr. (5) Secretary of the Company Executive Vice President, Treasurer and Chief Operating Officer of the Bank | 2001 | \$ 93,652 | \$17,063 | \$2,145 |
| | 2000 | 87,504 | 17,700 | \$2,104 |
| | 1999 | 75,000 | 13,191 | --- |

- (1) Compensation above does not include accrual of benefits under the Bank's defined pension plan or supplemental arrangements described below.
- (2) The Bank's matching contribution to the 401(k) plan for 2000.
- (3) The Bank's matching contribution to the 401(k) plan for 2001.
- (4) Craig E. Toensing retired as Senior Vice President and Trust Officer of the Bank on December 31, 2001.
- (5) Richard J. Cantele, Jr. was appointed Secretary of the Company on December 27, 2001.

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Insurance

In addition to the cash compensation paid to the executive officers of the Company and the Bank, the executive officers receive group life, health, hospitalization and medical insurance coverage. However, these plans do not discriminate in scope, terms or operation, in favor of officers or directors of the Company and the Bank and are available generally to all full-time employees.

Pension Plan

The Bank maintains a non-contributory defined pension plan for officers and other salaried employees of the Bank who become participants after attaining age 21 and completing one (1) year of service. Pension benefits are based upon average base salary (determined as of each January 1st) during the highest five (5) consecutive years of service prior to attaining normal retirement date. The amount of annual benefit is fifty percent (50%) of average base salary less fifty percent (50%) of the primary Social Security benefit, pro rated for less than 25 years of service, plus one-half of one percent (.5%) of average base salary for each of up to ten (10) additional years of service. This benefit formula may be modified to conform with recent changes in the pension laws.

The present average base salary and years of service to date of Messrs. Perotti, Toensing and Cantele are: Mr. Perotti: \$186,692; 29 years; Mr. Toensing: \$140,331; 21 years; and Mr. Cantele \$90,126; 20 years. The following table shows estimated annual retirement benefits payable at normal retirement date as a straight life annuity for various average base salary and service categories before the offset of a portion of the primary Social Security benefit.

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| Average Base Salary at Retirement ----- | Estimated Annual Retirement Benefit With Years of Service at Retirement Indicated ----- | | | |
|--|---|-------------------|-------------------|-------------------|
| | 10 Years ----- | 20 Years ----- | 25 Years ----- | 35 Years ----- |
| \$ 80,000 | \$16,000 | \$32,000 | \$ 40,000 | \$ 44,000 |
| 90,000 | 18,000 | 36,000 | 45,000 | 49,500 |
| 100,000 | 20,000 | 40,000 | 50,000 | 55,000 |
| 110,000 | 22,000 | 44,000 | 55,000 | 60,500 |
| 120,000 | 24,000 | 48,000 | 60,000 | 66,000 |
| 130,000 | 26,000 | 52,000 | 65,000 | 71,500 |
| 140,000 | 28,000 | 56,000 | 70,000 | 77,000 |
| 150,000 | 30,000 | 60,000 | 75,000 | 82,500 |
| 160,000 | 32,000 | 64,000 | 80,000 | 88,000 |
| 170,000 | 34,000 | 68,000 | 85,000 | 93,500 |
| 180,000 | 36,000 | 72,000 | 90,000 | 99,000 |
| 190,000 | 38,000 | 76,000 | 95,000 | 104,500 |
| 200,000 | 40,000 | 80,000 | 100,000 | 110,000 |
| 210,000 | 42,000 | 84,000 | 105,000 | 115,500 |

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Supplemental Retirement Arrangements

In 1994, the Bank entered into a supplemental retirement arrangement (the "Supplemental Retirement Agreement") with John F. Perotti. Following disability or retirement at the earlier of the age of 65, or after thirty (30) years of service to the Bank, Mr. Perotti will receive monthly payments of \$1,250 (increased by 5% per year or greater to reflect increases in the cost of living index) for a period of ten (10) years. These payments are in addition to any payments under the Bank's retirement plan. The Supplemental Retirement Agreement includes provisions which would prevent Mr. Perotti from working for a competitor in the proximity of the Bank.

Directors Stock Retainer Plan

At the 2001 Annual Meeting, the shareholders of the Company voted to approve the "Directors Stock Retainer Plan of Salisbury Bancorp, Inc." (the

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"Plan"). The Plan provides non-employee directors of the Company with shares of restricted stock of the Company as a component of their compensation for services as non-employee directors. The maximum number of shares of stock that may be issued pursuant to the Plan shall not exceed 15,000. The first grant date under this Plan will precede the 2002 Annual Meeting of Shareholders. Each non-employee director will be issued an "annual stock retainer" consisting of 120 shares of restricted common stock of the Company. The number of shares to be issued to any new non-employee director will be prorated to reflect the number of months which they served as a non-employee director prior to any grant date.

Change in Control Agreements

During 2001, the Bank entered into change in control agreements with the following Executive Officers of the Bank: John F. Perotti, Richard J. Cantele, Jr., John F. Foley, Todd M. Clinton and Diane E. R. Johnstone. The agreements provide that, in the event of a change in control of the Company or Bank, each Executive Officer will be entitled to a lump sum payment equal to his or her annual compensation based upon the most recent aggregate base salary paid to the Executive Officer in the twelve (12) month period immediately preceding the date of change in control. In no event shall such payments be made in an amount which would cause them to be deemed non-deductible to the Bank by reason of the operation of Section 280G of the Internal Revenue Code.

401(k) Plan

The Bank offers a 401(k) profit sharing plan. This plan began in the year 2000. Each Plan Year, the Bank will announce the amount of the matching contributions, if any. The amount of the matching contributions is directly related to the employees' 401(k) salary deferral contribution. For the Plan Year that began January 1, 2001, all eligible participants received a matching contribution equal to 50% of their 401(k) salary deferral contribution to the Plan; however, it is limited to 2% of the plan compensation not to exceed \$3,400. The Plan expense was \$42,874 for 2001.

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ITEM 11. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The following table sets forth certain information as of March 8, 2002 regarding the number of shares of Common Stock beneficially owned by each director and officer and by all directors and officers as a group.

| | Number of Shares (1) | Percentage of Class (2) |
|-------------------------|----------------------|-------------------------|
| John R. H. Blum | 15,336 (3) | 1.08% |
| Louise F. Brown | 3,156 (4) | .22% |
| Richard J. Cantele, Jr. | 2,868 (5) | .20% |
| John F. Foley | 3,696 (6) | .26% |
| Nancy F. Humphreys | 1,000 (7) | .07% |
| Gordon C. Johnson | 1,502 (8) | .11% |

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| | | |
|--|------------------|----------------|
| Holly J. Nelson | 1,048 (9) | .07% |
| John F. Perotti | 10,839 (10) | .76% |
| Walter C. Shannon, Jr. | 3,604 (11) | .25% |
| Craig E. Toensing | 3,000 (12) | .21% |
| Michael A. Varet | 65,646 (13) | 4.62% |
| | ----- | ---- |
| All Directors and Officers as a group of (11 persons) | 111,695 ===== | 7.85% ===== |

- (1) The shareholdings also include, in certain cases, shares owned by or in trust for a director's spouse and/or children or grandchildren, and in which all beneficial interest has been disclaimed by the director.
- (2) Percentages are based upon the 1,422,358 shares of the Bank's Common Stock outstanding and entitled to vote on March 8, 2002. The definition of beneficial owner includes any person who, directly or indirectly, through any contract, agreement or understanding, relationship or otherwise has or shares voting power or investment power with respect to such security.
- (3) Includes 2,100 shares owned by John R. H. Blum's wife.
- (4) Includes 1,068 shares owned by Louise F. Brown as custodian for her daughter.
- (5) Includes 1,182 shares owned jointly by Richard J. Cantele, Jr. and his wife and 6 shares owned by Richard J. Cantele, Jr. as custodian for his daughter.
- (6) Includes 1,518 shares owned jointly by John F. Foley and his wife and 66 shares owned by John F. Foley as custodian for his children.
- (7) Includes 1,000 shares owned jointly by Nancy F. Humphreys and her husband.

(footnotes continued on following page)

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(footnotes continued from previous page)

- (8) Includes 660 shares owned by Gordon C. Johnson's wife and for which Mr. Johnson has disclaimed beneficial ownership.
- (9) Includes 6 shares owned by Holly J. Nelson as guardian for a minor child.
- (10) Includes 9,514 shares owned jointly by John F. Perotti and his wife, 761 shares owned by his wife and 564 shares in trust for his son.
- (11) All shares are owned individually by Walter C. Shannon, Jr.
- (12) Includes 42 shares owned by Craig E. Toensing as custodian for his son.

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- (13) Includes 18,540 shares owned by Michael A. Varet's wife, 12,366 shares which are owned by his son and 6,180 shares owned by his daughter. Michael A. Varet has disclaimed beneficial ownership for all of these shares.

Principal Shareholders of the Company

As of March 8, 2002, management was not aware of any person (including any "group" as that term is used in Section 13 (d) (3) of the Exchange Act) who owns beneficially more than 5% of the Company's Common Stock.

ITEM 12. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

The Company and the Bank have had, and expect to have in the future, transactions in the ordinary course of business with directors, officers, principle shareholders and their associates on substantially the same terms as those available for comparable transactions with others.

John R. H. Blum is Chairman of the Board of Directors and an attorney engaged in the private practice of law. The Company has engaged Mr. Blum in past years and even though his services were not used in 2001, the Company may engage his services in 2002 in connection with certain legal matters.

Louise F. Brown is a director of the Company and a partner in the law firm of Gager & Peterson, LLP. The Company has engaged Ms. Brown in past years and even though her services were not used in 2001, the Company may engage her services in 2002 in connection with certain legal matters.

Walter C. Shannon, Jr. is a director of the Company and the President Emeritus of Wagner McNeil, Inc. which serves as the insurance agent for many of the Company's insurance needs.

The Bank has had, and expects to have in the future, banking transactions in the ordinary course of its business with directors, officers, principal shareholders of the Company, and their associates, on substantially the same terms, including interest rates and collateral on loans, as those prevailing at the same time for comparable transactions with others and such loans did not involve more than the normal risk of collectability or present other unfavorable features. Since January 1, 2001, the highest aggregate outstanding principal amount of all loans extended by the Bank to the Company's directors, executive officers and all associates of such persons as a group was \$1,487,466 representing an aggregate principal amount equal to 5.81% of the equity capital accounts of the Bank.

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ITEM 13. EXHIBITS, LIST AND REPORTS ON FORM 8-K

- (a) The following exhibits are filed as part of this report on Form 10-KSB.

| Exhibit No. ----- | Description ----- |
|----------------------|---|
| 3.1 | Certificate of Incorporation of Salisbury Bancorp, Inc. |
| 3.2 | Bylaws of Salisbury Bancorp, Inc., as amended. (2) |
| 10.1 | Pension Supplement Agreement with |

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John F. Perotti. (3)

- 10.2 Form of change in control agreement with Executive Officers.
- 10.3 Director Stock Retainer Plan.
- 21. Subsidiaries of the Company. (4)

- (1) Exhibit was filed on April 23, 1998 as Exhibit 3.1 to Company's Registration Statement on Form S-4 (No. 333-50857) and is incorporated herein by reference.
- (2) Exhibit was filed on March 30, 2001 as Exhibit 3.2 to the Company's Annual Report Form 10KSB for the Fiscal Year ended December 31, 2001 and is incorporated herein by reference.
- (3) Exhibit was filed on April 23, 1998 as Exhibit 10 to Company's Registration Statement on Form S-4 (No. 333- 50857) and is incorporated herein by reference.
- (4) Exhibit was filed on April 23, 1998 as Exhibit 21 to Company's Registration Statement on Form S-4 (No. 333- 50857) and is incorporated herein by reference.

(b) Reports on Form 8-K: The following reports on Form 8-K were filed during the fourth quarter of the 2001 fiscal year:

- 1. On November 26, 2001 the Company filed a Form 8-K reporting the declaration of a \$.21 per share quarterly cash dividend for the fourth quarter of 2001.

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SIGNATURES

Pursuant to the requirements of Section 13 and 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, in Lakeville, Connecticut on March 25, 2002

SALISBURY BANCORP, INC.

By: /s/ John F. Perotti

John F. Perotti
President and
Chief Executive Officer

By: /s/ John F. Foley

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John F. Foley
Chief Financial Officer

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

| Signature ----- | Title ----- | Date ----- |
|---|---|----------------|
| /s/ John F. Perotti ----- (John F. Perotti) | President, Chief Executive Officer and Director | March 25, 2002 |
| /s/ John R. H. Blum ----- (John R. H. Blum) | Chairman | March 25, 2002 |
| /s/ Louise F. Brown ----- (Louise F. Brown) | Director | March 25, 2002 |
| /s/ Nancy F. Humphreys ----- (Nancy F. Humphreys) | Director | March 25, 2002 |
| /s/ Gordon C. Johnson ----- (Gordon C. Johnson) | Director | March 25, 2002 |
| /s/ Holly J. Nelson ----- (Holly J. Nelson) | Director | March 25, 2002 |
| /s/ Walter C. Shannon, Jr. ----- (Walter C. Shannon, Jr.) | Director | March 25, 2002 |
| /s/ Craig E. Toensing ----- (Craig E. Toensing) | Director | March 25, 2002 |
| /s/ Michael A. Varet ----- (Michael A. Varet) | Director | March 25, 2002 |