

TF FINANCIAL CORP  
Form 10-Q  
November 12, 2010

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SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-Q

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

For the period ended September 30, 2010

- or -

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

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

Commission file number: 0-24168

TF FINANCIAL CORPORATION  
(Exact Name of Registrant as Specified in Its Charter)

Delaware  
(State or Other Jurisdiction of Incorporation  
or Organization)

74-2705050  
(I.R.S. Employer Identification No.)

3 Penns Trail, Newtown, Pennsylvania  
(Address of Principal Executive Offices)

18940  
(Zip Code)

Registrant's telephone number, including area code: (215) 579-4000

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES  NO

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

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Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

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

YES  NO

Indicate the number of shares outstanding of each of the issuer's classes of common stock as of the latest practicable date: November 08, 2010

Class	Outstanding
\$.10 par value common stock	2,686,485 shares

Table of Contents

CONTENTS

PART I-CONSOLIDATED FINANCIAL INFORMATION

<u>Item 1.</u>	<u>Consolidated Financial Statements</u>	<u>3</u>
<u>Item 2.</u>	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>20</u>
<u>Item 3.</u>	<u>Quantitative and Qualitative Disclosures about Market Risk</u>	<u>31</u>
<u>Item 4.</u>	<u>Controls and Procedures</u>	<u>32</u>

PART II-OTHER INFORMATION

<u>Item 1.</u>	<u>Legal Proceedings</u>	<u>33</u>
<u>Item 1A.</u>	<u>Risk Factors</u>	<u>33</u>
<u>Item 2.</u>	<u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	<u>33</u>
<u>Item 3.</u>	<u>Defaults Upon Senior Securities</u>	<u>33</u>
<u>Item 4.</u>	<u>[Removed and Reserved]</u>	<u>33</u>
<u>Item 5.</u>	<u>Other Information</u>	<u>33</u>
<u>Item 6.</u>	<u>Exhibits</u>	<u>33</u>
<u>Signatures</u>		<u>34</u>

Exhibits

<u>31.1</u>	<u>Certification of CEO pursuant to Section 302 of the Sarbanes-Oxley Act of 2002</u>
<u>31.2</u>	<u>Certification of CFO pursuant of Section 302 of the Sarbanes-Oxley Act of 2002</u>
<u>32.</u>	<u>Certification pursuant of Section 906 of the Sarbanes-Oxley Act of 2002</u>

Table of Contents

## TF Financial Corporation and Subsidiaries

## ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS

## CONSOLIDATED BALANCE SHEETS

(Unaudited)

	September 30, 2010	December 31, 2009
	(in thousands)	
<b>ASSETS</b>		
Cash and cash equivalents	\$6,916	\$ 12,801
Investment securities available for sale—at fair value	50,528	40,853
Mortgage-backed securities available for sale—at fair value	71,500	78,198
Mortgage-backed securities held to maturity (fair value of \$3,605 and \$4,033, respectively)	3,268	3,733
Loans receivable, net	519,374	529,652
Loans receivable held for sale	1,078	1,082
Federal Home Loan Bank stock—at cost	9,896	9,896
Accrued interest receivable	2,659	2,777
Premises and equipment, net	6,788	5,523
Goodwill	4,324	4,324
Bank-owned life insurance	17,699	17,190
Other assets	8,553	8,061
<b>TOTAL ASSETS</b>	<b>\$702,583</b>	<b>\$ 714,090</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>Liabilities</b>		
Deposits	\$552,562	\$ 552,716
Borrowings from the Federal Home Loan Bank	68,671	80,241
Advances from borrowers for taxes and insurance	1,485	2,231
Accrued interest payable	1,797	2,818
Other liabilities	3,395	4,210
<b>Total liabilities</b>	<b>627,910</b>	<b>642,216</b>
<b>Stockholders' equity</b>		
Preferred stock, no par value; 2,000,000 shares authorized at September 30, 2010 and December 31, 2009, none issued	—	—
Common stock, \$0.10 par value; 10,000,000 shares authorized, 5,290,000 shares issued and, 2,685,448 and 2,672,603 shares outstanding at September 30, 2010 and December 31, 2009, respectively, net of shares in treasury of 2,604,552 and 2,617,397, respectively	529	529
Additional paid-in capital	54,078	54,009
Unearned ESOP shares	(1,245 )	(1,334 )
Treasury stock-at cost	(54,064 )	(54,331 )
Retained earnings	73,543	72,376

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Accumulated other comprehensive income	1,832	625
Total stockholders' equity	74,673	71,874
<b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>	<b>\$702,583</b>	<b>\$ 714,090</b>

The accompanying notes are an integral part of these statements

Table of Contents

## TF Financial Corporation and Subsidiaries

CONSOLIDATED STATEMENTS OF INCOME  
(Unaudited)

	For the three months ended September 30,		For the nine months ended September 30,	
	2010	2009	2010	2009
	(in thousands, except per share data)			
Interest income				
Loans, including fees	\$7,020	\$7,638	\$21,472	\$22,951
Mortgage-backed securities	886	1,170	2,782	3,849
Investment securities	444	311	1,291	864
Interest-bearing deposits and other	—	1	2	1
<b>TOTAL INTEREST INCOME</b>	<b>8,350</b>	<b>9,120</b>	<b>25,547</b>	<b>27,665</b>
Interest expense				
Deposits	1,757	2,393	5,593	7,347
Borrowings	731	988	2,372	3,481
<b>TOTAL INTEREST EXPENSE</b>	<b>2,488</b>	<b>3,381</b>	<b>7,965</b>	<b>10,828</b>
<b>NET INTEREST INCOME</b>	<b>5,862</b>	<b>5,739</b>	<b>17,582</b>	<b>16,837</b>
Provision for loan losses	1,180	650	2,741	1,905
<b>NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES</b>	<b>4,682</b>	<b>5,089</b>	<b>14,841</b>	<b>14,932</b>
Non-interest income				
Service fees, charges and other operating income	404	464	1,296	1,498
Bank-owned life insurance	170	171	509	501
Gain on sale of investments	—	—	7	306
Gain on sale of loans	353	127	465	528
Gain (loss) on sale of foreclosed real estate	—	34	(137 )	337
<b>TOTAL NON-INTEREST INCOME</b>	<b>927</b>	<b>796</b>	<b>2,140</b>	<b>3,170</b>
Non-interest expense				
Compensation and benefits	2,269	2,601	7,636	7,917
Occupancy and equipment	774	756	2,256	2,174
Professional fees	196	195	680	651
Marketing and advertising	152	118	392	382
FDIC insurance premiums	233	182	686	714
Other operating	603	568	1,760	1,782
<b>TOTAL NON-INTEREST EXPENSE</b>	<b>4,227</b>	<b>4,420</b>	<b>13,410</b>	<b>13,620</b>

INCOME BEFORE INCOME TAXES	1,382	1,465	3,571	4,482
Income taxes	373	353	878	1,128
NET INCOME	\$1,009	\$1,112	\$2,693	\$3,354
Earnings per share—basic	\$0.39	\$0.44	\$1.06	\$1.33
Earnings per share—diluted	\$0.39	\$0.44	\$1.06	\$1.33
Dividends paid per share	\$0.20	\$0.20	\$0.60	\$0.60

The accompanying notes are an integral part of these statements

Table of Contents

## TF Financial Corporation and Subsidiaries

CONSOLIDATED STATEMENTS OF CASH FLOWS  
(Unaudited)

	For the nine months ended September 30,	
	2010	2009
	(in thousands)	
<b>OPERATING ACTIVITIES</b>		
Net income	\$2,693	\$3,354
Adjustments to reconcile net income to net cash provided by operating activities		
Amortization of:		
Mortgage loan servicing rights	290	136
Deferred loan origination fees	114	76
Premiums and discounts on investment securities, net	59	61
Premiums and discounts on mortgage-backed securities, net	63	(172 )
Premiums and discounts on loans, net	128	134
Provision for loan losses	2,741	1,905
Depreciation of premises and equipment	645	670
Increase in value of bank-owned life insurance	(509 )	(501 )
Stock grant expense	12	12
Stock option expense	39	42
Stock-based benefit programs: ESOP	180	161
Proceeds from sale of loans originated for sale	27,326	35,088
Origination of loans held for sale	(27,087 )	(34,797 )
(Gain) loss on sale of:		
Investments	(7 )	(306 )
Loans held for sale	(465 )	(528 )
Foreclosed real estate	137	(337 )
Decrease in:		
Accrued interest receivable	118	169
Other assets	411	467
(Decrease) increase in:		
Accrued interest payable	(1,021 )	198
Other liabilities	(1,426 )	208
<b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>	<b>4,441</b>	<b>6,040</b>
<b>INVESTING ACTIVITIES</b>		
Loan originations	(59,604 )	(67,343 )
Loan principal payments	65,106	75,442



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Principal repayments on mortgage-backed securities held to maturity	462	843
Principal repayments on mortgage-backed securities available for sale	20,649	25,311
Purchase of investment securities available for sale	(8,681 )	(7,856 )
Purchase of mortgage-backed securities available for sale	(13,995 )	(10,608 )
Proceeds from sale of investment securities available for sale	60	5,514
Proceeds from redemption/maturities of investment securities available for sale	590	755
Proceeds from the sale of foreclosed real estate	799	2,497
Purchase of premises and equipment	(1,910 )	(392 )
NET CASH PROVIDED BY INVESTING ACTIVITIES	3,476	24,163

Table of Contents

	For the nine months ended September 30,	
	2010	2009
	(in thousands)	
<b>FINANCING ACTIVITIES</b>		
Net (decrease) increase in customer deposits	(154 )	42,099
Net decrease in short-term borrowings from the Federal Home Loan Bank and other borrowings	—	(32,416 )
Proceeds of long-term Federal Home Loan Bank borrowings	12,884	—
Repayment of long-term Federal Home Loan Bank borrowings	(24,454 )	(35,988 )
Net decrease in advances from borrowers for taxes and insurance	(746 )	(727 )
Treasury stock acquired	—	(101 )
Exercise of stock options	177	115
Tax benefit arising from stock compensation	17	6
Common stock dividends paid	(1,526 )	(1,509 )
<b>NET CASH USED IN FINANCING ACTIVITIES</b>	<b>(13,802 )</b>	<b>(28,521 )</b>
<b>NET(DECREASE)/ INCREASE IN CASH AND CASH EQUIVALENTS</b>	<b>(5,885 )</b>	<b>1,682</b>
Cash and cash equivalents at beginning of period	12,801	2,719
Cash and cash equivalents at end of period	\$6,916	\$4,401
<b>Supplemental disclosure of cash flow information</b>		
<b>Cash paid for:</b>		
Interest on deposits and borrowings	\$8,986	\$10,630
Income taxes	\$1,462	\$825
<b>Non-cash transactions:</b>		
Capitalization of mortgage servicing rights	\$231	\$426
Transfers from loans to foreclosed real estate	\$1,793	\$3,163
Securities available for sale purchased not settled	\$175	\$—

The accompanying notes are an integral part of these statements

Table of Contents

TF FINANCIAL CORPORATION AND SUBSIDIARIES  
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

## NOTE 1 - PRINCIPLES OF CONSOLIDATION

The consolidated financial statements as of September 30, 2010 (unaudited) and December 31, 2009 and for the nine month periods ended September 30, 2010 and 2009 (unaudited) include the accounts of TF Financial Corporation (the “Company”) and its wholly owned subsidiaries Third Federal Bank (the “Bank”), TF Investments Corporation and Penns Trail Development Corporation. The accompanying consolidated balance sheet at December 31, 2009, has been derived from the audited consolidated balance sheet but does not included all of the information and notes required by U. S. GAAP for complete financial statements. The Company’s business is conducted principally through the Bank. All significant intercompany accounts and transactions have been eliminated in consolidation.

## NOTE 2 - BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements were prepared in accordance with the instructions for Form 10-Q and, therefore, do not include all of the disclosures or footnotes required by accounting principles generally accepted in the United States of America (“US GAAP”). In the opinion of management, all adjustments, consisting of normal recurring accruals, necessary for fair presentation of the consolidated financial statements have been included. The results of operations for the period ended September 30, 2010 are not necessarily indicative of the results which may be expected for the entire fiscal year or any other period. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company’s Annual Report on Form 10-K for the fiscal year ended December 31, 2009.

## NOTE 3 - CONTINGENCIES

The Company, from time to time, is a party to routine litigation that arises in the normal course of business. In the opinion of management, the resolution of this litigation, if any, would not have a material adverse effect on the Company’s consolidated financial position or results of operations.

## NOTE 4 - OTHER COMPREHENSIVE INCOME

Comprehensive income is the change in equity of a business enterprise during a period from transactions and other events and circumstances from non-owner sources. Total comprehensive income was \$1.8 million and \$2.3 million for the three months ended September 30, 2010 and 2009, respectively. The components of other comprehensive income are as follows for the three months ended:

	September 30, 2010		
	Before tax amount	Tax (expense) benefit (in thousands)	Net of tax amount
Unrealized gains on securities			
Unrealized holding gains arising during period	\$1,126	\$(381 )	\$745
Pension plan benefit adjustment related to actuarial losses	42	(14 )	28
Other comprehensive income, net	\$1,168	\$(395 )	\$773

September 30, 2009

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	Before tax amount	Tax (expense) benefit (in thousands)	Net of tax amount
Unrealized gains on securities			
Unrealized holding gains arising during period	\$1,749	\$(590 )	\$1,159
Pension plan benefit adjustment related to actuarial losses	46	(15 )	31
Other comprehensive income, net	\$1,795	\$(605 )	\$1,190

7

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Table of Contents

Total comprehensive income was \$3.9 million and \$5.1 million for the nine months ended September 30, 2010 and 2009, respectively. The components of other comprehensive income are as follows for the nine months ended:

	September 30, 2010		
	Before tax amount	Tax (expense) benefit (in thousands)	Net of tax amount
Unrealized gains on securities			
Unrealized holding gains arising during period	\$1,720	\$(586)	\$1,134
Reclassification adjustment for gains realized in net income	(7)	2	(5)
Pension plan benefit adjustment related to prior service costs and actuarial losses	117	(39)	78
Other comprehensive income, net	\$1,830	\$(623)	\$1,207

	September 30, 2009		
	Before tax amount	Tax (expense) benefit (in thousands)	Net of tax amount
Unrealized gains on securities			
Unrealized holding gains arising during period	\$2,878	\$(979)	\$1,899
Reclassification adjustment for gains realized in net income	(306)	104	(202)
Pension plan benefit adjustment related to actuarial losses	137	(50)	87
Other comprehensive income, net	\$2,709	\$(925)	\$1,784

## NOTE 5—EARNINGS PER SHARE

The following tables illustrate the reconciliation of the numerators and denominators of the basic and diluted earnings per share computations (dollars in thousands, except share and per share data):

	Three months ended September 30, 2010		
	Income (numerator)	Weighted average shares (denominator)	Per share Amount
Basic earnings per share			
Income available to common stockholders	\$ 1,009	2,559,466	\$ 0.39
Effect of dilutive securities			
Stock options and grants	—	—	—
Diluted earnings per share			
Income available to common stockholders plus effect of dilutive securities	\$ 1,009	2,559,466	\$ 0.39



Table of Contents

	Nine months ended September 30, 2010		
	Income	Weighted	Per share
	(numerator)	average	Amount
		shares	
		(denominator)	
Basic earnings per share			
Income available to common stockholders	\$ 2,693	2,551,353	\$ 1.06
Effect of dilutive securities			
Stock options and grants	—	—	—
Diluted earnings per share			
Income available to common stockholders plus effect of dilutive securities	\$ 2,693	2,551,353	\$ 1.06

There were 193,880 options to purchase shares of common stock at a price range of \$25.33 to \$34.14 per share which were outstanding during the three and nine months ended September 30, 2010 that were not included in the computation of diluted earnings per share because the options' exercise prices were greater than the average market price of the common shares.

	Three months ended September 30, 2009		
	Income	Weighted	Per share
	(numerator)	average	Amount
		shares	
		(denominator)	
Basic earnings per share			
Income available to common stockholders	\$ 1,112	2,523,429	\$ 0.44
Effect of dilutive securities			
Stock options and grants	—	—	—
Diluted earnings per share			
Income available to common stockholders plus effect of dilutive securities	\$ 1,112	2,523,429	\$ 0.44

	Nine months ended September 30, 2009		
	Income	Weighted	Per share
	(numerator)	average	Amount
		shares	
		(denominator)	
Basic earnings per share			
Income available to common stockholders	\$ 3,354	2,520,228	\$ 1.33
Effect of dilutive securities			
Stock options and grants	—	—	—
Diluted earnings per share			
Income available to common stockholders plus effect of dilutive securities	\$ 3,354	2,520,228	\$ 1.33

There were 256,883 options to purchase shares of common stock at a price range of \$20.30 to \$34.14 per share which were outstanding during the three and nine months ended September 30, 2009 that were not included in the

computation of diluted earnings per share because the options' exercise prices were greater than the average market price of the common shares.



Table of Contents

## NOTE 6—INVESTMENT AND MORTGAGE-BACKED SECURITIES

The amortized cost, gross unrealized gains and losses, and fair value of the Company's investment securities at September 30, 2010 and December 31, 2009, are summarized as follows:

	Amortized cost	September 30, 2010 Gross unrealized gains (in thousands)	Gross unrealized losses	Fair value
<b>Investment securities available for sale</b>				
U.S. Government and federal agencies	\$6,000	\$98	\$—	\$6,098
Corporate debt securities	3,340	241	—	3,581
State and political subdivisions	38,212	2,623	(84 )	40,751
Equity securities	97	1	—	98
	\$47,649	\$2,963	\$(84 )	\$50,528
<b>Residential mortgage-backed securities issued by quasi-governmental agencies</b>				
Residential mortgage-backed securities privately issued	\$54,766	\$2,135	\$—	\$56,901
Residential mortgage-backed securities available for sale	14,496	147	(44 )	14,599
	\$69,262	\$2,282	\$(44 )	\$71,500
Residential mortgage-backed securities held to maturity	\$3,268	\$337	\$—	\$3,605
<b>Investment securities available for sale</b>				
	Amortized cost	December 31, 2009 Gross unrealized gains (in thousands)	Gross unrealized losses	Fair value
U.S. Government and federal agencies	\$3,000	\$—	\$(55 )	\$2,945
Corporate debt securities	3,340	177	—	3,517
State and political subdivisions	33,180	1,170	(109 )	34,241
Equity securities	150	—	—	150
	\$39,670	\$1,347	\$(164 )	\$40,853
<b>Residential mortgage-backed securities issued by quasi-governmental agencies</b>				
Residential mortgage-backed securities privately issued	\$68,707	\$2,483	\$(39 )	\$71,151
Residential mortgage-backed securities available for sale	7,270	—	(223 )	7,047
	\$75,977	\$2,483	\$(262 )	\$78,198
Residential mortgage-backed securities held to maturity	\$3,733	\$300	\$—	\$4,033

Gross realized gains were \$7,000 for the nine months ended September 30, 2010. These gains resulted from the sale of investment equity securities of \$53,000. Gross realized gains were \$306,000 for the nine months ended September 30, 2009. These gains resulted from the sale of investment securities of \$5.1 million.



Table of Contents

The Company also holds stock in the Federal Home Loan Bank of Pittsburgh (“FHLB”) totaling \$9.9 million as of September 30, 2010 and December 31, 2009. The Company is required to maintain a minimum amount of FHLB stock as determined by its borrowing levels and amount of eligible assets. At September 30, 2010 the Company was required to hold \$4.6 million in FHLB stock. FHLB stock can only be repurchased by the FHLB or sold to another member, and all sales must be at par. The Company holds FHLB stock as a long term investment based on the ultimate recoverability of the par value. During the fourth quarter of 2008, the FHLB suspended the repurchase of stock and dividend payments which prompted the Company to give consideration to evaluating the potential impairment of the investment. The Company evaluates potential impairment of its investment in FHLB stock quarterly and considers the following: 1) the magnitude and direction of the change in the net assets of the FHLB as compared to the capital stock amount and the duration of this condition, 2) the ability of the FHLB to make payments required by law or regulation and the level of such payments in relation to the operating performance of the FHLB, 3) the impact of regulatory changes on the FHLB and on its members, and 4) the liquidity position of the FHLB. After evaluating these factors the Company has concluded that the par value of its investment in FHLB stock is recoverable and no impairment has been recorded at September 30, 2010 or December 31, 2009.

The table below indicates the length of time individual securities have been in a continuous unrealized loss position at September 30, 2010:

Description of Securities	Number of Securities	Less than 12 months		12 months or longer		Total	
		Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair value	Unrealized Loss
(in thousands)							
State and political subdivisions	2	\$1,096	\$(84 )	\$—	\$—	\$1,096	\$(84 )
Residential mortgage-backed securities privately issued	2	5,136	(44 )	—	—	5,136	(44 )
Total temporarily impaired securities	4	\$6,232	\$(128 )	\$—	\$—	\$6,232	\$(128 )

The table below indicates the length of time individual securities have been in a continuous unrealized loss position at December 31, 2009:

Description of Securities	Number of Securities	Less than 12 months		12 months or longer		Total	
		Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair value	Unrealized Loss
(in thousands)							
U.S. Government and federal agencies	1	\$2,945	\$(55 )	\$—	\$—	\$2,945	\$(55 )
State and political subdivisions	6	4,086	(109 )	—	—	4,086	(109 )
	2	4,352	(39 )	—	—	4,352	(39 )

Residential mortgage-backed securities issued by quasi-governmental agencies								
Residential mortgage-backed securities privately issued	4	5,536	(160 )	1,511	(63 )	7,047	(223 )	
Total temporarily impaired securities	13	\$16,919	\$(363 )	\$1,511	\$(63 )	\$18,430	\$(426 )	

On a quarterly basis, temporarily impaired securities are evaluated to determine whether such impairment is other-than-temporary impairment (“OTTI”). This evaluation involves consideration of the length of time and the amount by which the fair value has been lower than amortized cost, the financial condition and credit rating of the issuer, the changes in fair value in relation to the change in market interest rates and other relevant information. In addition, with respect to mortgage-backed securities issued by government and quasi-governmental agencies (i. e. Government National Mortgage Association (“GNMA”), Federal Home Loan Mortgage Corporation (“FHLMC”) and Federal National Mortgage Association (“FNMA”)) the Company considers the ultimate payment of principal and interest as an obligation of the United States Government and thus assured. With respect to mortgage-backed securities issued by private parties, the Company studies delinquencies, loss rates, loss severity and other information related to the underlying loans in order to form an opinion regarding the possibility of a cash flow shortfall. The Company also evaluates its intent to hold, intent to sell or need to sell the securities in light of its investment strategy, cash flow needs, interest rate risk position, prospects for the issuer and all other relevant factors.

Table of Contents

With respect to investments in equity securities, if it is determined that the impairment for an individual security is OTTI such impairment would be recognized as a reduction to non-interest income in the consolidated statement of income. With respect to debt securities, if it has been determined that the impairment for an individual security is OTTI, but the Company does not intend to sell the security and concludes that it is more likely than not that it will not be required to sell the security before recovering the carrying value, which may be maturity, the OTTI would be separated into the “credit” and “other” components. The “other” component of the OTTI would be included in other comprehensive loss, net of the tax effect, and the “credit” component of the OTTI would be included as a reduction to non-interest income in the consolidated statement of income. Otherwise, the OTTI impairment of debt securities would be recognized as a reduction to non-interest income in the consolidated statements of income. Accordingly, the Company has performed this evaluation and has determined that the unrealized losses at September 30, 2010 and December 31, 2009, respectively are not considered other-than-temporary and are therefore reflected in other comprehensive income.

At September 30, 2010, temporarily impaired securities were all debt securities classified as available for sale. There were no temporarily impaired equity securities. The Company did not intend to sell any of the temporarily impaired securities and has concluded that it will not be required to sell any of the temporarily impaired securities. Upon an evaluation of each individual debt security, the Company determined that the temporary impairment was predominately caused by widening interest rate spreads over the relevant interest rate benchmark in relation to the Company’s amortized cost, and not caused by deterioration in credit quality. Thus, the Company considered the impairment of each security to be temporary and not OTTI.

## NOTE 7—LOANS RECEIVABLE

Loans receivable are summarized as follows:

	September 30, 2010	December 31, 2009 (in thousands)
Held for investment:		
First mortgage loans		
Secured by one-to-four family residences	\$ 270,603	\$ 271,651
Secured by non-residential properties and/or non—owner occupied residential properties	137,919	134,584
Construction loans	23,308	29,671
Total first mortgage loans	431,830	435,906
Other loans		
Commercial-business, real estate secured	33,007	33,514
Commercial-business, non-real estate secured	5,541	7,462
Home equity and second mortgage	53,407	54,811
Other consumer	2,532	2,565
Total other loans	94,487	98,352
Total loans	526,317	534,258
Net deferred loan origination costs and unamortized premiums	663	609
Less allowance for loan losses	(7,606 )	(5,215 )
Total loans receivable	\$ 519,374	\$ 529,652
Held for sale:		
First mortgage loans		
Secured by one-to-four family residences	\$ 1,078	\$ 1,082



Table of Contents

Activity in the allowance for loan losses is summarized as follows (in thousands):

	For the nine months ended September 30,	
	2010	2009
Balance at January 1,	\$5,215	\$3,855
Provision charged to income	2,741	1,905
Charge-offs:		
Secured by one-to-four family residences	(10 )	(97 )
Secured by non-residential properties and/or non—owner occupied residential properties	(174 )	(278 )
Construction loans	—	(1,092 )
Commercial-business, non-real estate secured	(146 )	—
Home equity and second mortgage	—	(6 )
Other consumer	(28 )	(27 )
Recoveries:		
Commercial-business, non-real estate secured	—	22
Other consumer	8	10
Balance at September 30,	\$7,606	\$4,292

## NOTE 8- FAIR VALUE MEASUREMENTS

The following table presents information about the Company's assets and liabilities measured at fair value on a recurring basis as of September 30, 2010. Fair value is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. A fair value measurement hierarchy has been established for inputs in valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements).

The fair value hierarchy levels are summarized below:

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2 inputs are inputs that are observable for the asset or liability, either directly or indirectly.
- Level 3 inputs are unobservable and contain assumptions of the party fair valuing the asset or liability.

Table of Contents

Determination of the appropriate level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement for the instrument or security. Assets and liabilities measured at fair value on a recurring basis segregated by fair value hierarchy level are summarized below (dollars in thousands):

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance as of September 30, 2010
At September 30, 2010				
Assets				
Investment securities available for sale				
U.S. Government and federal agencies	\$—	\$6,098	\$ —	\$ 6,098
Corporate debt securities	—	3,581	—	3,581
State and political subdivisions	—	40,751	—	40,751
Equity securities	98	—	—	98
Total investment securities available for sale	\$98	\$50,430	\$ —	\$ 50,528
Residential mortgage-backed securities issued by quasi-governmental agencies				
Residential real estate mortgage - backed securities privately issued	—	14,599	—	14,599
Total mortgage-backed securities available for sale	\$—	\$71,500	\$ —	\$ 71,500
At December 31, 2009				
Assets				
Investment securities available for sale				
U.S. Government and federal agencies	\$—	\$2,945	\$ —	\$ 2,945
Corporate debt securities	—	3,517	—	3,517
State and political subdivisions	—	34,241	—	34,241
Equity securities	150	—	—	150
Total investment securities available for sale	\$150	\$40,703	\$ —	\$ 40,853
	\$—	\$71,151	\$ —	\$ 71,151



Residential mortgage-backed securities issued by quasi-governmental agencies				
Residential real estate mortgage - backed securities privately issued	—	7,047	—	7,047
Total mortgage-backed securities available for sale	\$—	\$78,198	\$—	\$ 78,198
Forward loan sales	\$—	\$—	\$ 21	\$ 21

Active listed equities are classified within Level 1 of the fair value hierarchy. Investment securities available for sale and mortgage-backed securities available for sale are valued primarily by a third party pricing agent. U.S. Government and federal agency and corporate debt securities are primarily priced through a multi-dimensional relational model, a Level 2 hierarchy, which incorporates dealer quotes and other market information including, defined sector breakdown, benchmark yields, base spread, yield to maturity, and corporate actions. State and political subdivision securities are also valued within the Level 2 hierarchy using inputs with a series of matrices that reflect benchmark yields, ratings updates, and spread adjustments. Mortgage-backed securities include FHLMC, GNMA, and FNMA certificates and privately issued real estate mortgage investment conduits which are valued under a Level 2 hierarchy using a matrix correlation to benchmark yields, spread analysis, and prepayment speeds.

Table of Contents

The fair value of forward loan sales is determined at the time the underlying loan is identified as held for sale with changes in fair value correlated to the change in secondary market loan pricing. The value is adjusted to reflect the Company's historical loan "fallout" experience which incorporates such factors as changes in market rates, origination channels and loan purpose.

The following table presents additional information about assets measured at fair value on a recurring basis for which the Company has utilized Level 3 inputs to determine fair value (in thousands):

	Forward loan sales
Beginning balance, January 1, 2010	\$ 21
Total gains (losses) — realized/unrealized:	
Included in earnings	(21)
Included in other comprehensive income	—
Purchases, issuances, and settlements	—
Ending balance, September 30, 2010	\$ —

Assets and liabilities measured at fair value on a nonrecurring basis segregated by fair value hierarchy level are summarized below (dollars in thousands):

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance as of September 30, 2010
At September 30, 2010				
Assets				
Impaired loans	\$—	\$—	\$ 19,608	\$ 19,608
Real estate acquired through foreclosure	\$—	\$—	\$ 2,153	\$ 2,153
Mortgage servicing rights	\$—	\$637	\$ —	\$ 637

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance as of December 31, 2009
At December 31, 2009				
Assets				
Impaired loans	\$—	\$—	\$ 7,744	\$ 7,744
Real estate acquired through foreclosure	\$—	\$—	\$ 1,279	\$ 1,279
Mortgage servicing rights	\$—	\$696	\$ —	\$ 696

Impaired loans are evaluated and valued at the time the loan is identified as impaired, at the lower of the recorded investment in the loan or fair value. Impaired loans secured by real estate totaled \$19.6 million and \$7.7 million at September 30, 2010 and December 31, 2009, respectively. Real estate acquired through foreclosure is initially valued at the lower of the recorded investment in the loan or fair value at foreclosure and subsequently adjusted for further decreases in market value, if necessary. Fair value is determined by using the value of the collateral securing the loans and is therefore classified as a Level 3 hierarchy. The value of the real estate securing impaired loans and real estate acquired through foreclosure is based on appraisals prepared by qualified independent licensed appraisers contracted by the Company to perform the assessment.

Table of Contents

The Company initially recognizes and measures servicing assets based on the fair value of the servicing right at the time the loan is sold. The Company uses the amortized cost method for subsequent measurement of its servicing assets and evaluates the recorded value for impairment quarterly. The Company retains a qualified valuation service to calculate the amortized cost and to determine the fair value of the mortgage servicing rights. The valuation service utilizes discounted cash flow analyses adjusted for prepayment speeds, market discount rates and conditions existing in the secondary servicing market. Hence, the fair value of mortgage servicing rights is deemed a Level 2 hierarchy. At September 30, 2010, the amortized cost basis of the Company's mortgage servicing rights was \$925,000 and the fair value of \$637,000 was included in other assets in the consolidated balance sheets.

## NOTE 9- FAIR VALUE OF FINANCIAL INSTRUMENTS

For the Bank, as for most financial institutions, the majority of its assets and liabilities are considered financial instruments. However, many such instruments lack an available trading market as characterized by a willing buyer and willing seller engaging in an exchange transaction. Also, it is the Company's general practice and intent to hold its financial instruments to maturity or available for sale and to not engage in trading or significant sales activities. For fair value disclosure purposes, the Company substantially utilized the fair value measurement criteria as explained in Note 8- Fair Value Measurements. Additionally, the Company used significant estimations and present value calculations to prepare this disclosure.

Changes in the assumptions or methodologies used to estimate fair values may materially affect the estimated amounts. In addition, there may not be reasonable comparability between institutions due to the wide range of permitted assumptions and methodologies in the absence of active markets. This lack of uniformity gives rise to a high degree of subjectivity in estimating financial instrument fair values.

Fair values have been estimated using data which management considered the best available, as generally provided by estimation methodologies deemed suitable for the pertinent category of financial instrument. The estimation methodologies, resulting fair values and recorded carrying amounts are as follows:

The fair value of cash and cash equivalents equals historical book value. The fair value of investment and mortgage backed securities is described and presented under fair value measurement guidelines as amended.

	September 30, 2010		December 31, 2009	
	Fair value	Carrying value	Fair value	Carrying value
	(in thousands)			
Cash and cash equivalents	\$6,916	\$6,916	\$12,801	\$12,801
Investment securities	50,528	50,528	40,853	40,853
Mortgage-backed securities	75,105	74,768	82,231	81,931

The fair value of the loans receivable, net has been estimated using the present value of cash flows, discounted at the approximate current market rates, and giving consideration to estimated prepayment risk but not adjusted for credit risk. Loans receivable, net also includes loans receivable held for sale.

	September 30, 2010		December 31, 2009	
	Fair value	Carrying value	Fair value	Carrying value
	(in thousands)			
Loans receivable, net	\$550,932	\$520,452	\$539,670	\$530,734

The fair value of deposits and borrowings with stated maturities has been estimated using the present value of cash flows, discounted at rates approximating current market rates for similar liabilities. Fair value of deposits and borrowings with floating interest rates is generally presumed to approximate the recorded carrying amounts.

	September 30, 2010		December 31, 2009	
	Fair value	Carrying value	Fair value	Carrying value
	(in thousands)			
<b>Liabilities</b>				
Deposits with stated maturities	\$215,747	\$212,087	\$228,676	\$225,093
Borrowings with stated maturities	\$71,266	\$68,671	\$82,947	\$80,241

Table of Contents

The fair value of deposits and borrowings with no stated maturities is generally presumed to approximate the carrying amount (the amount payable on demand). Fair value deposits and borrowings with floating interest rates are generally presumed to approximate the recorded carrying amounts.

	September 30, 2010		December 31, 2009	
	Fair value	Carrying value	Fair value	Carrying value
	(in thousands)			
Deposits with no stated maturities	\$340,475	\$340,475	\$327,623	\$327,623

The Bank's remaining assets and liabilities are not considered financial instruments. No disclosure of the relationship value of the Bank's deposits is required.

## NOTE 10- STOCK BASED COMPENSATION

The Company has stock benefit plans that allow the Company to grant options and restricted stock to employees and directors. The awards, which have a term of up to 10 years when issued, vest over a three to five year period. The exercise price of each award equals the market price of the Company's stock on the date of the grant. At September 30, 2010, there was \$97,000 of total unrecognized compensation cost, net of estimated forfeitures, related to non-vested awards under the Plan. That cost is expected to be recognized over a weighted average period of 17.2 months. Option activity under the Company's stock option plan as of September 30, 2010 was as follows:

	Number of shares	Weighted average exercise price per share	2010 Weighted average remaining contractual term (in years)	Aggregate intrinsic value (\$ 000)
Outstanding at January 1, 2010	271,646	\$ 26.23		
Options granted	—	—		
Options exercised	(12,845)	13.76		
Options forfeited	(6,865)	27.83		
Options expired	(3,383)	28.25		
Outstanding at September 30, 2010	248,553	\$ 26.80	1.83	\$ 16
Options exercisable at September 30, 2010	210,859	\$ 27.76	1.30	\$ 16

The aggregate intrinsic value in the table above represents the total pre-tax intrinsic value (the difference between the Company's closing stock price on the last trading day of the third quarter and the exercise price, multiplied by the number of in-the-money options).

The aggregate intrinsic value of options exercised during the nine months ended September 30, 2010 and 2009 was \$76,000 and \$17,500, respectively. Exercise of stock options during the nine months ended September 30, 2010 and 2009 resulted in cash receipts of \$177,000 and \$115,000, respectively.

Stock-based compensation expense included in net income related to stock options was \$13,000 and \$14,000 for the three months ended September 30, 2010 and 2009, respectively, resulting in a tax benefit of \$5,000 for each of the

periods. Stock-based compensation expense included in net income related to stock options was \$39,000 and \$42,000 for the nine months ended September 30, 2010 and 2009, respectively, resulting in a tax benefit of \$13,000 and \$14,000 for each of the periods.

Stock-based compensation expense included in net income related to stock grants was \$4,000 for both three month periods ended September 30, 2010 and 2009, respectively. Stock-based compensation expense included in net income related to the Company's employee stock ownership plan totaled \$51,000 and \$41,000 for the three months ended September 30, 2010 and 2009, respectively. Stock-based compensation expense included in net income related to stock grants was \$12,000 for both of the nine month periods ended September 30, 2010 and 2009. Stock-based compensation expense included in net income related to the Company's employee stock ownership plan totaled \$145,000 and \$124,000 for the nine months ended September 30, 2010 and 2009, respectively.

Table of Contents

## NOTE 11- EMPLOYEE BENEFIT PLANS

Net periodic defined benefit pension cost included the following (in thousands):

	Three months ended September 30,	
	2010	2009
Components of net periodic benefit cost		
Service cost	\$138	\$118
Interest cost	74	62
Expected return on plan assets	(141 )	(93 )
Amortization of prior service cost	1	—
Recognized net actuarial loss	41	46
<b>Net periodic benefit cost</b>	<b>\$113</b>	<b>\$133</b>

	Nine months ended September 30,	
	2010	2009
Components of net periodic benefit cost		
Service cost	\$415	\$354
Interest cost	222	186
Expected return on plan assets	(414 )	(278 )
Amortization of prior service cost	2	—
Recognized net actuarial loss	115	137
<b>Net periodic benefit cost</b>	<b>\$340</b>	<b>\$399</b>

There was no employer contribution for the nine months ended September 30, 2010 and 2009.

## NOTE 12 — ACCOUNTING STANDARDS UPDATE

In January 2010, the FASB added new requirements for disclosures of fair value measurements. The new requirements include disclosure about transfers in and out of Levels 1 and 2 and separate disclosures about purchases, sales, issuances and settlements relating to Level 3 measurements. The guidance includes new disclosures and changes to clarify existing disclosure requirements. The guidance is effective for the first reporting period (including interim periods) beginning after December 15, 2009, except for the requirement to provide Level 3 activity of purchases, sales, issuances, and settlements on a gross basis, which will be effective for fiscal years beginning after December 15, 2010, and for interim periods within those years. Early adoption is permitted. The required additional disclosures are contained in Note 8-Fair Value Measurements.

In April 2010, the FASB issued guidance on the treatment for a modified loan that was acquired as part of a pool of assets. The guidance establishes that entities should not evaluate whether a modification of loans that are part of a pool meets the criteria for a troubled debt restructuring. In addition, modified loans should not be removed from the pool unless certain criteria are met. The amendment will be effective for loans that are part of an asset pool and are modified during financial reporting periods that end July 15, 2010 or later. The Company does not anticipate that the adoption of this guidance will have a significant impact on the Company's financial statements.





Table of Contents

In July, 2010 FASB issued an amendment which will require disclosures about the credit quality of financing receivables and the allowance for credit losses. The amendment will improve the transparency in financial reporting by public and non public companies that hold financing receivables which include loans, lease receivables and other long-term receivables. The additional disclosures will include aging of past due receivables, credit quality indicators and modifications of financing receivables. The disclosures should also included information on the development of the credit loss allowance and the management of credit exposures. The amendment will be effective for financial reporting periods ending after December 15, 2010. The Company does not anticipate that the adoption of this guidance will have a significant impact on the Company's financial statements.

Table of Contents

TF FINANCIAL CORPORATION AND SUBSIDIARIES

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL POSITION AND RESULTS OF OPERATIONS

GENERAL

The Company may from time to time make written or oral "forward-looking statements", including statements contained in the Company's filings with the Securities and Exchange Commission (including this Quarterly Report on Form 10-Q and the exhibits thereto), in its reports to stockholders and in other communications by the Company, which are made in good faith by the Company pursuant to the "Safe Harbor" Provisions of the Private Securities Litigation Reform Act of 1995.

These forward-looking statements involve risks and uncertainties, such as statements of the Company's plans, objectives, expectations, estimates and intentions that are subject to change based on various important factors (some of which are beyond the Company's control). The following factors, among others, could cause the Company's financial performance to differ materially from the plans, objectives, expectations, estimates and intentions expressed in such forward-looking statements: the strength of the United States economy in general and the strength of the local economies in which the Company conducts operations; the effects of, and changes in, trade, monetary and fiscal policies and laws, including interest rate policies of the Board of Governors of the Federal Reserve System, inflation, interest rate, market and monetary fluctuations; the timely development of and acceptance of new products and services of the Company and the perceived overall value of these products and services by users, including the features, pricing and quality compared to competitors' products and services; the willingness of users to substitute competitors' products and services for the Company's products and services; the success of the Company in gaining regulatory approval of its products and services, when required; the impact of changes in financial services' laws and regulations (including laws concerning taxes, banking, securities and insurance); technological changes, acquisitions; changes in consumer spending and saving habits; and the success of the Company at managing the risks involved in the foregoing.

The Company cautions that the foregoing list of important factors is not exclusive. The Company does not undertake to update any forward-looking statement, whether written or oral, that may be made from time to time by or on behalf of the Company.

Financial Position

The Company's total assets at September 30, 2010 and December 31, 2009 were \$702.6 million and \$714.1 million, respectively, representing a decrease of \$11.5 million, or 1.6% during the nine-month period. Loans receivable, net decreased by \$10.3 million during the first nine months of 2010. Principal repayments of loans receivable totaled \$65.1 million which were offset by originations of consumer and single-family residential mortgage loans totaling \$51.8 million and of commercial loans totaling \$14.5 million. During this period, the Company increased the allowance for loan losses by \$2.7 million and transferred \$1.8 million from loans to real estate acquired through foreclosure. Loans receivable held for sale remained steady as proceeds of \$27.3 million from the sale of loans in the secondary market were offset by loans originated for sale of \$27.1 million. Mortgage-backed securities available for sale decreased by \$6.7 million due to principal repayments received of \$20.6 million offset by purchases of \$14.0 million. Mortgage-backed securities held to maturity decreased by \$0.5 million mainly as a result of principal repayments. Investment securities available for sale increased \$9.7 million due to purchases of municipal and federal agency bonds of \$8.7 million as well as a \$1.7 million increase in the fair value of the securities, offset by maturities and sales of \$0.6 million. As a result of the Company's cash-related activities, cash and cash equivalents decreased by \$5.9 million during 2010.

Total liabilities decreased by \$14.3 million during the first nine months of 2010. Advances from the Federal Home Loan Bank decreased by \$11.6 million, the net result of scheduled amortization and maturities of \$24.5 million offset by a \$12.9 million increase in long-term borrowings. Total deposit balances remained level during the period; money market, non-interest checking and savings accounts increased \$12.9 million whereas retail certificates of deposit decreased of \$13.0 million.

Total consolidated stockholders' equity of the Company was \$74.7 million or 10.6% of total assets at September 30, 2010. During the first nine months of 2010, the Company issued 12,845 shares of common stock as a result of stock option exercises. At September 30, 2010, there were approximately 102,000 shares available for repurchase under the previously announced share repurchase plan.

Table of Contents

## Asset Quality

Non-performing loans include impaired loans and loan balances past due over 90 days for which the accrual of interest has been discontinued. The following table sets forth information regarding the Company's asset quality:

	September 30, 2010	December 31, 2009	September 30, 2009		
	(in thousands)				
Non-performing loans with a related allowance					
Secured by non-residential properties and/or non—owner occupied residential properties	\$ 940	\$ —	\$ —		
Construction loans	3,887	2,389	—		
Commercial-business, real estate secured	2,605	—	—		
Commercial-business, non-real estate secured	44	—	—		
Non-performing loans without a related allowance					
Secured by one-to-four family residences(1)	1,470	1,120	651		
Secured by non-residential properties and/or non—owner occupied residential properties (2)	3,299	2,506	823		
Construction loans	354	2,167	1,497		
Commercial-business, real estate secured	7,862	—	—		
Home equity and second mortgage	1,084	99	127		
Other consumer	—	4	—		
Total non-performing loans	\$ 21,545	\$ 8,285	\$ 3,098		
Total loans past due 90 days as to interest or principal and accruing interest	\$ —	\$ —	\$ —		
Ratio of non-performing loans to gross loans	4.08	%	1.55	%	0.58
Ratio of non-performing loans to total assets	3.07	%	1.16	%	0.44
Real estate owned	\$ 2,153	\$ 1,279	\$ 999		
Ratio of total non-performing assets to total assets	3.37	%	1.34	%	0.58
Ratio of allowance for loan losses to total loans	1.44	%	0.97	%	0.80
Ratio of allowance for loan losses to non-performing loans	35.30	%	62.95	%	138.54
Loans delinquent 30-89 days(3)	\$ 2,701	\$ 934	\$ 87		

(1) Included in this category of non-performing loans at September 30, 2010 and December 31, 2009 are three troubled debt restructurings with combined balances of \$840,000 and \$844,000, respectively. There were no troubled

debt restructurings at September 30, 2009.

(2) Included in this category of non-performing loans at September 30, 2010 and December 31, 2009 is one troubled debt restructuring with a loan balance of \$560,000. There were no troubled debt restructurings at September 30, 2009.

(3) Loans delinquent 30-89 days are performing assets and continue to accrue interest.

#### Non-performing loans with a related allowance

Loans secured by non-residential properties and/or non-owner occupied residential properties includes a loan secured by a parcel of land. The borrower is attempting to sell the property and intends to apply the proceeds of the sale towards the outstanding loan balance. The Bank has allocated \$120,000 of the allowance for loan losses to this loan, equal to the difference between the loan balance and the fair value less estimated selling costs.

Construction loans include a loan with a balance of \$2.4 million, secured by a largely completed and partially occupied commercial office building, and the personal guarantee of the borrowers. The Bank has allocated to this loan \$782,000 of the allowance for loan losses, equal to the difference between the loan balance plus other acquisition costs and the fair value based upon a recent appraisal less estimated costs to sell. The Bank has initiated foreclosure proceedings.

Also included in construction loans is a loan with a balance of \$1.5 million secured by two contiguous parcels of commercial real estate and a lien on the guarantor's personal residence. The Bank has allocated to this loan \$592,000 of the allowance for loan losses, equal to the difference between the loan balance plus other acquisition costs and the fair value based upon a recent appraisal less estimated costs to sell. The Bank has initiated foreclosure proceedings and the borrower has filed for bankruptcy protection under Chapter 11 of the U.S. Bankruptcy Code.

## Table of Contents

Commercial –business loans secured by real estate include a loan secured by a parcel of vacant land approved for townhome development. The Bank has allocated \$398,000 of the allowance for loan losses to the loan, equal to the difference between the loan balance plus other acquisition costs and the fair value based upon a recent appraisal less estimated costs to sell. The Bank has initiated foreclosure proceedings.

### Non-performing loans without a related allowance

Loans secured by non-residential properties and/or non—owner occupied residential properties include four loans with a combined balance of \$2.4 million to a single borrower secured by 35 residential rental properties located in the greater Philadelphia area. The Bank is in the process of foreclosure or obtaining a deed in lieu of foreclosure on the properties. An in-house review of the fair values of all the properties less costs to sell indicates a value in excess of the loan balances

Commercial-business, real estate secured loans include two loans with a combined balance of \$5.9 million to a single borrower, secured by undeveloped commercial real estate and the personal guarantees of several individuals. At September 30, 2010, the Bank was in the midst of foreclosure proceedings. On November 2, 2010, the Bank completed foreclosure proceedings and has acquired the property. An appraisal less than one year old indicated a value in excess of the loan balance. However, the Bank is in the process of obtaining a new appraisal of the property and listing the property with a broker for sale.

Commercial-business, real estate secured loans also include two loans, with a combined balance of \$2.0 million secured by a parcel of land. The borrower is attempting to sell the property and intends to apply the sale proceeds to the outstanding loan balance. A recent appraisal of the property indicates an appraised value less selling cost is in excess of the loan balances.

With respect to each of the remaining non-performing loans, the Bank is taking appropriate steps to resolve the individual situations.

Foreclosed property at September 30, 2010 included five parcels of real estate with a combined carrying value of \$2.2 million whereas foreclosed property at September 30, 2009 consisted of two parcels of real estate with a combined carrying value of \$1.0 million. During the third quarter of 2010, the Bank completed foreclosure proceedings on a commercial loan which resulted in a charge to the allowance of \$0.2 million. The properties are listed or are in the process of being listed with real estate agents for sale in a timely manner. Foreclosed real estate is included in other assets in the consolidated balance sheet.

### Allowance for Loan Losses

The Bank provides valuation allowances for estimated losses from uncollectible loans. The allowance is increased by provisions charged to expense and reduced by net charge-offs. On a quarterly basis, the Company prepares an allowance for loan losses (ALLL) analysis. In the analysis, the loan portfolio is segmented into groups of homogeneous loans that share similar risk characteristics: commercial real estate, commercial construction, commercial business, single family residential, and consumer which is predominately real estate secured junior liens and home equity lines of credit. Each segment is assigned reserve factors based on quantitative and qualitative measurements. In addition, the Bank reviews it's internally classified loans, its loans classified for regulatory purposes, delinquent loans, and other relevant information in order to isolate loans for further scrutiny as potentially impaired loans.

Quantitative factors include an actual expected loss factor based on historical loss experience over a relevant look-back period. Quantitative factors also include the Bank's actual risk ratings for the commercial loan segments as

determined in accordance with loan review and loan grading policies and procedures, and additional factors as determined by management to be representative of additional risk due to the loan's geographic location, type, and other attributes. These quantitative factors are adjusted if necessary, up or down, based on actual experience and an evaluation of the qualitative factors.

Qualitative factors are based upon: (1) changes in lending policies and procedures, including but not limited to changes in underwriting standards and collection, charge-off, and recovery practices not considered elsewhere in estimating credit losses; (2) changes in international, national, regional, and local economic and business conditions and developments that affect the collectability of the portfolio, including the condition of various market segments; (3) changes in the nature and volume of the portfolio and in the terms of loans; (4) changes in the experience, ability, and depth of lending management and other relevant staff; (5) changes in the volume and severity of past due loans, the volume of nonaccrual loans, and the volume and severity of adversely classified or graded loans; (6) changes in the quality of the loan review system; (7) changes in the value of underlying collateral for collateral dependent loans; (8) the existence and effect of any concentration of credit, and changes in the level of such concentrations; and (9) the effect of other external factors such as competition and legal and regulatory requirements on the level of estimated credit losses in the existing loan portfolio.



Table of Contents

Potentially impaired loans selected for individual evaluation are reviewed in accordance with US GAAP which governs the accounting for impaired assets, and consideration of regulatory guidance regarding treatment of troubled, collateral dependent loans. Each potentially impaired loan is evaluated using all available information such as recent appraisals, whether the loan is currently on accrual or non-accrual status, discounted cash flow analyses, guarantor financial strength, the value of additional collateral, and the loan's and borrower's past performance to determine whether in management's best judgment it is probable that the Bank will be unable to collect all contractual interest and principal in accordance with the loan's terms. Loans deemed impaired are generally assigned a reserve derived from the value of the underlying collateral. Loans deemed not to be impaired are assigned a reserve factor based upon the segment from which they were selected.

The ALLL needed as a result of the foregoing evaluations is compared with the unadjusted amount, and an adjustment is made by means of a provision charged to expense for loan losses. Recognizing the inherently imprecise nature of the loss estimates and the large number of assumptions needed in order to perform the analysis, the required reserve may be less than the actual level of reserves at the end of any evaluation period, and thus there may be an unallocated portion of the ALLL. Management adjusts the unallocated portion to an amount which management considers reasonable under the circumstances.

The following table sets forth the allocation of the loan loss allowance by loan segment for the periods indicated:

	September 30, 2010	December 31, 2009 (in thousands)	September 30, 2009
Impaired loans:			
Secured by non-residential properties and /or non—owner occupied residential property	\$ 120	\$ —	\$—
Construction loans	1,374	540	—
Commercial-business, real estate secured	398	—	—
Commercial-business, non-real estate secured	44	—	—
Total	1,936	540	—
Unimpaired loans:			
Secured by one-to-four family residences	1,149	962	1,443
Secured by non-residential properties and or non—owner occupied residential property	1,819	1,275	1,048
Construction loans	1,173	1,126	584
Commercial-business, real estate secured	484	757	297
Commercial-business, non-real estate secured	33	168	48
Home equity and second mortgage	545	303	307
Other consumer	13	14	17
Total	5,216	4,605	3,744
Unallocated	454	70	548
Allowance for loan loss	\$7,606	\$ 5,215	\$4,292

Table of Contents

## RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2010 AND 2009

Net Income. The Company recorded net income of \$1.0 million, or \$0.39 per diluted share, for the three months ended September 30, 2010 as compared to net income of \$1.1 million, or \$0.44 per diluted share, for the three months ended September 30, 2009.

## Average Balance Sheet

The following table sets forth information (dollars in thousands) relating to the Company's average balance sheet and reflects the average yield on assets and average cost of liabilities for the periods indicated. Yield and cost are computed by dividing income or expense by the average daily balance of interest-earning assets or interest-bearing liabilities, respectively, for the three-month periods indicated.

	Three Months Ended September 30,						Average yld/cost		
	Average balance	2010 Interest	Average yld/cost		Average balance	2009 Interest			
<b>ASSETS</b>									
Interest-earning assets:									
Loans receivable(1)	\$522,181	\$7,020	5.33	%	\$535,358	\$7,638	5.66	%	
Mortgage-backed securities	79,070	886	4.45	%	100,482	1,170	4.62	%	
Investment securities(2)	59,077	586	3.94	%	41,849	430	4.08	%	
Other interest-earning assets(3)	10,122	—	*	—	%	2,027	1	0.20	%
Total interest-earning assets	670,450	8,492	5.03	%	679,716	9,239	5.39	%	
Non interest-earning assets	42,716				37,463				
Total assets	\$713,166				\$717,179				
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>									
Interest-bearing liabilities:									
Deposits	\$556,314	1,757	1.25	%	\$530,064	2,393	1.79	%	
Borrowings from the FHLB and other borrowings	75,130	731	3.86	%	107,746	988	3.64	%	
Total interest-bearing liabilities	631,444	2,488	1.56	%	637,810	3,381	2.10	%	
Non interest-bearing liabilities	7,744				9,065				
Total liabilities	639,188				646,875				
Stockholders' equity	73,978				70,304				
Total liabilities and stockholders' equity	\$713,166				\$717,179				
Net interest income—tax equivalent basis		6,004				5,858			
Interest rate spread(4)-tax equivalent basis			3.47	%			3.29	%	
Net yield on interest-earning assets(5)									
—tax equivalent basis			3.55	%			3.42	%	
Ratio of average interest-earning assets to average interest-bearing liabilities			106.18	%			106.57	%	
Less: tax—equivalent interest		(142)	)			(119)	)		

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adjustment					
Net interest income	\$5,862			\$5,739	
Interest rate spread(4)		3.38	%	3.22	%
Net yield on interest-earning assets(5)		3.47	%	3.35	%

24

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Table of Contents

- (1) Nonaccrual loans have been included in the appropriate average loan balance category, but interest on nonaccrual loans has not been included for purposes of determining interest income.
- (2) Tax equivalent adjustments to interest on investment securities were \$142,000 and \$119,000 for the quarter ended September 30, 2010 and 2009, respectively. Tax equivalent interest income is based upon a marginal effective tax rate of 34%.
- (3) Includes interest-bearing deposits in other banks.
- (4) Interest rate spread represents the difference between the average yield on interest-earning assets and the average cost of interest-bearing liabilities.
- (5) Net yield on interest-earning assets represents net interest income as a percentage of average interest-earning assets.
- \* Is less than \$500 for period indicated

## Rate/Volume Analysis

The following table presents, for the periods indicated, the change in interest income and interest expense (in thousands) attributed to (i) changes in volume (changes in the weighted average balance of the total interest earning asset and interest bearing liability portfolios multiplied by the prior year rate), and (ii) changes in rate (changes in rate multiplied by prior year volume). Changes attributable to the combined impact of volume and rate have been allocated proportionately based on the absolute value of changes due to volume and changes due to rate.

	Three months ended September 30 2010 vs 2009		
	Volume	Rate	Net
Interest income:			
Loans receivable, net	\$(185 )	\$(433 )	\$(618 )
Mortgage-backed securities	(241 )	(43 )	(284 )
Investment securities (1)	253	(97 )	156
Other interest-earning assets	6	(7 )	(1 )
Total interest-earning assets	(167 )	(580 )	(747 )
Interest expense:			
Deposits	717	(1,353 )	(636 )
Borrowings from the FHLB and other borrowings	(612 )	355	(257 )
Total interest-bearing liabilities	105	(998 )	(893 )
Net change in net interest income	\$(272 )	\$418	\$146

- (1) Tax equivalent adjustments to interest on investment securities were \$142,000 and \$119,000 for the quarters ended September 30, 2010 and 2009, respectively. Tax equivalent interest income is based upon a marginal effective tax rate of 34%.

**Total Interest Income.** Total interest income, on a taxable equivalent basis, decreased by \$747,000 or 8.1% to \$8.5 million for the quarter ended September 30, 2010 compared with the third quarter of 2009. Interest income from loans receivable decreased by \$618,000, the result of a \$13.2 million decrease in the average balance of loans outstanding plus a decrease in the average yield on loans of 33 basis points. The decrease in the yield was caused by an increase in non-performing loans between the periods which reduced interest income from loans by \$294,000. Interest income from mortgage-backed securities was lower in the third quarter of 2010 in comparison to the same period of 2009 mainly because principal repayments of \$28.2 million exceeded purchases of \$14.0 million during the intervening

period. Interest income from investment securities was higher as a result of purchases of \$15.6 million of investments during the intervening period, however the yield associated with newly acquired investment securities was lower causing a 14 basis point decline in the yield between the two quarters.

Total Interest Expense. Total interest expense decreased by \$893,000 to \$2.5 million during the three-month period ended September 30, 2010 as compared with the third quarter of 2009. Although the average balance of deposits increased by \$26.3 million between the two quarters, the interest rates paid on the Bank's deposits were 54 basis points lower in 2010 due to the maturity of certificates of deposit with higher interest rates than current market rates offered on the products into which the maturing CDs were renewed or reinvested. In addition, the Bank lowered the interest rates paid on certain non-CD products. Interest expense associated with borrowings from the Federal Home Loan Bank and the Federal Reserve Bank decreased \$257,000 between the third quarter of 2010 and 2009. During the intervening period, the Bank reduced its average outstanding borrowings by \$32.6 million, mainly by reducing low cost short-term advances. Thus, the remaining fixed rate, term advances outstanding during the third quarter of 2010 have a higher rate than those that were combined with the short-term borrowings available through the Federal Reserve Bank and Federal Home Loan Bank accessed in the third quarter of 2009.

Table of Contents

Non-interest income. Total non-interest income was \$927,000 for the third quarter of 2010 compared with \$796,000 for the same period in 2009. During 2010, the gain on sale of loans held for sale increased by \$226,000 as a result of increased residential loan sales activity in the third quarter of 2010. Income from mortgage servicing decreased \$38,000 in the third quarter of 2010 mainly due to a \$57,000 non-cash charge for impairment of mortgage servicing rights. Additionally, overdraft fees were \$50,000 lower during the third quarter of 2010, reflecting consumer awareness and recent legislation which has drawn attention to such fees.

Non-interest expense. Total non-interest expense decreased by \$193,000 to \$4.2 million for the three months ended September 30, 2010 compared to the same period in 2009. Employee compensation and benefits decreased \$332,000 as various bonus and incentive compensation programs for 2010 were suspended in the third quarter of 2010 resulting in a reversal of \$235,000 of compensation previously expensed through June 30, 2010. The absence of such expense when combined with the aforementioned reversal produced a total reduction of compensation expense of \$319,000. FDIC insurance premiums increased by \$51,000 between the two quarters due to an increased deposit base and an increased assessment rate. Other operating expense increased \$35,000 mainly because of increased appraisal costs associated with nonperforming loans and costs to maintain and liquidate real estate acquired through foreclosure. Although total professional fees remained stable between the two periods, legal costs associated with non-performing loans and foreclosures increased \$55,000 while consultant fees and audit and tax expenses were lower by \$54,000.

Income tax expense. The Company's effective tax rate was 27.0% for the quarter ended September 30, 2010 compared to 24.1% for the quarter ended September 30, 2009. These effective tax rates are lower than the Company's marginal tax rate of 34% largely due to the tax-exempt income associated with the Company's investments in tax-exempt municipal bonds and bank-owned life insurance. Income tax expense includes federal as well as state income tax which increased \$78,000 as a state tax loss carry-forward credit expired.

Table of Contents

## RESULTS OF OPERATIONS FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2010 AND 2009

Net Income. The Company recorded net income of \$2.7 million, or \$1.06 per diluted share, for the nine months ended September 30, 2010 as compared to net income of \$3.4 million, or \$1.33 per diluted share, for the nine months ended September 30, 2009.

## Average Balance Sheet

The following table sets forth information (dollars in thousands) relating to the Company's average balance sheet and reflects the average yield on assets and average cost of liabilities for the periods indicated. Yield and cost are computed by dividing income or expense by the average daily balance of interest-earning assets or interest-bearing liabilities, respectively, for the nine-month periods indicated.

	Nine Months Ended September 30,						Average yld/cost	
	Average balance	2010 Interest	Average yld/cost		Average balance	2009 Interest		
<b>ASSETS</b>								
Interest-earning assets:								
Loans receivable(1)	\$524,734	\$21,472	5.49	%	\$540,972	\$22,951	5.69	%
Mortgage-backed securities	80,538	2,782	4.63	%	104,752	3,849	4.93	%
Investment securities(2)	56,956	1,709	4.02	%	39,798	1,189	4.01	%
Other interest-earning assets(3)	10,112	2	0.03	%	1,519	1	0.09	%
Total interest-earning assets	672,340	25,965	5.18	%	687,041	27,990	5.46	%
Non interest-earning assets	42,050				37,092			
Total assets	\$714,390				\$724,133			
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>								
Interest-bearing liabilities:								
Deposits	\$554,259	5,593	1.35	%	\$514,614	7,347	1.91	%
Borrowings from the FHLB and other borrowings	78,684	2,372	4.04	%	131,248	3,481	3.56	%
Total interest-bearing liabilities	632,943	7,965	1.69	%	645,862	10,828	2.25	%
Non interest-bearing liabilities	8,240				9,033			
Total liabilities	641,183				654,895			
Stockholders' equity	73,207				69,238			
Total liabilities and stockholders' equity	\$714,390				\$724,133			
Net interest income—tax equivalent basis		18,000				17,162		
Interest rate spread(4)-tax equivalent basis			3.49	%			3.21	%
Net yield on interest-earning assets(5)—tax equivalent basis			3.59	%			3.35	%
Ratio of average interest-earning assets to average interest-bearing liabilities			106.22	%			106.38	%
Less: tax—equivalent interest adjustment		(418 )				(325 )		

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Net interest income	\$17,582			\$16,837	
Interest rate spread(4)		3.41	%	3.15	%
Net yield on interest-earning assets(5)		3.51	%	3.29	%

27

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Table of Contents

- (1 ) Nonaccrual loans have been included in the appropriate average loan balance category, but interest on nonaccrual loans has not been included for purposes of determining interest income.
- (2 ) Tax equivalent adjustments to interest on investment securities were \$418,000 and \$325,000 for the nine months ended September 30, 2010 and 2009, respectively. Tax equivalent interest income is based upon a marginal effective tax rate of 34%.
- (3 ) Includes interest-bearing deposits in other banks.
- (4 ) Interest rate spread represents the difference between the average yield on interest-earning assets and the average cost of interest-bearing liabilities.
- (5 ) Net yield on interest-earning assets represents net interest income as a percentage of average interest-earning assets.

## Rate/Volume Analysis

The following table presents, for the periods indicated, the change in interest income and interest expense (in thousands) attributed to (i) changes in volume (changes in the weighted average balance of the total interest earning asset and interest bearing liability portfolios multiplied by the prior year rate), and (ii) changes in rate (changes in rate multiplied by prior year volume). Changes attributable to the combined impact of volume and rate have been allocated proportionately based on the absolute value of changes due to volume and changes due to rate.

	Nine months ended September 30 2010 vs 2009		
	Volume	Rate	Net
Interest income:			
Loans receivable, net	\$(678 )	\$(801 )	\$(1,479 )
Mortgage-backed securities	(847 )	(220 )	(1,067 )
Investment securities (1)	515	5	520
Other interest-earning assets	3	(2 )	1
Total interest-earning assets	(1,007 )	(1,018 )	(2,025 )
Interest expense:			
Deposits	837	(2,591 )	(1,754 )
Borrowings from the FHLB and other borrowings	(1,778 )	669	(1,109 )
Total interest-bearing liabilities	(941 )	(1,922 )	(2,863 )
Net change in net interest income	\$(66 )	\$904	\$838

- (1 ) Tax equivalent adjustments to interest on investment securities were \$418,000 and \$325,000 for the nine months ended September 30, 2010 and 2009, respectively. Tax equivalent interest income is based upon a marginal effective tax rate of 34%.

**Total Interest Income.** Total interest income, on a taxable equivalent basis, decreased by \$2.0 million or 7.2% to \$26.0 million for the nine months ended September 30, 2010 compared with the first nine months of 2009. Interest income from loans receivable decreased by \$1.5 million, the result of a \$16.2 million decrease in the average balance of loans outstanding, plus a decrease in the yield on loans of 20 basis points. The decrease in the yield was caused by an increase in non-performing loans which reduced interest income from loans by \$643,000 between the periods. Interest income from mortgage-backed securities was lower during 2010 mainly because repayments of \$28.2 million exceeded purchases of \$14.0 million during the intervening period. In addition, the yield associated with repayments was higher than the yield on newly purchased mortgage-backed securities which caused a 30 basis point decline

between the two periods. Interest income from investment securities was higher as a result of purchases of \$15.6 million of investments during the intervening period.

**Total Interest Expense.** Total interest expense decreased by \$2.9 million to \$8.0 million during the nine-month period ended September 30, 2010 as compared with the same period in 2009. Although the average balance of deposits increased by \$39.6 million between the two periods, the interest rates paid on the Bank's deposits were 56 basis points lower in 2010 due to the maturity of certificates of deposit with higher interest rates than current market rates offered on the products into which the maturing CDs were renewed or reinvested. In addition, the Bank lowered the interest rates paid on certain non-CD products. Interest expense associated with borrowings from the Federal Home Loan Bank and the Federal Reserve Bank decreased \$1.1 million between the first nine-months of 2010 and 2009. During the intervening period, the Bank reduced its average outstanding borrowings by \$52.6 million, mainly by reducing low cost short-term advances. Thus, the remaining fixed rate, term advances outstanding during the nine months of 2010 have a higher rate than those that were combined with the short-term borrowings available through the Federal Reserve Bank and Federal Home Loan Bank accessed in 2009.

Table of Contents

Non-interest income. Total non-interest income was \$2.1 million for the first nine months of 2010 compared with \$3.2 million for the same period in 2009. Gain on sale of foreclosed real estate totaled \$337,000 in 2009 as compared to a loss from foreclosed real estate of \$137,000 in 2010. Gain on the sale of investment securities was \$306,000 during the first nine months of 2009 while there was only a gain of \$7,000 from a security sale in 2010. During 2010, the gain on sale of loans held for sale was \$63,000 lower as residential loan sales activity was down in the first half of the year with greater activity in the third quarter of 2010. Income from mortgage servicing decreased \$114,000 in 2010 mainly due to a \$195,000 non-cash charge for impairment of mortgage servicing rights. Additionally, overdraft fees were \$113,000 lower during 2010, due to increased consumer awareness and recent legislation which has drawn attention to such fees.

Non-interest expense. Total non-interest expense decreased by \$210,000 to \$13.4 million for the nine months ended September 30, 2010 compared to the same period in 2009. Employee compensation and benefits decreased \$281,000 as various bonus and incentive compensation programs for 2010 were suspended in the third quarter of 2010 resulting in a reversal of \$235,000 of compensation previously expensed through June 30, 2010. The absence of such expense when combined with the aforementioned reversal produced a total reduction of compensation expense of \$295,000. Employee benefits increased between the periods; the result of rising insurance premiums of employer- provided medical benefits of \$100,000. Costs associated with the Company's defined benefit plan were \$63,000 lower in 2010. FDIC insurance premiums decreased by \$28,000 as 2009 included a special assessment of \$330,000; whereas the FDIC insurance premium in 2010 reflects an increased deposit base and an increased assessment rate. Other operating expense decreased \$22,000 due to a change in a deposit services related contract that reduced the expense by \$88,000 in 2010. Also, robbery and deposit- related losses of \$50,000 were included in other operating expense in 2009 and there were no such losses in 2010. Partially, offsetting the decrease in other operating expense were increased costs of \$52,000 associated with maintenance of real estate acquired through foreclosure. Occupancy and equipment costs increased \$82,000 mainly the result of costs associated with a relocated and renovated branch office. Professional fees increased between the two periods as legal costs associated with non-performing loans and foreclosures during 2010 increased \$184,000. The Company's professional fees related to consultants and audit and tax services decreased \$160,000 in 2010.

Income tax expense. The Company's effective tax rate was 24.6% for the nine months ended September 30, 2010 compared to 25.2% for the same period in 2009. These effective tax rates are lower than the Company's marginal tax rate of 34% largely due to the tax-exempt income associated with the Company's investments in tax-exempt municipal bonds and bank-owned life insurance. Income tax expense includes federal as well as state income tax which increased \$180,000 as a state tax loss carry-forward credit expired.

Table of Contents

LIQUIDITY AND CAPITAL RESOURCES

Liquidity

The Bank's liquidity is a measure of its ability to fund loans, pay withdrawals of deposits, and other cash outflows in an efficient, cost-effective manner. The Bank's short-term sources of liquidity include maturity, repayment and sales of assets, excess cash and cash equivalents, new deposits, broker deposits, other borrowings, and new borrowings from the Federal Home Loan Bank and the Federal Reserve Bank. There has been no material adverse change during the nine-month period ended September 30, 2010 in the ability of the Bank's and its subsidiaries to fund their operations.

At September 30, 2010, the Bank's had commitments outstanding under letters of credit of \$1.0 million, commitments to originate loans of \$14.6 million, and commitments to fund undisbursed balances of closed loans and unused lines of credit of \$43.8 million. At September 30, 2010, the Bank had \$7.0 million in outstanding commitments to sell loans. There has been no material change during the nine months ended September 30, 2010 in any of the Bank's other contractual obligations or commitments to make future payments.

The Company's primary sources of liquidity are dividends from the Bank, principal and interest payments received from a loan made to the Bank's Employee Stock Ownership Plan, and tax benefits arising from the use of the Company's tax deductions by other members of its consolidated group pursuant to a tax sharing agreement. The Company is dependent upon these sources and cash on hand which totaled approximately \$1.9 million at September 30, 2010 in order to fund its operations and pay the dividend to its shareholders. There has been no material adverse change in the ability of the Company to fund its operations during the nine-month period ended September 30, 2010.

Capital Requirements

The Bank was in compliance with all of its capital requirements as of September 30, 2010.

Table of Contents

CRITICAL ACCOUNTING POLICIES

Certain critical accounting policies of the Company require the use of significant judgment and accounting estimates in the preparation of the consolidated financial statements and related data of the Company. These accounting estimates require management to make assumptions about matters that are highly uncertain at the time the accounting estimate is made. Management believes that the most critical accounting policy requiring the use of accounting estimates and judgment is the determination of the allowance for loan losses. If the financial position of a significant amount of debtors or the value of the collateral securing the loans should deteriorate more than the Company has estimated, the present allowance for loan losses may be insufficient and additional provisions for loan losses may be required. The allowance for loan losses was approximately \$7.6 million at September 30, 2010.

RECENT LEGISLATION

On July 21, 2010, the President signed into law the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") which will significantly change the current bank regulatory structure and affect the lending, investment, trading and operating activities of financial institutions and their holding companies. The Dodd-Frank Act will eliminate our current primary federal regulator, the Office of Thrift Supervision. The Dodd-Frank Act also authorizes the Board of Governors of the Federal Reserve System to supervise and regulate all savings and loan holding companies like the Company, in addition to bank holding companies which it currently regulates. As a result, the Federal Reserve Board's current regulations applicable to bank holding companies, including holding company capital requirements, will apply to savings and loan holding companies like the Company. These capital requirements are substantially similar to the capital requirements currently applicable to the Bank. The Dodd-Frank Act also requires the Federal Reserve Board to set minimum capital levels for bank holding companies that are as stringent as those required for the insured depository subsidiaries, and the components of Tier 1 capital would be restricted to capital instruments that are currently considered to be Tier 1 capital for insured depository institutions. Bank holding companies with assets of less than \$500 million are exempt from these capital requirements. Under the Dodd-Frank Act, the proceeds of trust preferred securities are excluded from Tier 1 capital unless such securities were issued prior to May 19, 2010 by bank or savings and loan holding companies with less than \$15 billion of assets. The legislation also establishes a floor for capital of insured depository institutions that cannot be lower than the standards in effect today, and directs the federal banking regulators to implement new leverage and capital requirements within 18 months that take into account off-balance sheet activities and other risks, including risks relating to securitized products and derivatives.

The Dodd-Frank Act also creates a new Consumer Financial Protection Bureau with broad powers to supervise and enforce consumer protection laws. The Consumer Financial Protection Bureau has broad rule-making authority for a wide range of consumer protection laws that apply to all banks and savings institutions such as the Bank, including the authority to prohibit "unfair, deceptive or abusive" acts and practices. The Consumer Financial Protection Bureau has examination and enforcement authority over all banks and savings institutions with more than \$10 billion in assets. Banks and savings institutions with \$10 billion or less in assets will be examined by their applicable bank regulators. The new legislation also weakens the federal preemption available for national banks and federal savings associations, and gives state attorneys general the ability to enforce applicable federal consumer protection laws.

The legislation also broadens the base for Federal Deposit Insurance Corporation insurance assessments. Assessments will now be based on the average consolidated total assets less tangible equity capital of a financial institution. The Dodd-Frank Act also permanently increases the maximum amount of deposit insurance for banks, savings institutions and credit unions to \$250,000 per depositor, retroactive to January 1, 2009, and non-interest bearing transaction accounts have unlimited deposit insurance through December 31, 2013. Lastly, the Dodd-Frank Act will increase stockholder influence over boards of directors by requiring companies to give stockholders a non-binding vote on executive compensation and so-called "golden parachute" payments, and authorizing the Securities and Exchange

Commission to promulgate rules that would allow stockholders to nominate their own candidates using a company's proxy materials. The legislation also directs the Federal Reserve Board to promulgate rules prohibiting excessive compensation paid to bank holding company executives, regardless of whether the company is publicly traded or not.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

As a "smaller reporting company" as defined by Item 10 of Regulation S-K, the Company is not required to provide the information required by this item.

Table of Contents

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Based on their evaluation of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) under the Securities Exchange Act of 1934 (the "Exchange Act")), the Company's principal executive officer and principal financial officer have concluded that as of the end of the period covered by this Quarterly Report on Form 10-Q such disclosure controls and procedures are effective to ensure that information required to be disclosed by the Company in the reports it files and submits pursuant to the rules and forms of the SEC is accumulated and communicated to the Company's management including the principal executive officer and principal financial officer, as appropriate, to allow timely decisions regarding required disclosures.

Changes in Internal Controls over Financial Reporting

During the quarter under report, there was no change in the Company's internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

Table of Contents

TF FINANCIAL CORPORATION AND SUBSIDIARIES

PART II

ITEM 1. LEGAL PROCEEDINGS

Neither the Company nor its subsidiaries are involved in any pending legal proceedings, other than routine legal matters occurring in the ordinary course of business that in the aggregate involve amounts which are believed by management to be immaterial to the consolidated financial condition or results of operations of the Company.

ITEM 1A. RISK FACTORS

As a “smaller reporting company” as defined by Item 10 of Regulation S-K, the Company is not required to provide the information required by this item.

ITEM 2. UNREGISTERED SALE OF EQUITY SECURITIES AND USE OF PROCEEDS

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable.

ITEM 4. [REMOVED AND RESERVED]

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

(a)	Exhibits	
	31.1	Certification of CEO pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
	31.2	Certification of CFO pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
	32.	Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.



Table of Contents

TF FINANCIAL CORPORATION

SIGNATURES

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

Date: November 12, 2010

/s/ Kent C. Lufkin  
Kent C. Lufkin  
President and CEO  
(Principal Executive Officer)

Date: November 12, 2010

/s/ Dennis R. Stewart  
Dennis R. Stewart  
Executive Vice President and Chief Financial  
Officer  
(Principal Financial & Accounting Officer)

34

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