ENTERPRISE BANCORP INC /MA/
Form 10-Q
August 09, 2013
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UNITED STATES
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 quarterly period ended June 30, 2013

Commission File Number: 001-33912
Enterprise Bancorp, Inc.
(Exact name of registrant as specified in its charter)

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

(978) 459-9000
(Registrant's telephone number, including area code)

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

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

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

| | |
|---|---|
| Large accelerated filer o | Accelerated filer x |
| Non-accelerated filer o | Smaller reporting company o |

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

As of August 5, 2013, there were 9,943,786 shares of the issuer's common stock outstanding- Par Value $0.01 per share

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PART I-FINANCIAL INFORMATION

Item 1 - Financial Statements
ENTERPRISE BANCORP, INC.
Consolidated Balance Sheets

| (Dollars in thousands) | June 30, 2013 (unaudited) | December 31, 2012 |
|---|---|---|
| Assets | | |
| Cash and cash equivalents: | | |
| Cash and due from banks | $40,795 | $38,007 |
| Interest-earning deposits | 6,878 | 12,218 |
| Fed funds sold | 4,055 | 2,510 |
| Total cash and cash equivalents | 51,728 | 52,735 |
| Investment securities at fair value | 190,459 | 184,464 |
| Federal Home Loan Bank Stock | 4,324 | 4,260 |
| Loans held for sale | 3,917 | 8,557 |
| Loans, less allowance for loan losses of $25,671 at June 30, 2013 and $24,254 at December 31, 2012, respectively | 1,421,675 | 1,335,401 |
| Premises and equipment | 28,602 | 27,206 |
| Accrued interest receivable | 6,092 | 5,828 |
| Deferred income taxes, net | 13,771 | 12,548 |
| Bank-owned life insurance | 15,678 | 15,443 |
| Prepaid income taxes | 1,387 | 174 |
| Prepaid expenses and other assets | 10,047 | 13,454 |
| Goodwill | 5,656 | 5,656 |
| Total assets | $1,753,336 | $1,665,726 |
| Liabilities and Stockholders' Equity | | |
| Liabilities | | |
| Deposits | $1,579,293 | $1,475,027 |
| Borrowed funds | 1,880 | 26,540 |
| Junior subordinated debentures | 10,825 | 10,825 |
| Accrued expenses and other liabilities | 16,766 | 13,182 |
| Accrued interest payable | 579 | 603 |
| Total liabilities | $1,609,343 | $1,526,177 |
| Commitments and Contingencies | | |
| Stockholders' Equity | | |
| Preferred stock, $0.01 par value per share; 1,000,000 shares authorized; no shares issued | — | — |
| Common stock, $0.01 par value per share; 20,000,000 shares authorized; 9,872,735 issued and outstanding at June 30, 2013 (including 171,481 shares of unvested participating restricted awards) and 9,676,477 shares issued and outstanding at December 31, 2012 (including 154,186 shares of unvested participating restricted awards) | 99 | 97 |
| Additional paid-in-capital | 50,479 | 48,194 |
| Retained earnings | 91,427 | 87,159 |
| Accumulated other comprehensive income | 1,988 | 4,099 |
| Total stockholders' equity | $143,993 | $139,549 |
| Total liabilities and stockholders' equity | $1,753,336 | $1,665,726 |

See the accompanying notes to the unaudited consolidated financial statements.

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ENTERPRISE BANCORP, INC.
Consolidated Statements of Income
(unaudited)

| | Three months ended June 30, | | Six months ended June 30, | |
|---|---|---|---|---|
| (Dollars in thousands, except per share data) | 2013 | 2012 | 2013 | 2012 |
| Interest and dividend income: | | | | |
| Loans and loans held for sale | $16,653 | $16,228 | $33,026 | $32,186 |
| Investment securities | 794 | 835 | 1,604 | 1,634 |
| Other interest-earning assets | 11 | 24 | 21 | 43 |
| Total interest and dividend income | 17,458 | 17,087 | 34,651 | 33,863 |
| Interest expense: | | | | |
| Deposits | 996 | 1,368 | 2,030 | 2,905 |
| Borrowed funds | 40 | 13 | 86 | 29 |
| Junior subordinated debentures | 295 | 295 | 589 | 589 |
| Total interest expense | 1,331 | 1,676 | 2,705 | 3,523 |
| Net interest income | 16,127 | 15,411 | 31,946 | 30,340 |
| Provision for loan losses | 534 | 1,050 | 1,317 | 1,350 |
| Net interest income after provision for loan losses | 15,593 | 14,361 | 30,629 | 28,990 |
| Non-interest income: | | | | |
| Investment advisory fees | 1,045 | 934 | 2,061 | 1,955 |
| Deposit and interchange fees | 1,181 | 1,107 | 2,289 | 2,128 |
| Income on bank-owned life insurance, net | 119 | 128 | 235 | 262 |
| Net gains on sales of investment securities | 468 | 112 | 948 | 159 |
| Gains on sales of loans | 222 | 218 | 557 | 458 |
| Other income | 518 | 453 | 1,102 | 964 |
| Total non-interest income | 3,553 | 2,952 | 7,192 | 5,926 |
| Non-interest expense: | | | | |
| Salaries and employee benefits | 8,651 | 7,841 | 16,699 | 15,344 |
| Occupancy and equipment expenses | 1,488 | 1,430 | 3,059 | 2,844 |
| Technology and telecommunications expenses | 1,203 | 1,077 | 2,356 | 2,076 |
| Advertising and public relations expenses | 946 | 497 | 1,566 | 1,286 |
| Audit, legal and other professional fees | 411 | 487 | 825 | 970 |
| Deposit insurance premiums | 284 | 283 | 533 | 560 |
| Supplies and postage expenses | 250 | 196 | 487 | 427 |
| Investment advisory and custodial expenses | 134 | 112 | 260 | 209 |
| Other operating expenses | 1,094 | 1,049 | 2,130 | 2,074 |
| Total non-interest expense | 14,461 | 12,972 | 27,915 | 25,790 |
| Income before income taxes | 4,685 | 4,341 | 9,906 | 9,126 |
| Provision for income taxes | 1,606 | 1,436 | 3,394 | 3,048 |
| Net income | $3,079 | $2,905 | $6,512 | $6,078 |
| | | | | |
| Basic earnings per share | $0.31 | $0.30 | $0.67 | $0.64 |
| Diluted earnings per share | $0.31 | $0.30 | $0.66 | $0.63 |
| | | | | |
| Basic weighted average common shares outstanding | 9,825,335 | 9,588,420 | 9,770,559 | 9,543,994 |
| Diluted weighted average common shares outstanding | 9,889,639 | 9,655,728 | 9,840,016 | 9,612,187 |

See the accompanying notes to the unaudited consolidated financial statements.

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ENTERPRISE BANCORP, INC.
Consolidated Statements of Comprehensive Income
(Unaudited)

| | Three months ended June 30, | | Six months ended June 30, | |
|---|---|---|---|---|
| (Dollars in thousands) | 2013 | 2012 | 2013 | 2012 |
| Net income | $3,079 | $2,905 | $6,512 | $6,078 |
| Other comprehensive (loss) income, net of taxes: | | | | |
| Gross unrealized holding (losses) gains on investments arising during the period | (2,744) | 312 | (2,386) | 816 |
| Income tax benefit (expense) | 999 | (117) | 884 | (287) |
| Net unrealized holding (losses) gains, net of tax | (1,745) | 195 | (1,502) | 529 |
| Less: Reclassification adjustment for net gains included in net income | | | | |
| Net realized gains on sales of securities during the period | 468 | 112 | 948 | 159 |
| Income tax expense | (163) | (40) | (339) | (56) |
| Reclassification adjustment for gains realized, net of tax | 305 | 72 | 609 | 103 |
| Total other comprehensive (loss) income | (2,050) | 123 | (2,111) | 426 |
| Comprehensive income | $1,029 | $3,028 | $4,401 | $6,504 |

See the accompanying notes to the unaudited consolidated financial statements.

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ENTERPRISE BANCORP, INC.
Consolidated Statement of Changes in Stockholders' Equity
(Unaudited)

| (Dollars in thousands) | Common Stock | Additional Paid-in Capital | Retained Earnings | Accumulated Other Comprehensive Income | Total Stockholders' Equity |
|---|---|---|---|---|---|
| Balance at December 31, 2012 | $97 | $48,194 | $87,159 | $ 4,099 | $139,549 |
| Net income | | | 6,512 | | 6,512 |
| Other comprehensive loss, net | | | | (2,111) | (2,111) |
| Tax benefit from exercise of stock options | | 7 | | | 7 |
| Common stock dividend paid ($0.23 per share) | | | (2,244) | | (2,244) |
| Common stock issued under dividend reinvestment plan | — | 630 | | | 630 |
| Stock-based compensation | 1 | 933 | | | 934 |
| Stock options exercised, net | 1 | 715 | | | 716 |
| Balance at June 30, 2013 | $99 | $50,479 | $91,427 | $ 1,988 | $143,993 |

See the accompanying notes to the unaudited consolidated financial statements.

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ENTERPRISE BANCORP, INC.
Consolidated Statements of Cash Flows
(Unaudited)

| | Six months ended June 30, | |
|---|---|---|
| (Dollars in thousands) | 2013 | 2012 |
| Cash flows from operating activities: | | |
| Net income | $6,512 | $6,078 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Provision for loan losses | 1,317 | 1,350 |
| Depreciation and amortization | 2,458 | 2,133 |
| Stock-based compensation expense | 859 | 652 |
| Mortgage loans originated for sale | (25,274) | (21,388) |
| Proceeds from mortgage loans sold | 30,471 | 24,644 |
| Net gains on sales of loans | (557) | (458) |
| Net gains on sales of OREO | (121) | (45) |
| Net gains on sales of investments | (948) | (159) |
| Income on bank-owned life insurance, net | (235) | (262) |
| Changes in: | | |
| Accrued interest receivable | (264) | 191 |
| Prepaid expenses and other assets | 1,802 | 683 |
| Accrued expenses and other liabilities | (1,319) | 1,391 |
| Accrued interest payable | (24) | (169) |
| Net cash provided by operating activities | 14,677 | 14,641 |
| Cash flows from investing activities: | | |
| Proceeds from sales of investment securities available for sale | 7,361 | 2,921 |
| Net proceeds (purchase) from FHLB capital stock | (64) | 480 |
| Proceeds from maturities, calls and pay-downs of investment securities | 8,040 | 9,689 |
| Purchase of investment securities | (19,297) | (36,874) |
| Net increase in loans | (87,759) | (46,522) |
| Additions to premises and equipment, net | (3,332) | (962) |
| Proceeds from OREO sales and payments | 652 | 885 |
| Net cash used in investing activities | (94,399) | (70,383) |
| Cash flows from financing activities: | | |
| Net increase in deposits | 104,266 | 120,454 |
| Net decrease in borrowed funds | (24,660) | (1,625) |
| Cash dividends paid | (2,244) | (2,098) |
| Proceeds from issuance of common stock | 630 | 635 |
| Proceeds from the exercise of stock options | 716 | 100 |
| Tax benefit from the exercise of stock options | 7 | 1 |
| Net cash provided by financing activities | 78,715 | 117,467 |
| | | |
| Net (decrease) increase in cash and cash equivalents | (1,007) | 61,725 |
| Cash and cash equivalents at beginning of period | 52,735 | 39,131 |
| Cash and cash equivalents at end of period | $51,728 | $100,856 |
| | | |
| Supplemental financial data: | | |
| Cash Paid For: Interest | $2,729 | $3,692 |
| Cash Paid For: Income Taxes | 4,583 | 4,134 |

| | | |
|---|---|---|
| Supplemental schedule of non-cash investing activity: | | |
| Purchase of investment securities not yet settled | 4,978 | — |
| Transfer from loans to other real estate owned | 167 | 400 |
| Capital expenditures incurred not yet paid | — | 74 |

See accompanying notes to the unaudited consolidated financial statements.

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ENTERPRISE BANCORP, INC.
Notes to the Unaudited Consolidated Financial Statements

(1) Organization of Holding Company and Basis of Presentation

The accompanying unaudited consolidated financial statements and these notes should be read in conjunction with the December 31, 2012 audited consolidated financial statements and notes thereto contained in the 2012 Annual Report on Form 10-K of Enterprise Bancorp, Inc. (the "Company" or "Enterprise"), a Massachusetts corporation, as filed with the Securities and Exchange Commission (the "SEC") on March 15, 2013. The Company has not changed its reporting policies from those disclosed in its 2012 Annual Report on Form 10-K.

The accompanying unaudited consolidated interim financial statements have been prepared in accordance with accounting principles generally accepted in the United States ("GAAP") for interim financial information and the instructions for Form 10-Q through the rules and interpretive releases of the SEC under federal securities law. In the opinion of management, the accompanying unaudited consolidated interim financial statements reflect all necessary adjustments consisting of normal recurring accruals for a fair presentation. All significant intercompany balances and transactions have been eliminated in the accompanying unaudited consolidated interim financial statements. Certain previous year amounts in the unaudited consolidated interim financial statements and accompanying footnotes have been reclassified to conform to the current year's presentation. Interim results are not necessarily indicative of results to be expected for the entire year.

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

The Bank's subsidiaries include Enterprise Insurance Services, LLC and Enterprise Investment Services, LLC, organized under the laws of the State of Delaware for the purposes of engaging in insurance sales activities and offering non-deposit investment products and services, respectively. In addition, the Bank has the following subsidiaries that are incorporated in the Commonwealth of Massachusetts and classified as security corporations in accordance with applicable Massachusetts General Laws: Enterprise Security Corporation; Enterprise Security Corporation II; and Enterprise Security Corporation III, which hold various types of qualifying securities. The security corporations are limited to conducting securities investment activities that the Bank itself would be allowed to conduct under applicable laws.

Pursuant to the Accounting Standards Codification ("ASC") Topic 810 "Consolidation of Variable Interest Entities," issued by the Financial Accounting Standards Board (originally issued as Financial Interpretation No. 46R) in December 2003, the Company carries Junior Subordinated Debentures as a liability on its consolidated financial statements, along with the related interest expense. The debentures were issued by a statutory business trust (the "Trust") created by the Company in March 2000 under the laws of the State of Delaware, and the trust preferred securities issued by the Trust, and the related non-interest expense, are excluded from the Company's consolidated financial statements.

Comprehensive income is defined as all changes to equity except investments by and distributions to stockholders. Net income is one component of comprehensive income, with other components referred to in the aggregate as other comprehensive income. The Company's only other comprehensive income component is the net unrealized holding gains or losses on investments available-for-sale. Pursuant to Accounting Standards Update ("ASU") No. 2013-02, Comprehensive Income (Topic 220): Reporting Amounts Reclassified Out of Accumulated Comprehensive Income, the Company initially excludes these unrealized holding gains and losses from net income; however they are later reported as reclassifications out of accumulated other comprehensive income into net income when the securities are sold. When securities are sold, the reclassification of realized gains and losses on available-for-sale securities are included on the Consolidated Statements of Income under the "non-interest income" subheading on the line item "net gains on sales of investment securities" and the related income tax expense is included in the line item "provision for income taxes," both of which are also detailed on the Consolidated Statements of Comprehensive Income under the subheading "reclassification adjustment for net gains included in net income."

The Company has 21 full service branches serving the Merrimack Valley and North Central regions of Massachusetts and Southern New Hampshire. The Company is currently constructing a branch office in Nashua, NH with an anticipated opening in the fourth quarter of 2013. Through the Bank and its subsidiaries, the Company offers a range of commercial and consumer loan products, deposit and cash management products, investment advisory and wealth management, and insurance services.  The services offered through the Bank and subsidiaries are managed as one strategic unit and represent the Company’s only reportable operating segment.

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

(2) Critical Accounting Estimates

As discussed in the Company’s 2012 Annual Report on Form 10-K, the three most significant areas in which management applies critical assumptions and estimates that are particularly susceptible to change relate to the determination of the allowance for loan losses, impairment review of investment securities and the impairment review of goodwill. Refer to Note 1, "Summary of Significant Accounting Policies," to the Company’s consolidated financial statements included in the Company’s 2012 Annual Report on Form 10-K for significant accounting policies. The Company has not changed its significant accounting policies from those disclosed in its 2012 Annual Report filed on Form 10-K.

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

(3) Recent Accounting Pronouncements

In February 2013, the Financial Accounting Standards Board (“FASB”) issued ASU No. 2013-02, Comprehensive Income (Topic 220): Reporting Amounts Reclassified out of Accumulated Other Comprehensive Income. The new amendments require an organization to present the effects on the income statement of significant amounts reclassified out of accumulated other comprehensive income or cross-reference to other disclosures currently required under GAAP for certain items. The new amended standard is effective for annual periods beginning after December 15, 2012, and interim periods within those annual periods. As this ASU addresses only disclosure requirements, the adoption in the first quarter of 2013 did not have a material impact on the Company's financial statements. See Note 1, "Organization of Holding Company and Basis of Presentation," for the disclosure of the effects of amounts reclassified out of accumulated other comprehensive income.

In December 2011, the FASB issued ASU No. 2011-11, Balance Sheet (Topic 210): Disclosures about Offsetting Assets and Liabilities, which was subsequently clarified in January 2013 by ASU 2013-01. The new amended standard was effective for annual periods beginning January 1, 2013, and interim periods within those annual periods. As this ASU primarily deals with disclosure requirements and the Company has no netting arrangements, the adoption in January 2013 did not have an impact on the Company's financial statements.

(4) Investments

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

| (Dollars in thousands) | June 30, 2013 Amortized cost | Unrealized gains | Unrealized losses | Fair Value |
|---|---|---|---|---|
| Federal agency obligations [1] | $65,111 | $191 | $50 | $65,252 |
| Federal agency mortgage backed securities (MBS) [1] | 52,563 | 570 | 976 | 52,157 |
| Municipal securities | 56,222 | 1,847 | 391 | 57,678 |
| Corporate bonds | 3,786 | 4 | 54 | 3,736 |
| Certificates of deposit | 858 | — | 3 | 855 |
| Total fixed income securities | 178,540 | 2,612 | 1,474 | 179,678 |
| Equity investments | 8,886 | 2,020 | 125 | 10,781 |
| Total available for sale securities, at fair value | $187,426 | $4,632 | $1,599 | $190,459 |

| (Dollars in thousands) | December 31, 2012 Amortized cost | Unrealized gains | Unrealized losses | Fair Value |
|---|---|---|---|---|
| Federal agency obligations[1] | $65,247 | $438 | $— | $65,685 |
| Federal agency mortgage backed securities (MBS) [1] | 48,429 | 1,287 | 42 | 49,674 |
| Municipal securities | 53,437 | 3,103 | 17 | 56,523 |
| Corporate bonds | 1,905 | 15 | 6 | 1,914 |
| Total fixed income securities | 169,018 | 4,843 | 65 | 173,796 |
| Equity investments | 9,080 | 1,622 | 34 | 10,668 |
| Total available for sale securities, at fair value | $178,098 | $6,465 | $99 | $184,464 |

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

Included in the carrying amount of the federal agency MBS category were CMOs totaling $20.6 million and $23.6 million at June 30, 2013 and December 31, 2012, respectively.

Certificates of Deposit (CDs) represent term deposits issued by banks that are subject to FDIC insurance and purchased on the open market. The Company utilizes these CDs as an alternative investment option to holding short-term excess cash in lower yielding overnight deposit accounts. These securities have maturities of less than a year and the market value approximates the carrying value.

At June 30, 2013, the equity portfolio consisted primarily of investments in a diversified group of mutual funds, with a small portion of the portfolio (approximately 17%) invested in exchange traded funds or individual common stock of entities in the financial services industry.

The net unrealized gain or loss in the Company's fixed income portfolio fluctuates as market interest rates rise and fall.  Due to the fixed rate nature of this portfolio, as market rates fall, the value of the portfolio rises, and as market rates rise, the value of the portfolio declines.  The unrealized gains or losses on fixed income investments will also decline as the securities approach maturity, or if the issuer is credit impaired. Unrealized gains or losses will be recognized in the statements of income if the securities are sold. However, if an unrealized loss on the fixed income portfolio is deemed to be other than temporary, the credit loss portion is charged to earnings and the noncredit portion is recognized in accumulated other comprehensive income. Net unrealized appreciation and depreciation on investments available for sale, net of applicable income taxes, are reflected as a component of accumulated other comprehensive income.

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

Management regularly reviews the portfolio for securities with unrealized losses that are other-than-temporarily impaired. During the six months ended June 30, 2013 and 2012, the Company did not record any fair value impairment charges on its investments. As of June 30, 2013, there were a total of 64 investments (fixed income and equity, excluding CDs), with a fair market value of $71.6 million, in an unrealized loss position totaling $1.6 million. The Company attributes these unrealized losses to increases in current market yields since the date the underlying securities were purchased and does not consider these investments to be other-than-temporarily impaired at June 30, 2013, because the decline in market value is not attributable to credit quality for fixed income securities, or a fundamental deterioration in the equity fund or issuers, and because the Company does not intend to, and it is more likely than not that it will not be required to, sell those investments prior to a market price recovery or maturity.

In assessing MBS investments and Federal Agency obligations, the contractual cash flows of these investments are guaranteed by an agency of the U.S. Government, and the agency that issued these securities is sponsored by the U.S. Government. Accordingly, it is expected that the securities would not be settled at a price less than the par value of the Company's investments. Management's assessment of other fixed income investments within the portfolio includes reviews of market pricing, ongoing credit quality evaluations, assessment of the investment's materiality, and duration of the unrealized loss position. In addition, the Company utilizes an outside registered investment adviser to manage the corporate and municipal bond portfolios, within prescribed guidelines set by management. At June 30, 2013 the Company's corporate and municipal bond portfolios did not contain any securities below investment grade, as reported by major credit rating agencies. For equities and funds, management's assessment includes the severity of the declines, whether it is unlikely that the security or fund will completely recover its unrealized loss within a reasonable time period and if the equity security or fund exhibits fundamental deterioration.

The small portion of the portfolio invested in short-term CDs was also in an unrealized loss position at June 30, 2013 due to market rates. The unrealized loss was not considered to be material and the securities are expected to be settled at par value at maturity.

The contractual maturity distribution at June 30, 2013 of total fixed income investments, excluding CDs which mature in less than one year, is as follows:

| | Within One Year | | | After One, But Within Five Years | | | After Five, But within Ten Years | | | After Ten Years | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Amortized Cost | Yields | | Amortized Cost | Yields | | Amortized Cost | Yields | | Amortized Cost | Yields | |
| At amortized cost: | | | | | | | | | | | | |
| Federal agency obligations | $15,502 | 0.76 | % | $49,609 | 0.92 | % | $— | — | % | $— | — | % |
| MBS | — | — | % | 49 | 1.54 | % | 11,150 | 3.00 | % | 41,364 | 1.80 | % |
| Municipal securities | 2,226 | 2.53 | % | 15,250 | 2.83 | % | 31,841 | 4.32 | % | 6,905 | 6.78 | % |

| | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Corporate bonds | — | — | % | 2,389 | 1.87 | % | 1,397 | 2.47 | % | — | — | % |
| Total fixed income securities | $17,728 | 0.98 | % | $67,297 | 1.39 | % | $44,388 | 3.93 | % | $48,269 | 2.51 | % |
| | | | | | | | | | | | | |
| At fair value: | | | | | | | | | | | | |
| Total fixed income securities | $17,794 | | | $67,696 | | | $45,488 | | | $47,845 | | |

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ENTERPRISE BANCORP, INC.
Notes to the Unaudited Consolidated Financial Statements (continued)

Scheduled contractual maturities may not reflect the actual maturities of the investments. MBS/CMOs are shown at their final maturity. However, due to prepayments and amortization the actual MBS/CMO cash flows may be faster than presented above. Similarly, included in the carrying value of fixed income investments above are callable securities, comprised of municipal securities, federal agency obligations and corporate bonds totaling $46.0 million, which can be redeemed by the issuer prior to the maturity presented above. Management considers these factors when evaluating the net interest margin in the Company's asset-liability management program.

See Note 12, "Fair Value Measurements" below for further information regarding the Company's fair value measurements for available-for-sale securities.

From time to time the Company may pledge securities as collateral against deposit account balances of municipal deposit customers, for Federal Home Loan Bank of Boston ("FHLB") borrowing capacity and as collateral for borrowing from the Federal Reserve Bank of Boston ("FRB"). The fair value of securities pledged as collateral for these purposes was $173.8 million at June 30, 2013.

(5) Restricted Investments

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

Based on management's ongoing review, the Company has not recorded any other-than-temporary impairment charges on this investment to date. However, if negative events or deterioration in the FHLB financial condition or capital levels occurs, the Company's investment in FHLB capital stock may become other-than-temporarily impaired to some degree.

(6) Loans

Major classifications of loans at the periods indicated, are as follows:

| (Dollars in thousands) | June 30, 2013 | December 31, 2012 |
|---|---|---|
| Real estate: | | |
| Commercial real estate | $785,994 | $710,265 |
| Commercial construction | 116,348 | 121,367 |
| Residential mortgages | 122,704 | 120,278 |
| Total real estate | 1,025,046 | 951,910 |
| Commercial and industrial | 343,509 | 328,579 |
| Home equity | 74,639 | 75,648 |
| Consumer | 5,649 | 4,911 |
| Gross loans | 1,448,843 | 1,361,048 |
| Deferred loan origination fees, net | (1,497) | (1,393) |
| Total loans | 1,447,346 | 1,359,655 |
| Allowance for loan losses | (25,671) | (24,254) |
| Net loans | $1,421,675 | $1,335,401 |

The Company specializes in lending to business entities, non-profit organizations, professionals and individuals. The Company's primary lending focus is on the development of high quality commercial relationships achieved through active business development efforts, long-term relationships with established commercial developers, strong community involvement and focused marketing strategies. Loans made to businesses include commercial mortgage loans, construction and land development loans, secured and unsecured commercial loans and lines of credit, and standby letters of credit. The Company also originates equipment lease financing for businesses. Loans made to individuals include conventional residential mortgage loans, home equity loans and lines, residential construction loans on primary and secondary residences, and secured and unsecured personal loans and lines of credit (see Note 7, "Allowance for Loan Losses," for additional information on the Company's credit risk management).

Loan Categories

- Commercial loans:

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

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

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

From time to time, the Company participates with other banks in the financing of certain commercial projects.  In some cases, the Company may act as the lead lender, originating and servicing the loans, but participating out a portion of the funding to other banks.  In other cases, the Company may participate in loans originated by other institutions. In each case, the participating bank funds a percentage of the loan commitment and takes on the related risk.  In each case in which the Company participates in a loan, the rights and obligations of each participating bank are divided proportionately among the participating banks in an amount equal to their share of ownership and with equal priority among all banks.  The balances participated out to other institutions are not carried as assets on the Company’s financial statements.  Loans originated by other banks in which the Company is the participating institution are carried in the loan portfolio at the Company’s pro rata share of ownership.  The Company performs an independent credit analysis of each commitment and a review of the participating institution prior to participation in the loan.  Loans originated by other banks in which the Company is the participating institution amounted to $35.5 million at June 30, 2013 and $28.6 million at December 31, 2012.

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

- Residential loans:

Enterprise originates conventional mortgage loans on one-to-four family residential properties. These properties may serve as the borrower's primary residence, vacation homes, or investment properties. Loan to value limits vary, generally from 80% for adjustable rate and multi-family, owner occupied properties, up to 97% for fixed rate loans on single family, owner occupied properties, with mortgage insurance coverage required for loan-to-value ratios greater than 80% based on program parameters. In addition, financing is provided for the construction of owner occupied primary and secondary residences. Residential

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mortgage loans may have terms of up to 30 years at either fixed or adjustable rates of interest. Fixed and adjustable rate residential mortgage loans are generally originated using secondary market underwriting and documentation standards.

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

- Home equity loans and lines of credit:

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

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

- Consumer loans:

Consumer loans primarily consist of secured or unsecured personal loans and overdraft protection lines on checking accounts extended to individual customers. The aggregate amount of overdrawn deposit accounts are reclassified as loan balances.

Loans serviced for others

At June 30, 2013 and December 31, 2012, the Company was servicing residential mortgage loans owned by investors amounting to $21.5 million and $22.2 million, respectively. Additionally, the Company was servicing commercial loans participated out to various other institutions amounting to $53.9 million and $53.6 million at June 30, 2013 and December 31, 2012, respectively. See the discussion above for further information regarding commercial participations.

Loans serving as collateral

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

| (Dollars in thousands) | June 30, 2013 | December 31, 2012 |
|---|---|---|
| Commercial real estate | $205,210 | $216,080 |
| Residential mortgages | 88,836 | 94,552 |
| Home equity | 18,009 | 18,907 |
| Total loans pledged to FHLB | $312,055 | $329,539 |

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Notes to the Unaudited Consolidated Financial Statements (continued)

(7) Allowance for Loan Loss

The Company manages its loan portfolio to avoid concentration by industry and loan size to minimize its credit risk exposure. In addition, the Company does not have a “sub-prime” mortgage program. However, inherent in the lending process is the risk of loss due to customer non-payment, or “credit risk.” While the Company endeavors to minimize this risk through the credit risk management function, management recognizes that loan losses will occur and that the amount of these losses will fluctuate depending on the risk characteristics of the loan portfolio and economic conditions.

Credit Quality Indicators

The level of adversely classified loans, delinquent and non-performing assets is largely a function of economic conditions, the overall banking environment, and the Company's underwriting, and credit risk management standards. The Company’s commercial lending focus may entail significant additional risks compared to long term financing on existing, owner-occupied residential real estate. The Company endeavors to minimize this risk through sound underwriting practices and the risk management function. The credit risk management function focuses on a wide variety of factors, including, among others, current and expected economic conditions, the real estate market, the financial condition of borrowers, the ability of borrowers to adapt to changing conditions or circumstances affecting their business and the continuity of borrowers’ management teams. Early detection of credit issues is critical to minimize credit losses. Accordingly, management regularly monitors these factors, among others, through ongoing credit reviews by the Credit Department, an external loan review service, reviews by members of senior management and the Loan Committee of the Board of Directors. This review includes the assessment of internal credit quality indicators such as the risk classification of individual loans, adversely classified loans, past due and non-accrual loans, impaired and restructured loans, and the level of foreclosure activity. However, despite prudent loan underwriting and ongoing credit risk management, adverse changes within the Company's market area or deterioration in the local, regional or national economic conditions could negatively impact the portfolio's credit risk profile and the Company's asset quality in the future.

The loan portfolio continued to show improving statistics related to migration of adversely classified, non-accrual, impaired loans and the level of Other Real Estate Owned ('"OREO") properties held during the quarter ended June 30, 2013. However, management believes that the credit profile of the portfolio will continue to be affected by lagging effects that the economic environment has had on the regional and local commercial markets.

- Adversely Classified Loans

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

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

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

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

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

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Notes to the Unaudited Consolidated Financial Statements (continued)

The following tables present the credit risk profile by internally assigned risk rating category at the periods indicated.

| | June 30, 2013 | | | | |
|---|---|---|---|---|---|
| | Adversely Classified | | | Not Adversely | |
| (Dollars in thousands) | Substandard | Doubtful | Loss | Classified | Gross Loans |
| Commercial real estate | $15,253 | $— | $— | $770,741 | $785,994 |
| Commercial and industrial | 6,012 | 500 | — | 336,997 | 343,509 |
| Commercial construction | 3,685 | — | — | 112,663 | 116,348 |
| Residential | 1,380 | — | — | 121,324 | 122,704 |
| Home equity | 696 | — | — | 73,943 | 74,639 |
| Consumer | 40 | — | — | 5,609 | 5,649 |
| Total gross loans | $27,066 | $500 | $— | $1,421,277 | $1,448,843 |

| | December 31, 2012 | | | | |
|---|---|---|---|---|---|
| | Adversely Classified | | | Not Adversely | |
| (Dollars in thousands) | Substandard | Doubtful | Loss | Classified | Gross Loans |
| Commercial real estate | $21,999 | $— | $— | $688,266 | $710,265 |
| Commercial and industrial | 5,993 | 1,460 | 48 | 321,078 | 328,579 |
| Commercial construction | 2,986 | — | — | 118,381 | 121,367 |
| Residential | 1,254 | — | — | 119,024 | 120,278 |
| Home equity | 661 | — | — | 74,987 | 75,648 |
| Consumer | 34 | — | — | 4,877 | 4,911 |
| Total gross loans | $32,927 | $1,460 | $48 | $1,326,613 | $1,361,048 |

The decrease in adversely classified loans since the prior period was due primarily to paydowns on several commercial relationships, and upgraded commercial loans, in particular one larger commercial real estate relationship of approximately $6.0 million classified as accruing/impaired/Troubled Debt Restructure (or "TDR") at December 31, 2012 which was upgraded during the period, due to the borrower's improved financial condition and sustained performance over time, partially offset by additional credit downgrades during the period.

- Past Due and Non-Accrual Loans

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

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The following tables present age analysis of past due loans as of the dates indicated.
Balance at June 30, 2013

| (Dollars in thousands) | Loans 30-59 Days Past Due | Loans 60-89 Days Past Due | Loans 90 or More Days Past Due (non-accrual) | Total Past Due Loans | Current Loans | Gross Loans |
|---|---|---|---|---|---|---|
| Commercial real estate | $1,921 | $183 | $12,645 | $14,749 | $771,245 | $785,994 |
| Commercial and industrial | 449 | 34 | 5,997 | 6,480 | 337,029 | 343,509 |
| Commercial construction | 727 | — | 1,442 | 2,169 | 114,179 | 116,348 |
| Residential | 1,500 | — | 995 | 2,495 | 120,209 | 122,704 |
| Home equity | 85 | — | 477 | 562 | 74,077 | 74,639 |
| Consumer | 10 | 9 | 14 | 33 | 5,616 | 5,649 |
| Total gross loans | $4,692 | $226 | $21,570 | $26,488 | $1,422,355 | $1,448,843 |

Balance at December 31, 2012

| (Dollars in thousands) | Loans 30-59 Days Past Due | Loans 60-89 Days Past Due | Loans 90 or More Days Past Due (non-accrual) | Total Past Due Loans | Current Loans | Gross Loans |
|---|---|---|---|---|---|---|
| Commercial real estate | $1,560 | $551 | $12,608 | $14,719 | $695,546 | $710,265 |
| Commercial and industrial | 472 | 55 | 6,993 | 7,520 | 321,059 | 328,579 |
| Commercial construction | — | — | 743 | 743 | 120,624 | 121,367 |
| Residential | 42 | 558 | 862 | 1,462 | 118,816 | 120,278 |
| Home equity | 73 | 9 | 390 | 472 | 75,176 | 75,648 |
| Consumer | 42 | 11 | 5 | 58 | 4,853 | 4,911 |
| Total gross loans | $2,189 | $1,184 | $21,601 | $24,974 | $1,336,074 | $1,361,048 |

At June 30, 2013 and December 31, 2012, all loans 90 or more days past due were carried as non-accruing. Included in the consumer non-accrual numbers in the table above were $8 thousand and $5 thousand of overdraft deposit account balances 90 days or more past due at June 30, 2013 and December 31, 2012, respectively. Total non-performing loans amounted to $21.6 million at both June 30, 2013 and December 31, 2012. Non-accrual loans which were not adversely classified amounted to $1.1 million at June 30, 2013 and $1.2 million at December 31, 2012. These balances primarily represented the guaranteed portions of non-performing Small Business Administration loans. The majority of the non-accrual loan balances were also carried as impaired loans during the periods noted, and are discussed further below. The increase in loans 30-59 days past due occurred primarily within the residential portfolio, due to a single large balance mortgage which was subsequently brought current, and in the commercial real estate and construction portfolios, with the majority of these loans just 30 days overdue at June 30, 2013.

The ratio of non-accrual loans to total loans amounted to 1.49% at June 30, 2013, 1.59% at December 31, 2012, and 1.93% at June 30, 2012.

At June 30, 2013, additional funding commitments for loans on non-accrual status totaled $592 thousand. The Company’s obligation to fulfill the additional funding commitments on non-accrual loans is generally contingent on the borrower’s compliance with the terms of the credit agreement. If the borrower is not in compliance, additional funding commitments may be made at the Company’s discretion.

- Impaired Loans

Impaired loans are individually significant loans for which management considers it probable that not all amounts due (principal and interest) in accordance with the original contractual terms will be collected. The majority of impaired loans are included within the non-accrual balances; however, not every loan in non-accrual status has been designated as impaired.

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Impaired loans include loans that have been modified in a troubled debt restructuring (see below). Impaired loans exclude large groups of smaller-balance homogeneous loans, such as residential mortgage loans and consumer loans, which are collectively evaluated for impairment and loans that are measured at fair value, unless the loan is amended in a TDR.

Management does not set any minimum delay of payments as a factor in reviewing for impaired classification. Management considers the individual payment status, net worth and earnings potential of the borrower, and the value and cash flow of the collateral as factors to determine if a loan will be paid in accordance with its contractual terms.

Impaired loans are individually evaluated for credit loss and a specific reserve is assigned for the amount of the estimated credit loss. Refer to heading "Allowance for probable loan losses methodology" contained in Note 5 "Allowance For Loan Losses," to the Company's consolidated financial statements contained in the Company's 2012 Annual Report on Form 10-K for further discussion of management's methodology used to estimate specific reserves for impaired loans.

Total impaired loans amounted to $29.3 million and $37.4 million, at June 30, 2013 and December 31, 2012, respectively. Total accruing impaired loans amounted to $8.6 million and $16.6 million at June 30, 2013 and December 31, 2012, respectively, while non-accrual impaired loans amounted to $20.7 million and $20.8 million as of June 30, 2013 and December 31, 2012, respectively. The decrease was primarily due to the changes discussed above under the heading "Adversely Classified Loans."

The following tables set forth the recorded investment in impaired loans and the related specific allowance allocated as of the dated indicated.

Balance at June 30, 2013

| (Dollars in thousands) | Unpaid contractual principal balance | Total recorded investment in impaired loans | Recorded investment with no allowance | Recorded investment with allowance | Related allowance |
|---|---|---|---|---|---|
| Commercial real estate | $ 18,212 | $16,245 | $11,873 | $4,372 | $915 |
| Commercial and industrial | 10,534 | 9,235 | 4,293 | 4,942 | 2,302 |
| Commercial construction | 3,034 | 2,916 | 986 | 1,930 | 739 |
| Residential | 846 | 799 | 377 | 422 | 163 |
| Home equity | 110 | 109 | — | 109 | 36 |
| Consumer | 19 | 19 | — | 19 | 19 |
| Total | $ 32,755 | $29,323 | $17,529 | $11,794 | $4,174 |

Balance at December 31, 2012

| (Dollars in thousands) | Unpaid contractual principal balance | Total recorded investment in impaired loans | Recorded investment with no allowance | Recorded investment with allowance | Related allowance |
|---|---|---|---|---|---|
| Commercial real estate | $24,760 | $22,859 | $18,735 | $4,124 | $1,041 |
| Commercial and industrial | 12,184 | 10,831 | 6,016 | 4,815 | 2,186 |
| Commercial construction | 3,091 | 2,932 | 995 | 1,937 | 753 |
| Residential | 687 | 648 | 390 | 258 | 65 |

| | | | | | |
|---|---|---|---|---|---|
| Home equity | 110 | 109 | — | 109 | 87 |
| Consumer | 14 | 14 | — | 14 | 14 |
| Total | $40,846 | $37,393 | $26,136 | $11,257 | $4,146 |

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

| | Three Months Ended June 30, 2013 | | Three Months Ended June 30, 2012 | |
|---|---|---|---|---|
| (Dollars in thousands) | Average recorded investment | Interest income recognized | Average recorded investment | Interest income recognized |
| Commercial real estate | $17,868 | $ 51 | $24,378 | $186 |
| Commercial and industrial | 9,252 | 24 | 9,806 | 68 |
| Commercial construction | 2,906 | 9 | 2,092 | (4) |
| Residential | 804 | 3 | 722 | 5 |
| Home equity | 109 | — | 50 | (1) |
| Consumer | 19 | — | 17 | — |
| Total | $30,958 | $ 87 | $37,065 | $254 |

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

| | Six Months Ended June 30, 2013 | | Six Months Ended June 30, 2012 | |
|---|---|---|---|---|
| (Dollars in thousands) | Average recorded investment | Interest income recognized | Average recorded investment | Interest income recognized |
| Commercial real estate | $20,155 | $149 | $24,281 | $310 |
| Commercial and industrial | 9,427 | 54 | 10,213 | 86 |
| Commercial construction | 2,902 | 33 | 2,054 | 17 |
| Residential | 807 | 4 | 698 | 5 |
| Home equity | 124 | — | 50 | — |
| Consumer | 16 | — | 17 | 1 |
| Total | $33,431 | $240 | $37,313 | $419 |

At June 30, 2013, additional funding commitments for impaired loans totaled $592 thousand. The Company's obligation to fulfill the additional funding commitments on impaired loans is generally contingent on the borrower's compliance with the terms of the credit agreement. If the borrower is not in compliance, additional funding commitments may be made at the Company's discretion.

- Troubled Debt Restructures

Loans are designated as a TDR when, as part of an agreement to modify the original contractual terms of the loan, the Bank grants a concession on the terms, that would not otherwise be considered, as a result of financial difficulties of the borrower.  Typically, such concessions may consist of a reduction in interest rate to a below market rate, taking into account the credit quality of the note, or a deferment or reduction of payments (principal or interest) which materially alters the Bank’s position or significantly extends the note’s maturity date, such that the present value of cash flows to be received is materially less than those contractually established at the loan’s origination. All loans that are modified are reviewed by the Company to identify if a TDR has occurred. TDR loans are included in the impaired loan category and, as such, these loans are individually evaluated and a specific reserve is assigned for the amount of the estimated credit loss.

Total TDR loans, included in the impaired loan figures above as of June 30, 2013 and December 31, 2012 were $18.9 million and $26.6 million, respectively.

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TDR loans on accrual status amounted to $8.1 million and $16.0 million at June 30, 2013 and December 31, 2012, respectively. During the current quarter, an accruing TDR commercial real estate relationship of approximately $6.0 million was upgraded and removed from impaired/TDR status, due to the borrower's improved financial condition and sustained performance over time. TDR loans included in non-performing loans amounted to $10.8 million and $10.5 million at June 30, 2013 and December 31, 2012, respectively. The Company continues to work with commercial relationships and enters into loan modifications to the extent deemed to be necessary or appropriate to ensure the best mutual outcome given the current economic environment.

Troubled debt restructure agreements entered into during the three month period ended June 30, 2013

| (Dollars in thousands) | Three months ended June 30, 2013 Number of restructurings | Pre-modification outstanding recorded investment | Post-modification outstanding recorded investment |
|---|---|---|---|
| Commercial real estate | — | $ — | $ — |
| Commercial and industrial | 1 | 100 | 62 |
| Commercial construction | — | — | — |
| Residential | — | — | — |
| Home equity | — | — | — |
| Consumer | — | — | — |
| Total | 1 | $ 100 | $ 62 |

Loans modified as troubled debt restructuring within the previous twelve months for which there was a subsequent payment default during the period noted are detailed below.

| (Dollars in thousands) | Three months ended June 30, 2013 Number of TDR's that defaulted | Post-modification outstanding recorded investment |
|---|---|---|
| Commercial real estate | — | $ — |
| Commercial and industrial | — | — |
| Commercial construction | 2 | 715 |
| Residential | — | — |
| Home equity | — | — |
| Consumer | — | — |
| Total | 2 | $ 715 |

Troubled debt restructure agreements entered into during the six month period ended June 30, 2013.

| (Dollars in thousands) | Six months ended June 30, 2013 | | |
|---|---|---|---|
| | Number of restructurings | Pre-modification outstanding recorded investment | Post-modification outstanding recorded investment |
| Commercial real estate | — | $ — | $ — |
| Commercial and industrial | 1 | 100 | 62 |
| Commercial construction | — | — | — |
| Residential | — | — | — |
| Home equity | — | — | — |
| Consumer | — | — | — |
| Total | 1 | $ 100 | $ 62 |

Loans modified as troubled debt restructuring within the previous twelve months for which there was a subsequent payment default during the period noted are detailed below.

| (Dollars in thousands) | Six months ended June 30, 2013 | |
|---|---|---|
| | Number of TDR's that defaulted | Post-modification outstanding recorded investment |
| Commercial real estate | 1 | $ 137 |
| Commercial and industrial | — | — |
| Commercial construction | 3 | 746 |
| Residential | — | — |
| Home equity | — | — |
| Consumer | — | — |
| Total | 4 | $ 883 |

There were $38 thousand in charge-offs associated with the TDRs, noted in the table above, during the six months ended June 30, 2013. Included in the table above were two TDR's modified during the previous twelve months which defaulted and were subsequently transferred to OREO during the current period with a total post modification outstanding balance of $167 thousand. At June 30, 2013, specific reserves allocated to the TDRs entered into during the 2013 period amounted to $1 thousand, as management considered it likely the principal would ultimately be collected.

ENTERPRISE BANCORP, INC.
Notes to the Unaudited Consolidated Financial Statements (continued)

Troubled debt restructure agreements entered into during the three month period ended June 30, 2012.

| | Three months ended June 30, 2012 | | |
|---|---|---|---|
| (Dollars in thousands) | Number of restructurings | Pre-modification outstanding recorded investment | Post-modification outstanding recorded investment |
| Commercial real estate | — | $ — | $ — |
| Commercial and industrial | 2 | 16 | 12 |
| Commercial construction | — | — | — |
| Residential | — | — | — |
| Home equity | — | — | — |
| Consumer | — | — | — |
| Total | 2 | $ 16 | $ 12 |

Loans modified as troubled debt restructuring within the previous twelve months for which there was a subsequent payment default during the period noted are detailed below.

| | Three months ended June 30, 2012 | |
|---|---|---|
| (Dollars in thousands) | Number of TDR's that defaulted | Post-modification outstanding recorded investment |
| Commercial real estate | — | $— |
| Commercial and industrial | 2 | 12 |
| Commercial construction | — | — |
| Residential | — | — |
| Home Equity | — | — |
| Consumer | — | — |
| Total | 2 | $12 |

Troubled debt restructure agreements entered into during six month the period ended June 30, 2012.

| | Six months ended June 30, 2012 | | |
|---|---|---|---|
| (Dollars in thousands) | Number of restructurings | Pre-modification outstanding recorded investment | Post-modification outstanding recorded investment |
| Commercial real estate | — | $ — | $ — |
| Commercial and industrial | 5 | 126 | 123 |
| Commercial construction | — | — | — |
| Residential | 1 | 130 | 128 |
| Home equity | — | — | — |
| Consumer | — | — | — |
| Total | 6 | $ 256 | $ 251 |

ENTERPRISE BANCORP, INC.
Notes to the Unaudited Consolidated Financial Statements (continued)

Loans modified as troubled debt restructuring within the previous twelve months for which there was a subsequent payment default during the period noted are detailed below.

| | Six months ended June 30, 2012 | |
|---|---|---|
| (Dollars in thousands) | Number of TDR's that defaulted | Post-modification outstanding recorded investment |
| Commercial real estate | — | $— |
| Commercial and industrial | 3 | 17 |
| Commercial construction | — | — |
| Residential | 1 | 128 |
| Home Equity | — | — |
| Consumer | — | — |
| Total | 4 | $145 |

There were no charge-offs associated with the TDRs noted in the tables above during the six months ended June 30, 2012. At June 30, 2012, specific reserves allocated to the TDRs entered into during the 2012 period amounted to $31 thousand, as management considered it likely the principal would ultimately be collected. Interest payments received on non-accruing new 2012 TDR loans which were applied to principal and not recognized as interest income amounted to $3 thousand for the six months ended June 30, 2012.

Other Real Estate Owned

Real estate acquired by the Company through foreclosure proceedings or the acceptance of a deed in lieu of foreclosure is classified as OREO. When property is acquired, it is generally recorded at the lesser of the loan’s remaining principal balance, net of any unamortized deferred fees, or the estimated fair value of the property acquired, less estimated costs to sell. Any loan balance in excess of the estimated realizable fair value on the date of transfer is charged to the allowance for loan losses on that date. All costs incurred thereafter in maintaining the property, as well as subsequent declines in fair value are charged to non-interest expense.

The carrying value of OREO at June 30, 2013 was $136 thousand and consisted of 1 property, compared to $500 thousand comprised of 1 property at December 31, 2012. During the six months ended June 30, 2013, 2 properties were sold, 1 of which was held at December 31, 2012, and 2 properties were added to OREO. There was $121 thousand of gains realized on the sale of OREO in 2013. There were $45 thousand gains on OREO sales during the six months ended June 30, 2012.

Allowance for probable loan losses methodology

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

There have been no material changes in the Company's underwriting practices, credit risk management system, or to the allowance assessment methodology used to estimate loan loss exposure as reported in the Company's most recent Annual Report on Form 10-K. Refer to heading "Allowance for probable loan losses methodology" contained in Note 5 "Allowance For Loan Losses," to the Company's consolidated financial statements contained in the Company's 2012 Annual Report on Form 10-K for further discussion of management's methodology used to estimate the loan loss exposure inherent in the portfolio for purposes of establishing a sufficient allowance.

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Allowance for loan loss activity

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

During the fourth quarter of 2012, the Company purchased a group of residential mortgage loans with a June 30, 2013 carrying value of $17.2 million. These purchased loans are initially booked at fair market value and, in accordance with accounting guidance, do not carry an initial allowance for loan losses. Management will continue to closely monitor this portfolio of non classified loans for estimated credit loss under general loss allocations taking into account the loss experience as well as the quantitative and qualitative factors identified above.

The allowance for loan losses amounted to $25.7 million at June 30, 2013 compared to $24.3 million at December 31, 2012. The allowance for loan losses to total loans ratio was 1.77% at June 30, 2013 and 1.78% at December 31, 2012 compared to 1.79% at June 30, 2012.

Based on management's judgment as to the existing credit risks inherent in the loan portfolio, as discussed above under the heading "Credit Quality Indicators," management believes that the Company's allowance for loan losses is adequate to absorb probable losses from specifically known and other credit risks associated with the portfolio as of June 30, 2013.

Changes in the allowance for loan losses by segment for the three months ended June 30, 2013, are presented below:

| (Dollars in thousands) | Cmml Real Estate | Cmml and Industrial | Cmml Constr | Resid. Mortgage | Home Equity | Consumer | Total |
|---|---|---|---|---|---|---|---|
| Beginning Balance at March 31, 2013 | $ 12,359 | $ 7,396 | $ 3,486 | $ 975 | $ 672 | $ 128 | $ 25,016 |
| Provision | 614 | 207 | (382) | 58 | 10 | 27 | 534 |
| Recoveries | 61 | 31 | 50 | — | — | 3 | 145 |
| Less: Charge offs | 14 | 1 | — | — | — | 9 | 24 |
| Ending Balance at June 30, 2013 | $ 13,020 | $ 7,633 | $ 3,154 | $ 1,033 | $ 682 | $ 149 | $ 25,671 |

Changes in the allowance for loan losses by segment for the six months ended June 30, 2013, are presented below:

| (Dollars in thousands) | Cmml Real Estate | Cmml and Industrial | Cmml Constr | Resid. Mortgage | Home Equity | Consumer | Total |
|---|---|---|---|---|---|---|---|
| Beginning Balance at December 31, 2012 | $ 11,793 | $ 7,297 | $ 3,456 | $ 854 | $ 728 | $ 126 | $ 24,254 |
| Provision | 1,180 | 428 | (352) | 51 | (23) | 33 | 1,317 |
| Recoveries | 61 | 41 | 50 | 128 | 21 | 6 | 307 |
| Less: Charge offs | 14 | 133 | — | — | 44 | 16 | 207 |
| Ending Balance at June 30, 2013 | $ 13,020 | $ 7,633 | $ 3,154 | $ 1,033 | $ 682 | $ 149 | $ 25,671 |
| Ending allowance balance: | | | | | | | |
| Allotted to loans individually evaluated for impairment | $ 915 | $ 2,302 | $ 739 | $ 163 | $ 36 | $ 19 | $ 4,174 |
| Allotted to loans collectively evaluated for impairment | $ 12,105 | $ 5,331 | $ 2,415 | $ 870 | $ 646 | $ 130 | $ 21,497 |

Changes in the allowance for loan losses by segment for the three months ended June 30, 2012, are presented below:

| (Dollars in thousands) | Cmml Real Estate | Cmml and Industrial | Cmml Constr | Resid. Mortgage | Home Equity | Consumer | Total |
|---|---|---|---|---|---|---|---|
| Beginning Balance at March 31, 2012 | $ 10,598 | $ 7,142 | $ 3,196 | $ 827 | $ 764 | $ 80 | $ 22,607 |
| Provision | 622 | 185 | 133 | 129 | (43) | 24 | 1,050 |
| Recoveries | — | 146 | — | — | — | | |