HINGHAM INSTITUTION FOR SAVINGS

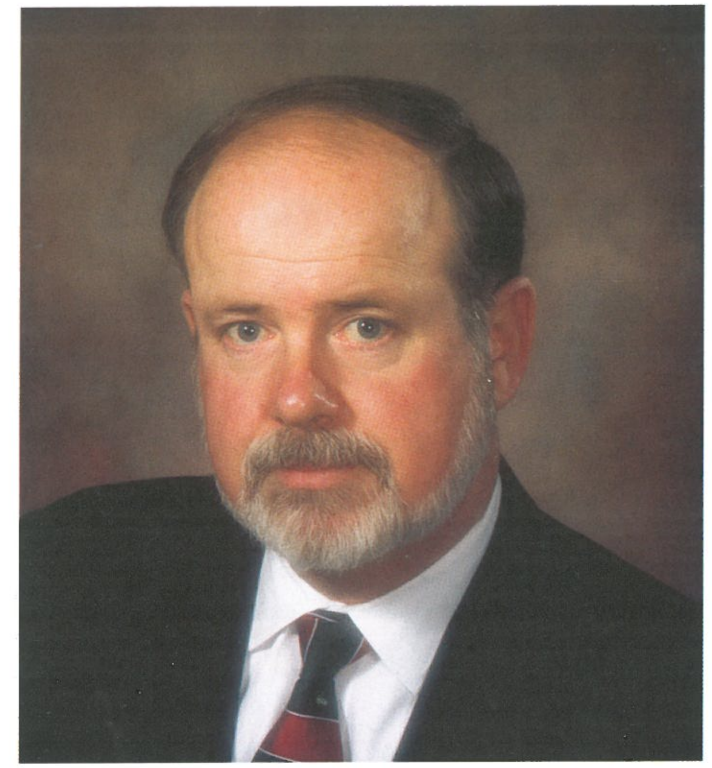
ESTABLISHED 1834

1995 ANNUAL REPORT

The traditional 4th of July parade proceeding down Main Street in front of Hingham Institution for Savings.

Photograph by: John F. Lavey

President's Message



Robert H. Gaughen, Jr., *President and C.E.O.*

Dear Stockholders:

In 1995, after two years of rapid recovery, the Bank commenced an aggressive expansion within our local market. We are well positioned to continue this expansion in 1996.

Our 1995 financial results demonstrate the following notable achievements. We had the highest pre-tax earnings in our 161-year history. Our total deposits grew by 14% over those of year end 1994. This growth rate was more than double the average of other New England thrifts. Our loan portfolio increased by 19%. This growth rate was triple that of the average of other New England thrifts.

This growth was achieved while we simultaneously continued to improve our asset quality. Total non-performing assets again decreased. They were reduced from $944,000 at December 31, 1994 to $672,000 at year end 1995. These assets represented only .38% of total assets, less than one-third the median for all publicly traded thrifts in Massachusetts.

This performance provided the framework for major enhancement in shareholder value. The market value of our stock experienced an impressive 44% increase during the course of the year. Cash dividends declared to stockholders increased by more than 100% over those declared in 1994.

The opening of our new branch offices in the towns of Cohasset and Scituate is intended to assist in our efforts to generate additional growth. These communities, along with the towns of Hingham and Hull, form a cohesive and attractive marketplace on the coast south of Boston. Our attentions in 1996 will continue to focus on the development of an institution that can provide the necessary array of basic financial services in a manner which acknowledges our market's unique history and sense of community.

The Board of Directors and management believe that the needs of stockholders, employees and the community at large are complementary. We are firm in our resolve to act in the best interest of each of these groups. We remain committed to the notion that a qualified and motivated staff, serving the needs of our community, will produce long-term benefits for our stockholders. Our primary competitive advantage continues to be the talented and committed staff whose efforts are highlighted in this report. Together, we look forward to meeting the challenges presented by our 162nd year.

Very truly yours,

Robert H. Gaughen, Jr.
President and Chief Executive Officer

Introducing Our Primary Assets

MAIN OFFICE AND ADMINISTRATION BUILDING

Main Office: *Phyllis Falletti, Helen Fuda, Jeanne Magner, Margaret Santacroce*

Lending Staff: *Sally Paulson, John DelSelva, Peter Smollett, Michael Sinclair, Deborah Pinkus*

HULL BRANCH OFFICE

Hull Branch: *Deborah Bearde, Laura Carlson*

COHASSET BRANCH OFFICE

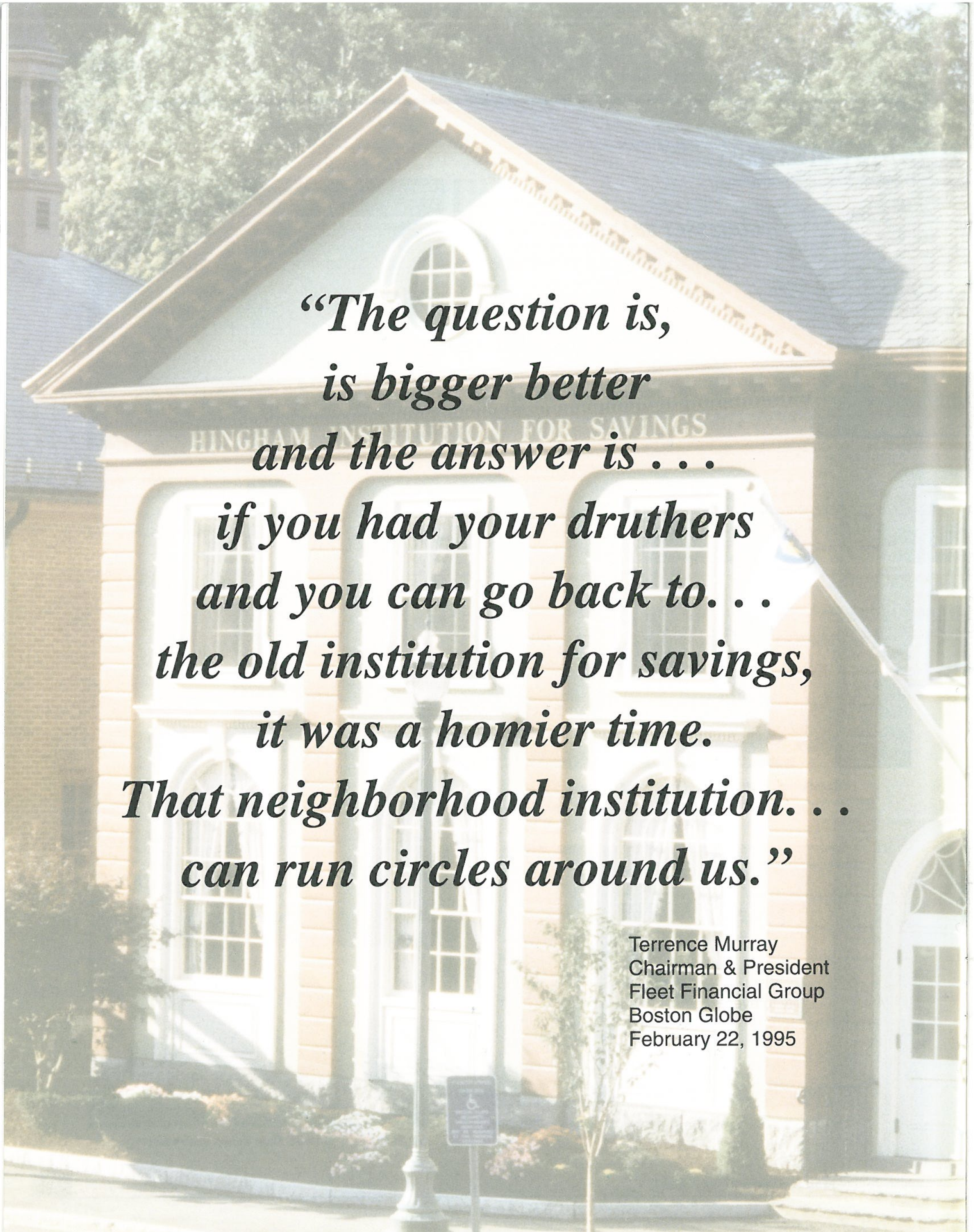
Cohasset Branch: *Patricia Murphy, Joanne Reynolds, Stephen Amico*

SCITUATE BRANCH OFFICE

Scituate Branch: *Marjorie Young, Stacy McKenna*

SOUTH HINGHAM BRANCH OFFICE

South Hingham Branch: *Rhea Kanke, Judith Hegarty*



"The question is,
is bigger better
and the answer is . . .
if you had your druthers
and you can go back to. . .
the old institution for savings,
it was a homier time.
That neighborhood institution. . .
can run circles around us."

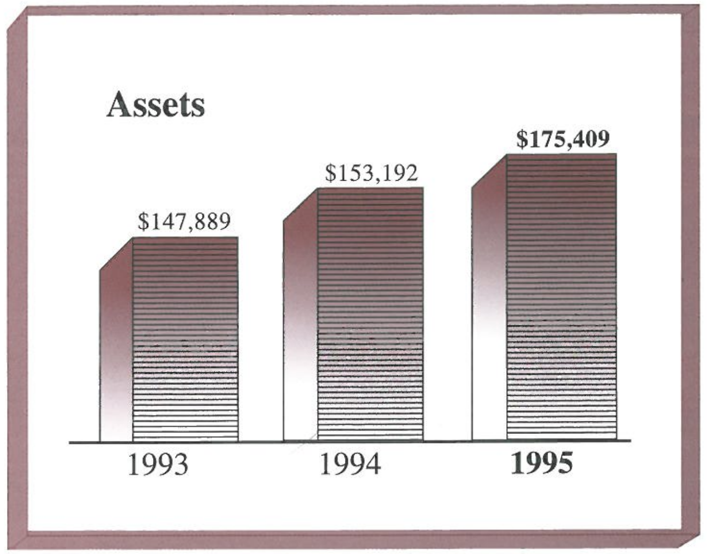
Terrence Murray
Chairman & President
Fleet Financial Group
Boston Globe
February 22, 1995

Selected Consolidated Financial Data

The following information does not purport to be complete and is qualified in its entirety by the more detailed information contained elsewhere herein.

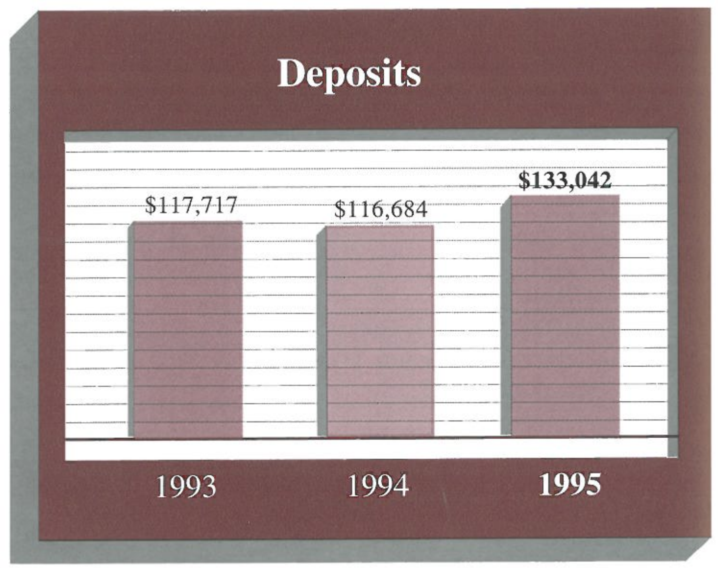
	At December 31,				
	1995	1994	1993	1992	1991
			(In Thousands)		
Balance Sheet Data:					
Total assets	$175,409	$153,192	$147,889	$149,460	$148,760
Investment securities	39,152	42,930	58,904	66,183	49,343
Loans:					
Mortgage	119,043	100,019	76,177	67,952	81,085
Commercial	978	959	695	920	1,047
Consumer	1,021	1,045	1,426	2,225	3,117
Allowance for loan losses	1,277	1,338	1,191	1,501	1,628
Foreclosed real estate, net	34	439	2,384	2,938	4,772
Deposits	133,042	116,684	117,717	119,885	120,721
Federal Home Loan Bank advances	22,000	19,000	15,000	15,000	15,000
Stockholders' equity	17,819	15,981	14,074	13,712	11,988

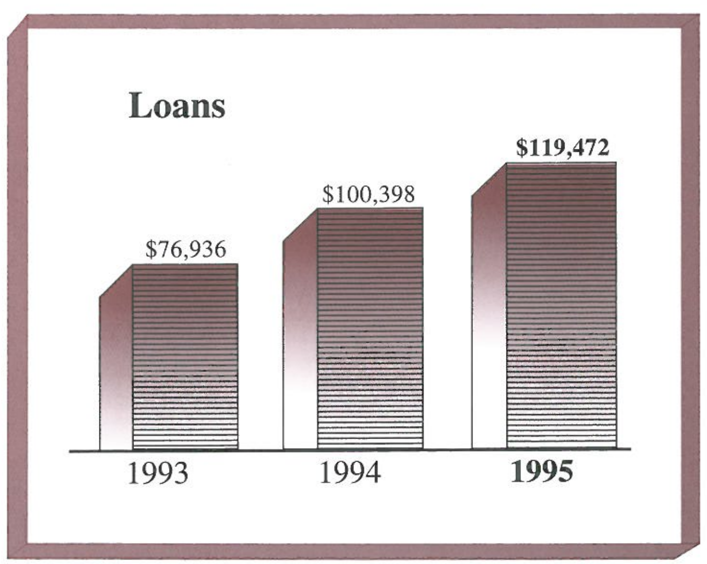
	Years Ended December 31,				
	1995	1994	1993	1992	1991
	(In Thousands, Except Per Share Amounts)				
Operating Data:					
Total interest and dividend income	$ 12,074	$ 9,963	$ 9,232	$ 11,374	$ 12,631
Total interest expense	5,871	4,324	4,593	6,451	8,850
Net interest income	6,203	5,639	4,639	4,923	3,781
Provision for loan losses	120	120	63	390	1,690
Other income	509	642	1,484	1,624	785
Operating expenses	3,641	3,860	6,340	4,999	4,734
Income (loss) before income taxes	2,951	2,301	(280)	1,158	(1,858)
Income tax provision (benefit)	1,045	(255)	(469)	(398)	1
Net income (loss)	$ 1,906	$ 2,556	$ 189	$ 1,556	$ (1,859)
Net income (loss) per share	$ 1.47	$ 1.99	$ 0.15	$ 1.24	$ (1.49)
Weighted average shares outstanding	1,294	1,284	1,268	1,251	1,250
Financial Ratios:					
Return (loss) on average assets	1.17%	1.70%	0.13%	1.02%	(1.23)%
Return (loss) on average equity	11.11	17.09	1.34	12.01	(13.74)
Average equity to average assets	10.54	9.94	9.52	8.52	8.92
Interest rate spread	3.42	3.55	3.06	3.21	2.69
Net yield on average earning assets	3.96	3.92	3.34	3.49	2.78
Cash dividends declared per share	$ 0.35	$ 0.17	—	—	—
Dividend payout ratio	23.81%	8.54%	—	—	—



Assets have increased nearly 19% since the end of 1993. Management has made a concerted effort to attract quality loans while decreasing its reliance on its investment portfolio. With a strong capital to asset ratio in excess of 10%, the Bank is poised for continued controlled growth.

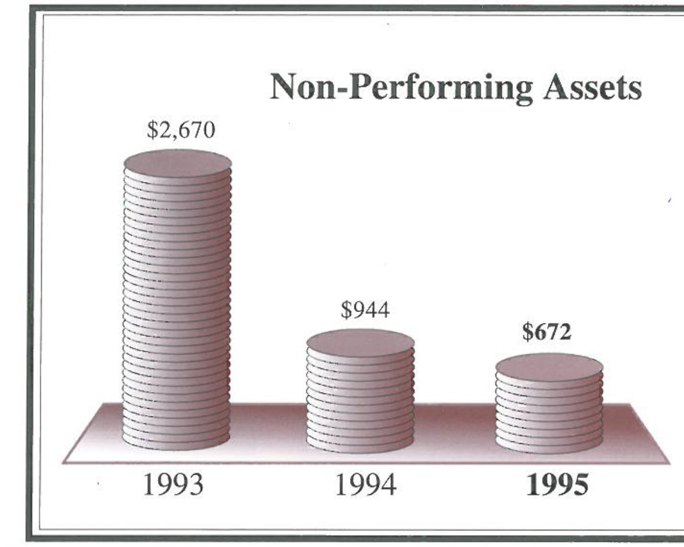
The Banks deposits are insured by both the Federal Deposit Insurance Corporation and the Depositors Insurance Fund. Product offerings include Passbook, Club and Statement Savings, NOW, Demand Deposit and Money Market Deposit accounts and certificates of deposit. Two new branches were opened in the fourth quarter of 1995 contributing to the significant increase in deposits. These new offices in Scituate and Cohasset will provide opportunities for further growth.

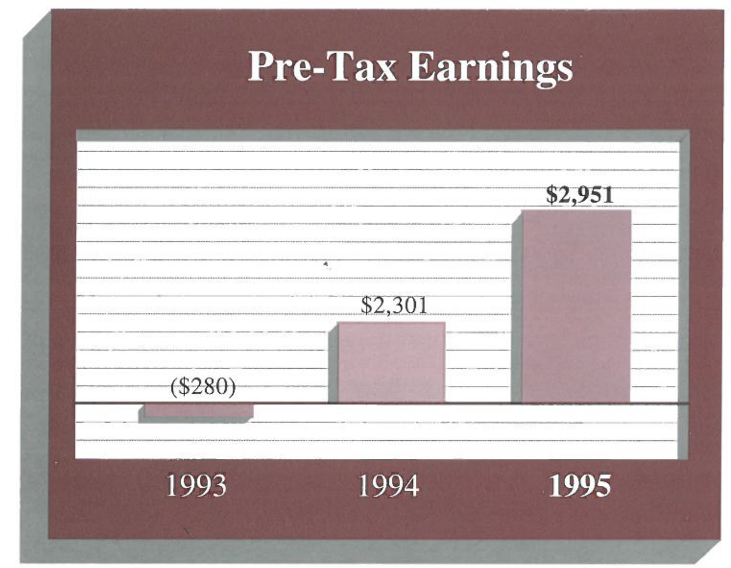




The Bank is committed to providing home ownership opportunities within the communities it serves. The Bank has achieved success in building its loan portfolio by originating residential and commercial mortgages and home equity loans.

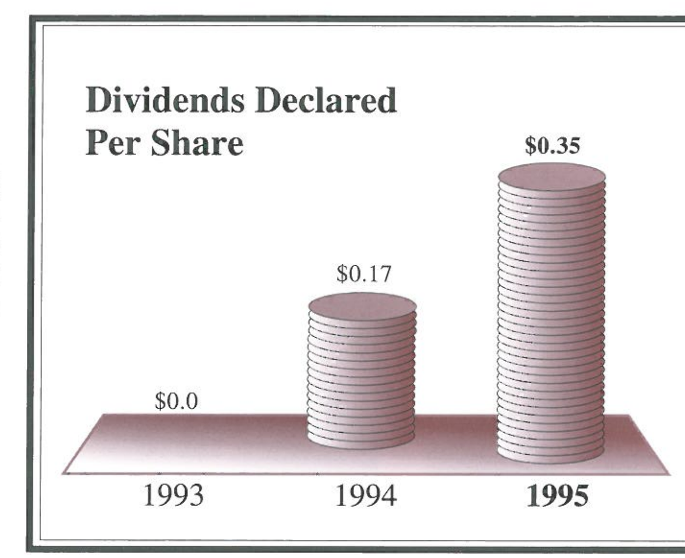
Nonperforming assets include both nonaccrual loans and foreclosed real estate. At year end 1995 the Bank held only one foreclosed asset. The Bank identifies troubled borrowers and works closely with them toward repayment. The positive trend in nonperforming assets reflects managements intensified collection efforts and improvements in underwriting.



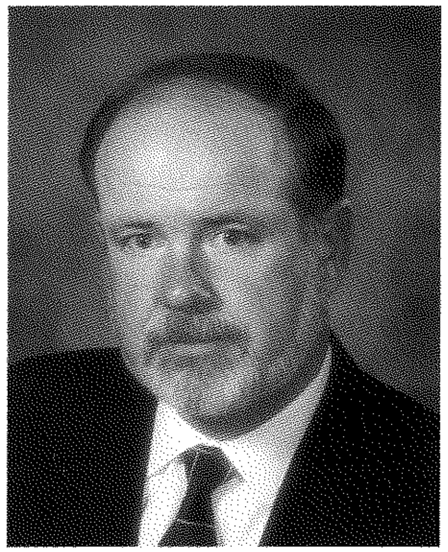


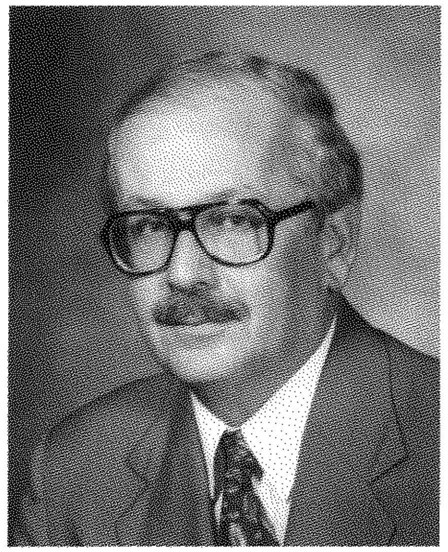
Improvements in net interest income and reductions in operating expenses brought pre-tax income to nearly $3.0 million for 1995. Asset mix played a key role in earnings performance with more than 68% of the Bank's assets in loans at year end 1995.

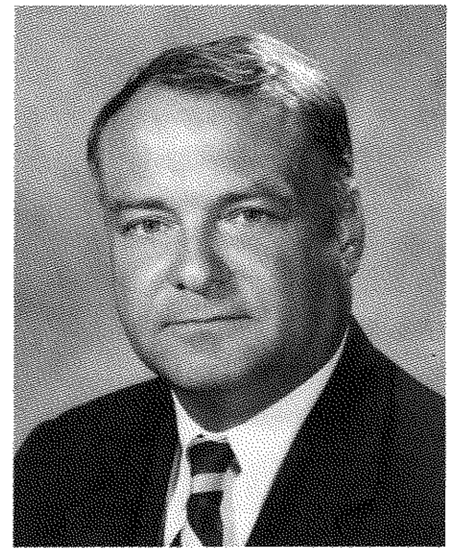
Quarterly dividends have shown steady improvement since 1993 culminating with an $0.08 per share dividend declared in the fourth quarter of 1995. In addition to the quarterly dividend, the Board of Directors also declared an $0.08 special cash dividend for the quarter based on the Bank's solid earnings performance.

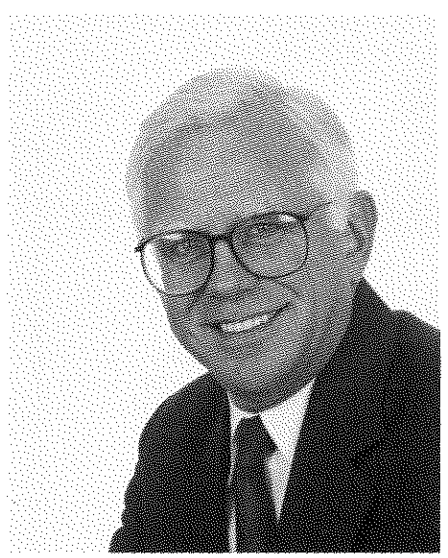


Senior Officers

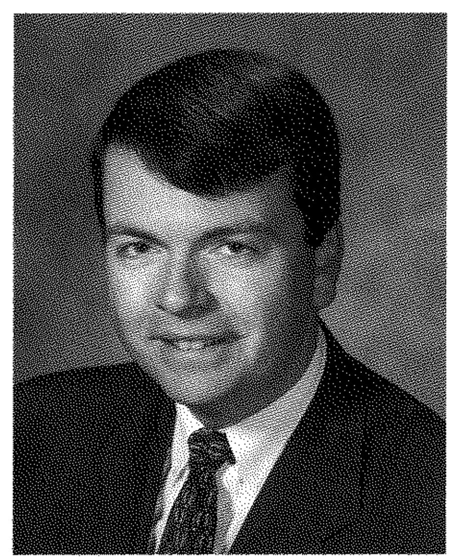

Robert H. Gaughen, Jr.
President and C.E.O.


William M. Donovan, Jr.
Vice President-Administration

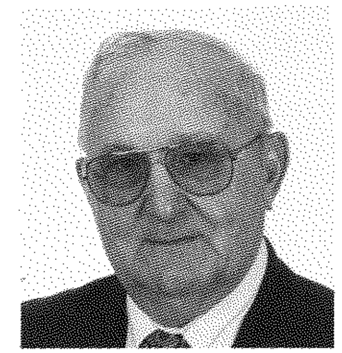

Peter R. Smollett
Vice President-Lending


Edward P. Zec
Vice President-Branch Operations

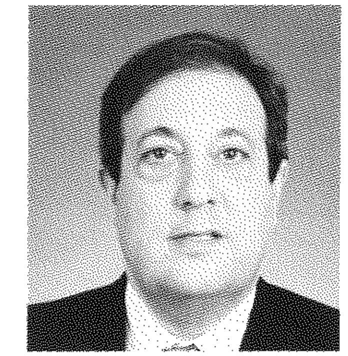

Deborah J. Jackson
Vice President and Treasurer

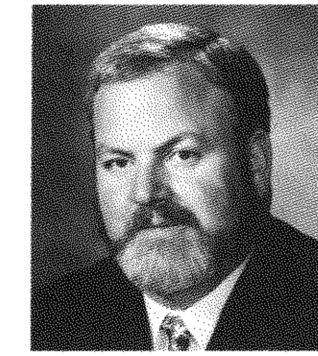

Michael J. Sinclair
Retail Lending Officer

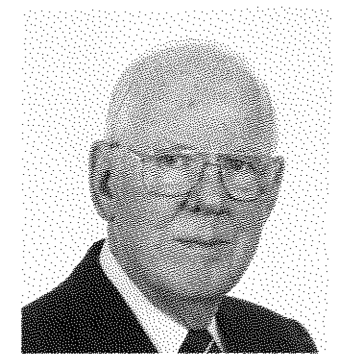
Directors

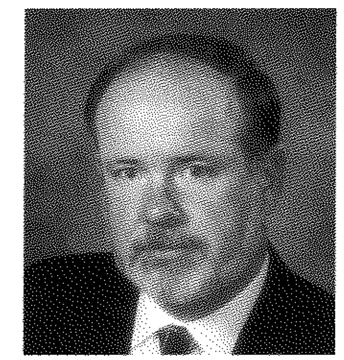

James V. Consentino

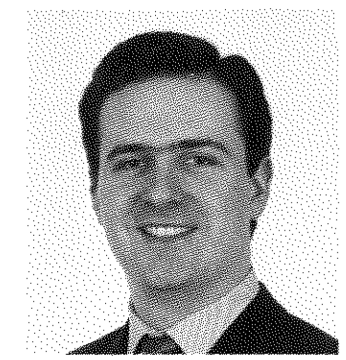

Marion J. Fahey


Ronald D. Falcione


Kevin W. Gaughen, Esq.


Robert H. Gaughen, Esq.


Robert H. Gaughen, Jr., Esq.


Julio R. Hernando, Esq.


Robert A. Lane, Esq.

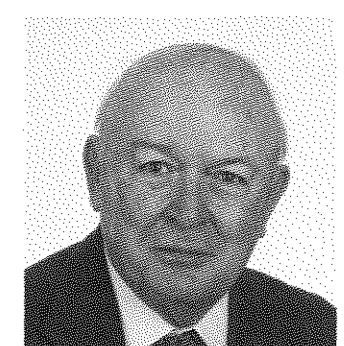

Warren B. Noble


Stacey M. Page

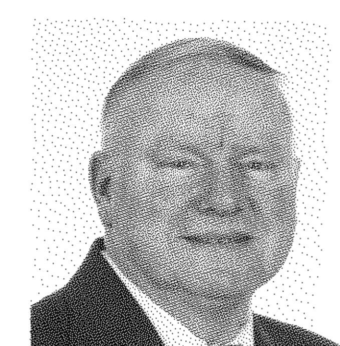

Edward L. Sparda


Donald E. Staszko


Donald M. Tardiff, M.D.


James R. White


Geoffrey C. Wilkinson, Sr.


Thomas H. Youngworth, Sr.

Management's Discussion and Analysis

Founded in 1834, Hingham Institution for Savings has served the local community for more than 161 years. On December 20, 1988, the Bank converted its ownership from mutual to stock form. Banking services are provided through branch offices in Hingham, South Hingham, Hull, Scituate and Cohasset.

The following information should be read in conjunction with the Consolidated Financial Statements and Notes contained in this report.

COMPARISON OF THE YEARS 1995, 1994, and 1993

RESULTS OF OPERATIONS

For the year ended December 31, 1995, the Bank earned $1.9 million, or $1.47 per share, as compared to $2.6 million, or $1.99 per share, for the same period in 1994, and $189,000 or $0.15 per share in 1993. The reduction in net income in 1995 can be attributed to the discontinuation of net tax benefits which were recorded in each of 1994 and 1993.

Pre-tax income shows continued and significant improvement. In 1995, pre-tax income was $3.0 million as compared to $2.3 million for 1994 and a negative $280,000 for 1993. The results in 1995 were achieved by a $564,000 improvement in the Bank's net interest income, a 49% reduction in deposit insurance expenses and a 94% reduction in foreclosed and other real estate expenses when compared to 1994. Pre-tax income increased in 1994 over 1993 by $2.6 million, primarily the result of an increase in net interest income and decreases in proxy related expenses and foreclosed and other real estate expenses.

Net Interest Income

The Bank reported $6.2 million in net interest income for 1995 as compared to $5.6 million in 1994, and $4.6 million in 1993. This positive trend was primarily the result of growth in loans and declines in the lower yielding investment portfolio. Further, the Bank's net yield on average earning assets was 3.96% in 1995, 3.92% in 1994 and 3.34% in 1993.

The following table presents information regarding changes in interest and dividend income and interest expense of the Bank for the years indicated. For each category, information is provided with respect to changes attributable to changes in rate (change in rate multiplied by old volume) and changes in volume (change in volume multiplied by old rate.) The change attributable to both volume and rate is allocated proportionately to the changes due to volume and rate.

	Years Ended December 31,					
	1995 Compared to 1994 Increase (Decrease)			1994 Compared to 1993 Increase (Decrease)		
	Due to			Due to		
	Volume	Rate	Total	Volume	Rate	Total
	(In Thousands)					
Interest and dividend income:						
Total loans	$1,792	$ 380	$2,172	$ 1,491	$(127)	$1,364
Investment securities and Federal Home Loan Bank stock	(533)	334	(199)	(610)	—	(610)
Interest-bearing deposits	70	68	138	(57)	34	(23)
Total interest and dividend income	1,329	782	2,111	824	(93)	731
Interest expense:						
Deposits	591	523	1,114	26	(422)	(396)
FHLB advances	232	201	433	48	79	127
Total interest expense	823	724	1,547	74	(343)	(269)
Net interest income	$ 506	$ 58	$ 564	$ 750	$ 250	$ 1,000

Management's Discussion and Analysis

The following table details changes in net interest income and net yield on average earning assets.

	Years Ended December 31,								
	1995			1994			1993		
	Average Balance	Interest	Yield/ Rate	Average Balance	Interest	Yield/ Rate	Average Balance	Interest	Yield/ Rate
	(Dollars in Thousands)								
Assets:									
Loans:									
Real estate loans	$107,842	$9,157	8.49%	$ 86,748	$7,011	8.08%	$ 67,791	$5,587	8.24%
Commercial loans	1,062	112	10.55	634	60	9.46	591	55	9.31
Other loans	944	86	9.11	1,264	112	8.86	1,773	177	9.98
Total loans (1) (2)	109,848	9,355	8.52	88,646	7,183	8.10	70,155	5,819	8.29
Investment securities (3) (4)	42,759	2,473	5.78	52,467	2,672	5.09	64,443	3,282	5.09
Interest-bearing deposits	4,232	246	5.81	2,795	108	3.86	4,483	131	2.92
Total earning assets	156,839	12,074	7.70	143,908	9,963	6.92	139,081	9,232	6.64
Other assets	5,884			6,571			8,882		
Total assets	$162,723			$150,479			$147,963		
Liabilities and stockholders' equity:									
Interest-bearing deposits:									
NOW accounts (5)	$ 10,581	157	1.48	$ 10,889	171	1.57	$ 10,234	246	2.40
Money market deposits	20,392	603	2.96	28,744	795	2.77	35,262	1,065	3.02
Regular	30,956	775	2.50	35,814	929	2.59	34,577	1,062	3.07
Term certificates	55,213	3,104	5.62	36,757	1,630	4.43	33,220	1,548	4.66
Total interest-bearing deposits	117,142	4,639	3.96	112,204	3,525	3.14	113,293	3,921	3.46
Federal Home Loan Bank advances	20,181	1,232	6.10	16,032	799	4.98	15,000	672	4.48
Total interest-bearing liabilities	137,323	5,871	4.28	128,236	4,324	3.37	128,293	4,593	3.58
Demand deposits	6,572			6,540			5,171		
Other liabilities	1,672			748			418		
Stockholders' equity	17,156			14,955			14,081		
Total liabilities and stockholders' equity	$162,723			$150,479			$147,963		
Net interest income		$6,203			$5,639			$4,639	
Weighted average rate spread			3.42%			3.55%			3.06%
Net yield on average earning assets (6)			3.96%			3.92%			3.34%

(1) Gross of allowance for loan losses.
(2) Includes average non-accrual loans.
(3) Excludes the impact of the average unrealized gain (loss) on securities available for sale.
(4) Includes Federal Home Loan Bank stock.
(5) Includes mortgagors' escrow accounts.
(6) Net interest income divided by average total earning assets.

Management's Discussion and Analysis

Interest income is derived from residential and commercial mortgages, home equity, commercial and installment loans, and the investment portfolio. The Bank earned an average yield of 7.70% on these assets in 1995, as compared to 6.92% in 1994 and 6.64% in 1993. For 1995, 1994 and 1993, interest income totaled $12.1 million, $10.0 million and $9.2 million, respectively. Average total earning assets increased $12.9 million, or 9%, in 1995 over 1994 and $4.8 million or 3%, in 1994 over 1993. The Bank achieved this growth by focusing on real estate lending and decreasing its emphasis on the investment portfolio. In addition, non-performing assets declined over the three periods to a total of $672,000 at December 31, 1995 from $944,000 at year end 1994 and $2.7 million at year end 1993.

Interest expense is incurred on certificates of deposit, NOW, savings and money market deposit accounts, and Federal Home Loan Bank ("FHLB") advances. The average rate paid on interest-bearing deposits was 3.96% during 1995, as compared to 3.14% for the 1994 period. During 1995, the Bank continued to experience growth in its higher cost certificate accounts. The average balance of interest-bearing deposit accounts was $117.1 million during 1995, compared to $112.2 million in 1994. The average rates paid on interest-bearing deposits declined during 1994 to 3.14% from 3.46% for 1993. Despite an increase in higher cost certificate accounts, the average balance of total interest-bearing deposits declined to $112.2 million during 1994 from $113.3 million in 1993.

Interest expense on FHLB advances continued to rise during 1995. The average rate paid on these advances as well as the average balance of advances continued to increase during 1995. The average rate paid on FHLB advances was 6.10% during 1995 as compared to 4.98% in 1994 and 4.48% during 1993. The average balance outstanding amounted to $20.2 million, $16.0 million and $15.0 million for the years ended December 31, 1995, 1994, and 1993, respectively. The recent downturn in market interest rates has allowed the Bank to refinance a substantial portion of its advances at lower rates, for longer terms, to insulate the Bank from future rises in market rates. The average rate for advances held at December 31, 1995 was lowered to 5.94%.

Provision for Loan Losses

The provision for loan losses is based on management's assessment of the adequacy of the allowance for loan losses. Management considers the size of the loan portfolio, the risks associated with certain loan types, and the underlying collateral values of individual loans as well as other factors. During 1995, the Bank originated more than $38.2 million in residential, commercial, and personal loans combined, increasing the loan portfolio to a total of $119.5 million at December 31, 1995. The provision for loan losses for 1995, 1994 and 1993 was $120,000, $120,000 and $63,000, respectively.

Other Income

Other income is comprised of customer service fees, net gains or losses on sales of investments, loans and other miscellaneous items. For 1994 and 1993 other income also included litigation settlements in the amounts of $282,000 and $515,000, respectively. The most significant component of other income in 1995 and 1994 was fees earned on customer accounts with $346,000 reported for 1995 and $345,000 for 1994. There were $271,000 in such fees earned in 1993. The rise in this income category when comparing 1994 to 1993 reflects revisions to the Bank's fee schedule. In 1995 and 1994, the Bank reported $49,000 and $232,000 in net losses on sales of securities classified as available for sale. The securities were earning below-market rates of interest and were sold to obtain liquidity to fund growth in the loan portfolio. There was $559,000 in net gains on sales of investments in 1993. Further, the Bank sold $2.4 million in fixed rate mortgages and student loans during the first quarter of 1994 at a combined gain of $30,000. There were no gains on loan sales in either 1995 or 1993.

Operating Expenses

There were $3.6 million in operating expenses in 1995 as compared to $3.9 million in 1994, and $6.3 million in 1993. The decline of $219,000 in 1995 from 1994 is primarily attributable to decreases in deposit insurance premiums and foreclosed and other real estate expenses. The decline of $2.5 million in 1994 from 1993 is primarily attributable to $1.5 million in expenses related to a proxy contest and the recognition of $310,000 in prior years' pension costs which were reported in 1993.

Salaries and employee benefits were the largest component of operating expenses at $1.8 million for 1995, $1.7 million for 1994, and $2.0 million for 1993. In the fourth quarter of 1995, the Bank hired eight employees to staff two new branches. This increased expense will continue throughout 1996. Prior year pension expenses of $310,000 are included as employee benefits expenses for 1993.

Foreclosed and other real estate expenses, net, include write-downs in property values, professional fees such as legal and property management, utilities, as well as various sundry items which are necessary to the operation of the real estate. These expenses are offset by any gains upon sale or recovery of expenses. Expenses related to foreclosed and other real estate, net, declined dramatically over each of the past three years with $15,000 reported in 1995, $265,000 in 1994, and $1.1 million in 1993. The declines are attributable to comparable declines in the number and value of foreclosed real estate properties. The Bank held only one property at December 31, 1995 at a net value of $34,000 as compared to $439,000 and $2.4 million at years ending 1994 and 1993, respectively.

Deposit insurance expense, comprised of federal and state deposit insurance premiums, also declined when comparing 1995 to 1994 and 1993. The most significant decrease occurred during 1995 when the Federal Deposit Insurance Corporation ("FDIC") awarded the Bank its lowest premium rate due to the Bank's improved financial condition and then, effective June, 1995 reduced this premium rate 85% to only $0.04 per hundred dollars of average deposits. The FDIC has indicated that there will be another significant reduction to this premium for 1996.

Other operating expenses including data processing, occupancy and equipment, legal, and other were $1.6 million combined for 1995 as compared to $1.6 million in 1994 and $1.5 million in 1993.

Income Taxes

In 1995, 1994 and 1993, the Bank was able to utilize net operating loss carryforwards to offset current taxable income and recognize deferred tax assets. As a result, the Bank recorded a net provision for income taxes in the amount of $1.0 million for the year ended December 31, 1995 versus income tax benefits amounting to $255,000 and $469,000 during 1994 and 1993, respectively. The effective net rate for federal and state income taxes in 1995 was 35%. The Bank anticipates that the combined rate will be approximately 41% during 1996.

COMPARISON OF THE YEARS 1995 AND 1994

BALANCE SHEET ANALYSIS

The Bank had total assets of $175.4 million at December 31, 1995, an increase of $22.2 million, or 15%, from the $153.2 million level at year end 1994.

Loans

At December 31, 1995, the Bank reported net loans of $119.5 million, or 68% of total assets. Comparably at December 31, 1994, net loans were $100.4 million, or 66% of total assets. This dramatic growth of $19.1 million, or 19%, was achieved through the origination of $38.2 million in mortgage and other loan products, a continuation of the lending effort initiated in mid-1993 by the new management team. A more stringent underwriting policy continues to complement this lending strategy. At December 31, 1995 and 1994, mortgage loans accounted for more than 98% of gross loans with commercial mortgages representing approximately 36% of this portfolio in 1995 and 33% in 1994.

The Bank's lending strategy during 1995 and 1994 has been to provide residential loans at primarily adjustable rates and multi-family or commercial property loans at an initial fixed rate for three to five years with a floating rate thereafter. Residential mortgages are generally underwritten to conform to Federal National Mortgage Association or Federal Home Loan Mortgage Corporation guidelines. The Bank also promotes home equity loans tied to the prime lending rate.

On January 1, 1995, the Bank adopted Statement of Financial Accounting Standards ("SFAS") No. 114 "Accounting by Creditors for Impairment of a Loan." The statement requires that impaired loans be measured on a loan by loan basis by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price, or the fair value of the collateral if the loan is collateral dependant. SFAS No. 114 also limits the classification of loans as in-substance foreclosures to situations where the creditor actually receives physical possession of the debtor's assets. There were $129,000 in properties which were reclassified to loans from foreclosed real estate pursuant to the adoption of this accounting standard.

The Bank's loan portfolio is reported net of the allowance for loan losses. At both December 31, 1995 and 1994, the allowance had a balance of $1.3 million.

The allowance is maintained at a level to absorb possible losses. Loan losses are charged against the allowance when the collectibility of loan principal becomes unlikely. Recoveries are recorded as additional reserves when received. There were $188,000 in charge-offs and $7,000 in recoveries in 1995. Comparably, in 1994 there were $105,000 in loans charged against the allowance and $132,000 in recoveries received.

Non-performing assets, which consist of nonaccrual loans and foreclosed real estate totaled $672,000, or 0.38% of total assets, at December 31, 1995, as compared to $944,000, or 0.62% of total assets, at year end 1994.

The following table presents information regarding the Bank's non-performing assets:

At December 31,	1995	1994
	(In Thousands)	
Nonaccrual Loans:		
Residential Mortgages (1)	$630	$ 432
Commercial Loans	6	48
Installment Loans	2	25
Total Nonaccrual Loans	638	505
Foreclosed Real Estate, Net	34	439
Total Non-performing Assets	$672	$ 944

(1) Includes home equity loans.

Investments

The purpose of the Bank's investment portfolio is to supplement the Bank's lending activities by generating income, providing liquidity through the receipt of principal and interest payments, and use as collateral to obtain borrowed funds. At December 31, 1995, the portfolio was comprised of mortgage-backed and agency issues for a total of $39.2 million, or 22% of total assets, as compared to $42.9 million, or 28% of total assets, at year end 1994. All securities in the portfolio are issued or guaranteed by U.S. Government agencies or U.S. Government sponsored agencies and, as such, carry a relatively low risk-weighting under Federal Deposit Insurance Corporation ("FDIC") risk-based capital guidelines.

A substantial portion of the Bank's investment portfolio is comprised of mortgage-backed securities which are subject to declines in principal balances due to principal repayments. These repayments tend to increase as market interest rates fall and the individual underlying mortgages are refinanced at lower rates. Conversely, repayments tend to decrease as market interest rates rise. There were $3.7 million in principal repayments received during 1995 as compared to $8.8 million during 1994.

Since the establishment of SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities", the FDIC has contemplated the treatment of unrealized gains and losses on available-for-sale securities for regulatory capital calculations. Effective January 27, 1995, the FDIC issued a final rule which allowed member banks to exclude any unrealized gains and losses from the definition of Tier 1 Capital. Subsequently, the Financial Accounting Standards Board, ("FASB") allowed companies to reclassify held-to-maturity securities to available for sale or trading.

On December 31, 1995 the Bank opted to classify its entire portfolio as available for sale. In comparison, the portfolio consisted of $13.9 million in available-for-sale securities and $29.1 million in held-to-maturity securities at December 31, 1994. There were no securities classified as trading in either year.

Available-for-sale securities are carried at fair value with unrealized gains or losses reported as a separate component of stockholders' equity and held-to-maturity securities are carried at amortized cost. The unrealized loss on available-for-sale securities amounted to $155,000, net of tax effects, at December 31, 1995 as compared to $525,000 at year end 1994, reflecting an improvement in market conditions. The fair value of securities fluctuates with the movement of interest rates. Generally, during periods of decreasing interest rates, the fair values increase whereas the opposite may hold true during a rising interest rate environment.

Deposits

At December 31, 1995, the Bank held a total of $133.0 million in deposits, an increase of $16.3 million from the $116.7 million in deposits at year end 1994. The Bank offers a wide range of products, competitively priced, accompanied by quality service. During the fourth quarter of 1995 the Bank opened branch offices in the towns of Scituate and Cohasset. Approximately $3.7 million of the 1995 deposit growth is the result of the Bank's expansion.

Primary competition for deposits are the other banks in the Bank's market area and mutual funds. The Bank's ability to attract and retain deposits depends upon satisfaction of depositors' requirements with respect to rate, liquidity, risk, and service. The Bank offers competitive

rates, convenient branch locations, and the added convenience of automated teller machines. Deposits are insured in full through the Federal Deposit Insurance Corporation and Depositors Insurance Fund. This insurance, combined with the Bank's strong capital position, should provide an advantage in allaying any customer concerns regarding the safety of their deposits.

Core deposits, comprised of savings, NOW, and money market accounts were $69.2 million, or 52% of total deposits, at December 31, 1995 as compared to $74.1 million, or 63% of total deposits, at year end 1994, a decrease of $4.9 million. Conversely, certificates of deposit were $63.9 million at December 31, 1995 as compared to $42.6 million at year end 1994, an increase of $21.3 million. This shift from core deposits to certificates of deposit, at higher rates, has resulted in increased deposit costs.

Borrowings

The Bank had $22.0 million in FHLB advances at December 31, 1995, as compared to $19.0 million at year end 1994. The Bank borrowed an additional $3.0 million in 1995 to fund growth in the loan portfolio and to effectively manage its interest rate sensitivity position.

Liquidity and Capital Resources

The Bank's primary sources of liquidity are its available-for-sale securities portfolio, principal and interest payments on loans and investment securities, net increases in deposit balances, and FHLB advances.

As a member of the Federal Home Loan Bank, the Bank is eligible to obtain both short and long-term credit advances. The Bank can borrow up to approximately $89.7 million to meet its borrowing needs. Borrowing capacity is limited to the Bank's available qualified collateral which consists primarily of 1-4 family residential mortgages and certain investment securities. At December 31, 1995, the Bank had $22.0 million in advances with original maturities from three months to three years. There were no advances against the Bank's $2.6 million short-term credit line at that date.

The Bank can also enter into repurchase agreement transactions should the need for additional liquidity arise. At December 31, 1995, the Bank had no repurchase agreements outstanding.

At December 31, 1995, the Bank had capital of $17.8 million, or 10.16% of total assets, as compared to $16.0 million, or 10.43%, at December 31, 1994. The Bank's capital is subject to fluctuations resulting from changes in the market values of its investment securities. Total capital is adjusted by the unrealized gains or losses in the Bank's available-for-sale securities portfolio. At December 31, 1995 the Bank's entire securities portfolio was classified as available for sale, which had the effect of reducing capital by $155,000. In comparison, at year end 1994, when the Bank had 32% of its portfolio classified as available for sale, capital was reduced by $525,000. A decreasing interest rate environment in the latter part of 1995 translated into increased Bank capital. Effective January 27, 1995 these unrealized gains and losses are no longer considered in calculating FDIC capital ratios.

Massachusetts chartered savings banks that are insured by the FDIC are subject to minimum capital maintenance requirements. Regulatory guidelines define the minimum amount of qualifying capital an institution must maintain as a percentage of risk-weighted assets (Risk-Based Capital Ratios) and average total assets (Leverage Ratio). The Bank's ratios exceeded these regulatory capital requirements in both 1995 and 1994.

	December 31, 1995	December 31, 1994	Minimum Regulatory Ratios
Risk-Based Capital Ratios:			
Tier One Capital	17.05%	18.84%	4%
Total Capital	18.26%	20.09%	8%
Leverage Ratio	10.33%	10.88%	3-5%

These high capital levels were maintained despite a more aggressive dividend policy. During 1995 the Bank declared dividends of $0.35 per share, which included an $0.08 per share special dividend which was declared in the fourth quarter. In comparison, in 1994, the Bank declared $0.17 per share in dividends. The most recent quarterly dividend of $0.08 per share reflects a 100% improvement over the $0.04 per share dividend when the Bank resumed dividend declarations during the first quarter of 1994. The Bank's dividend payout ratio, which is calculated by dividing dividends per share into earnings per share, improved to 23.81% for 1995 as compared to 8.54% for 1994.

Management's Discussion and Analysis

IMPACT OF INFLATION AND CHANGING PRICES

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

REGULATORY MATTERS

In March of 1992, the Bank's Board of Directors entered into a Memorandum of Understanding ("Memorandum") with the FDIC and the Massachusetts Commissioner of Banks. Based on the December 27, 1994 Regulatory Report of Examination, the Bank was found to be in general compliance with the provisions contained in the Memorandum and material improvement in the Bank's financial condition was noted. As a result, the Commissioner of Banks and the FDIC removed the Memorandum effective May 8, 1995.

MATERIAL LITIGATION

In February 1993, Robert H. Gaughen, a shareholder and Director of the Bank, notified the Bank of his intention to nominate an independent slate of nominees for the Board of Directors. Subsequent to this notification, the Board of Directors by an 8 to 7 vote, initiated litigation against Mr. Gaughen and three other Directors and substantial shareholders, which litigation sought to prevent the solicitation of proxies in support of the independent slate of nominees. Mr. Gaughen then initiated suit against existing management of the Bank and the majority of the Board of Directors alleging breach of fiduciary responsibility and other irregularities with regard to prior management's conduct of the affairs of the Bank. After a hearing in the United States District Court of Massachusetts, the Bank's request for injunctive relief preventing Mr. Gaughen's solicitation of proxies was denied by United States District Court Judge Edward Harrington. Subsequent to prior management's failure to obtain such an order, the foregoing litigation was concluded by the exchange of mutual releases and the agreement to allow all shareholders to vote at the annual meeting. Proxy related expenses totalling $1.5 million were reflected in the Bank's Statement of Income in 1993.

The Bank contends that a substantial amount of cumulative loan losses it sustained prior to 1993 resulted from former president Wilfred H. Creighton's alleged conduct. In February 1993, the Bank reached a settlement agreement with its insurance carrier in the amount of $515,000 to compensate the Bank for its losses suffered by the former president's conduct. The settlement allowed the Bank to maintain its lawsuit against its former president without competition from the insurance carrier to recover the amount paid under the claim. This recovery is reflected in the Statement of Income in 1993. In February 1994, the Bank obtained four parcels of developed real estate from the former president as settlement of its lawsuit. This recovery of $282,000 is reflected in the Statement of Income in 1994.

Currently, the Bank is not a party to any legal proceedings other than routine litigation incidental to the Bank's business. The Bank is a defendant in one lawsuit. In addition, in certain collection actions initiated by the Bank, the debtor defendants have counterclaimed. In each case, the Bank anticipates a successful result with no probable losses.

INDEPENDENT AUDITORS' REPORT

To the Board of Directors and Stockholders of
Hingham Institution for Savings

We have audited the consolidated balance sheets of Hingham Institution for Savings and subsidiaries as of December 31, 1995 and 1994, and the related consolidated statements of income, changes in stockholders' equity and cash flows for each of the years in the three-year period ended December 31, 1995. These consolidated financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Hingham Institution for Savings and subsidiaries as of December 31, 1995 and 1994, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 1995 in conformity with generally accepted accounting principles.

Wolf + Company, P. C.

Boston, Massachusetts
January 22, 1996

Consolidated Balance Sheets

December 31, 1995 and 1994

ASSETS

	1995	1994
	(In Thousands)	
Cash and due from banks (Note 2)	$ 4,515	$ 3,897
Interest-bearing deposits	6,071	11
Cash and cash equivalents	10,586	3,908
Securities available for sale (Notes 3 and 8)	39,152	13,866
Securities held to maturity (Notes 3 and 8)	—	29,064
Loans, net of allowance for loan losses of $1,277,000 in 1995 and $1,338,000 in 1994 (Notes 4 and 8)	119,472	100,398
Foreclosed real estate, net (Note 5)	34	439
Banking premises and equipment, net (Note 6)	2,496	1,699
Accrued interest receivable	1,048	835
Deferred income tax asset, net (Note 9)	1,045	1,557
Federal Home Loan Bank stock, at cost (Note 8)	1,200	994
Other assets	376	432
	$ 175,409	$ 153,192

LIABILITIES AND STOCKHOLDERS' EQUITY

	1995	1994
Deposits (Note 7)	$ 133,042	$ 116,684
Federal Home Loan Bank advances (Note 8)	22,000	19,000
Accrued interest payable	505	358
Mortgagors' escrow accounts	287	252
Other liabilities (Note 14)	1,756	917
Total liabilities	157,590	137,211
Commitments and contingencies (Notes 10 and 11)		
Stockholders' equity (Notes 12 and 13):		
Preferred stock, $1.00 par value, 2,500,000 shares authorized; none issued	—	—
Common stock, $1.00 par value, 5,000,000 shares authorized; 1,295,000 and 1,293,000 shares issued and outstanding	1,295	1,293
Additional paid-in capital	8,597	8,584
Undivided profits	8,082	6,629
	17,974	16,506
Net unrealized loss on securities available for sale, after tax effect (Note 3)	(155)	(525)
Total stockholders' equity	17,819	15,981
	$175,409	$153,192

See accompanying notes to consolidated financial statements.

Consolidated Statements of Income

Years Ended December 31, 1995, 1994 and 1993

	1995	1994	1993
	(In Thousands, Except Per Share Data)		
Interest and dividend income:			
Loans	$ 9,355	$ 7,183	$ 5,819
Investment securities	2,473	2,672	3,282
Interest-bearing deposits	246	108	131
Total interest and dividend income	12,074	9,963	9,232
Interest expense:			
Deposits (Note 7)	4,639	3,525	3,921
Federal Home Loan Bank advances	1,232	799	672
Total interest expense	5,871	4,324	4,593
Net interest income	6,203	5,639	4,639
Provision for loan losses (Note 4)	120	120	63
Net interest income, after provision for loan losses	6,083	5,519	4,576
Other income:			
Customer service fees on deposits	346	345	271
Gain (loss) on sale of investments, net (Note 3)	(49)	(232)	559
Litigation settlement (Note 11)	—	282	515
Other	212	247	139
Total other income	509	642	1,484
Operating expenses:			
Salaries and employee benefits (Note 14)	1,838	1,677	1,968
Data processing	298	288	292
Occupancy and equipment (Note 6)	372	332	373
Foreclosed and other real estate, net (Note 5)	15	265	1,053
Expenses related to proxy contest (Note 11)	—	—	1,508
Legal	66	143	133
Deposit insurance	159	309	330
Other	893	846	683
Total operating expenses	3,641	3,860	6,340
Income (loss) before income taxes	2,951	2,301	(280)
Income tax provision (benefit) (Note 9)	1,045	(255)	(469)
Net income	$ 1,906	$ 2,556	$ 189
Earnings per common share	$ 1.47	$ 1.99	$ .15
Weighted average shares outstanding	1,294	1,284	1,268

See accompanying notes to consolidated financial statements.

HINGHAM INSTITUTION FOR SAVINGS ESTABLISHED 1834

Consolidated Statements of Changes in Stockholders' Equity

Years Ended December 31, 1995, 1994 and 1993

	Common Stock	Additional Paid-in Capital	Undivided Profits	Net Unrealized Loss on Marketable Equity Securities (In Thousands)	Net Unrealized Gain (Loss) on Securities Available for Sale	Total Stockholders' Equity
Balance at December 31, 1992	$1,253	$8,380	$4,103	$ (24)	$ —	$13,712
Net income	—	—	189	—	—	189
Decrease in net unrealized loss on marketable equity securities	—	—	—	24	—	24
Stock options exercised	24	73	—	—	—	97
Change in method of accounting for investment securities (Note 1)	—	—	—	—	52	52
Balance at December 31, 1993	1,277	8,453	4,292	—	52	14,074
Net income	—	—	2,556	—	—	2,556
Change in net unrealized gain (loss) on securities available for sale, after tax effect	—	—	—	—	(577)	(577)
Stock options exercised, after tax effect	16	131	—	—	—	147
Cash dividends declared ($.17 per share)	—	—	(219)	—	—	(219)
Balance at December 31, 1994	1,293	8,584	6,629	—	(525)	15,981
Net income	—	—	1,906	—	—	1,906
Change in net unrealized gain (loss) on securities available for sale, after tax effect	—	—	—	—	370	370
Stock options exercised, after tax effect	2	13	—	—	—	15
Cash dividends declared ($.35 per share)	—	—	(453)	—	—	(453)
Balance at December 31, 1995	$1,295	$8,597	$8,082	—	$ (155)	$17,819

See accompanying notes to consolidated financial statements.

HINGHAM INSTITUTION FOR SAVINGS ESTABLISHED 1834

Consolidated Statements of Cash Flows

Years Ended December 31, 1995, 1994 and 1993

	1995	1994 (In Thousands)	1993
Cash flows from operating activities:			
Net income	$1,906	$2,556	$ 189
Adjustments to reconcile net income to net cash provided by operating activities:			
Provision for loan losses	120	120	63
Provision for losses on foreclosed and other real estate	20	142	762
Amortization of premium on investment securities, net of accretion	288	514	533
Amortization of deferred loan fees, net	(62)	(54)	(40)
Depreciation	133	115	139
(Gain) loss on sale of investments, net	49	232	(559)
Gain on sale of loans	—	(30)	—
Gain on sale of foreclosed and other real estate	(4)	(63)	(20)
Changes in operating assets and liabilities:			
Accrued interest receivable	(213)	67	94
Deferred income tax asset	(249)	(300)	(472)
Other assets	(17)	(127)	153
Accrued interest payable and other liabilities	843	302	193
Net cash provided by operating activities	3,312	3,474	1,035
Cash flows from investing activities:			
Proceeds from sales of securities available for sale	1,463	10,400	—
Purchase of securities available for sale	(4,882)	(2,036)	—
Purchase of securities held to maturity	(2,183)	(3,000)	—
Proceeds from maturities of securities available for sale	4,000	100	—
Proceeds from maturities of securities held to maturity	2,000	—	—
Proceeds from sales of investment securities	—	—	36,396
Principal payments received on mortgage-backed securities	3,676	8,802	20,946
Purchase of investment securities	—	—	(49,961)
Loans originated, net of payments received	(18,832)	(25,295)	(7,829)
Proceeds from sale of loans	—	2,424	447
Additions to foreclosed and other real estate, net of payments	(110)	4	(4)
Proceeds from sales of foreclosed and other real estate	279	1,414	2,487
(Increase) decrease in Federal Home Loan Bank stock	(206)	—	6
Additions to banking premises and equipment	(930)	(265)	(55)
Net cash provided by (used in) investing activities	(15,725)	(7,452)	2,433

(continued)

See accompanying notes to consolidated financial statements.

Consolidated Statements of Cash Flows

(Concluded)

Years Ended December 31, 1995, 1994 and 1993

	1995	1994	1993
		(In Thousands)	
Cash flows from financing activities:			
Increase (decrease) in deposits, net	$16,358	$(1,033)	$(2,168)
Increase in mortgagors' escrow accounts	35	62	42
Proceeds from stock options exercised	8	122	97
Cash dividends paid on common stock	(310)	(154)	—
Proceeds from Federal Home Loan Bank advances with maturities of 3 months or more	50,500	7,000	—
Repayment of Federal Home Loan Bank advances with maturities of 3 months or more	(47,500)	(3,000)	—
Net cash provided by (used in) financing activities	19,091	2,997	(2,029)
Net increase (decrease) in cash and cash equivalents	6,678	(981)	1,439
Cash and cash equivalents at beginning of year	3,908	4,889	3,450
Cash and cash equivalents at end of year	$10,586	$ 3,908	$ 4,889
Supplementary information:			
Interest paid on deposit accounts	$ 4,499	$ 3,509	$ 4,010
Interest paid on borrowed funds	1,225	768	683
Income taxes paid	72	51	—
Loans transferred to foreclosed real estate	—	913	3,331
Financed sales of foreclosed real estate	171	1,254	3,154
Foreclosed real estate transferred to loans	129	286	289
Real estate held for investment transferred to foreclosed real estate	—	—	2,426
Securities held to maturity transferred to available for sale	26,301	—	—

See accompanying notes to consolidated financial statements.

Notes to Consolidated Financial Statements

December 31, 1995, 1994 and 1993

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation and consolidation

The consolidated financial statements include the accounts of Hingham Institution for Savings ("Bank") and its wholly-owned subsidiaries, Hingham Securities Corporation and Hingham Motel Corporation. Hingham Securities Corporation holds title to investment securities and Hingham Motel Corporation is presently inactive. All intercompany accounts and transactions have been eliminated in consolidation. The accounting and reporting policies of the Bank conform to generally accepted accounting principles and prevailing practices within the banking industry.

Use of estimates

In preparing financial statements in conformity with generally accepted accounting principles, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the consolidated balance sheet and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for losses on loans, the valuation of real estate acquired in connection with foreclosures or in satisfaction of loans, and the valuation reserve against deferred tax assets.

Business

The Bank provides a variety of financial services to individuals and small businesses through its five offices in southeastern Massachusetts. Its primary deposit products are savings, checking and term certificate accounts and its primary lending products are residential and commercial mortgage loans.

Reclassification

Certain amounts have been reclassified in the 1994 and 1993 consolidated financial statements to conform to the 1995 presentation.

Cash and cash equivalents

Cash and cash equivalents include amounts due from banks and interest-bearing deposits.

Interest-bearing deposits

Interest-bearing deposits mature within ninety days and are carried at cost, which approximates fair value.

Investment securities

Effective December 31, 1993, the Bank adopted the provisions of Statement of Financial Accounting Standards ("SFAS") No. 115, "Accounting for Certain Investments in Debt and Equity Securities." Accordingly, investments in debt securities that management has the positive intent and ability to hold to maturity are classified as "held to maturity" and reflected at amortized cost. Investments not classified as "held to maturity" are classified as "available for sale" and reflected on the balance sheet at fair value, with unrealized gains and losses excluded from earnings and reported as a separate component of stockholders' equity. The cumulative effect of the change in accounting principle at December 31, 1993 was to increase stockholders' equity by $52,000. There was no effect on net income for the year ended December 31, 1993 relating to the adoption of SFAS No. 115.

Prior to December 31, 1993, marketable equity securities and securities held for sale were stated at the lower of aggregate cost or fair value. Net unrealized losses applicable to marketable equity securities were reflected as a charge to stockholders' equity while write-downs applicable to securities held for sale were reflected in operations, if applicable.

Purchased premiums and discounts are amortized to earnings by a method which approximates the interest method

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

over the terms of the investments. Declines in the value of investments that are deemed to be other than temporary are reflected in earnings when identified. Gains and losses on disposition of investments are computed by the specific identification method.

Loans

The Bank grants mortgage, commercial and consumer loans to customers. A substantial portion of the loan portfolio is represented by mortgage loans in the southeastern Massachusetts area. The ability of the Bank's debtors to honor their contracts is dependent upon the real estate, construction and general economic sectors.

Loans, as reported, have been reduced by unadvanced loan funds, net deferred loan fees and the allowance for loan losses.

Interest on loans is recognized on a simple interest basis and is not accrued on loans which are ninety days or more past due or for which collection is not assured. Interest income previously accrued on such loans is reversed against current period earnings. Interest income on all non-accrual loans is recognized only to the extent of interest payments received.

Net deferred loan fees are amortized as an adjustment of the related loan yields using the level-interest method.

Allowance for loan losses

The allowance for loan losses is established through a provision for loan losses charged to operations and is maintained at a level considered adequate to provide for reasonably foreseeable loan losses.

The provision and the level of the allowance are evaluated on a regular basis by management and are based upon management's periodic review of the collectibility of the loans in light of historical experience, known and inherent risks in the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral and prevailing economic conditions.

The allowance is an estimate and ultimate losses may vary from current estimates and future additions to the allowance may be necessary. As adjustments become necessary, they are reported in the results of operations for the periods in which they become known. Loan losses are charged against the allowance when management believes the collectibility of the loan balance is unlikely.

The Bank adopted SFAS No. 114, "Accounting by Creditors for Impairment of a Loan," on January 1, 1995. Under this Statement, a loan is considered impaired when, based on current information and events, it is probable that a creditor will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Impairment is measured on a loan-by-loan basis by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price, or the fair value of the collateral if the loan is collateral dependent. Substantially all of the Bank's loans which have been identified as impaired have been measured by the fair value of existing collateral.

The Statement is not applicable to large groups of smaller balance homogeneous loans that are collectively evaluated for impairment, and loans that are measured at fair value. Accordingly, the Bank has not applied SFAS No. 114 to its consumer loans which are collectively evaluated for impairment.

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

SFAS No. 114 also limits the classification of loans as in-substance foreclosures to situations where the creditor actually receives physical possession of the debtor's assets. Accordingly, upon adoption of SFAS No.114, the Bank transferred loans previously classified as in-substance foreclosures in the amount of $129,000 to its impaired loan portfolio.

The adoption of SFAS No. 114 had no effect on the Bank's assessment of the overall adequacy of the allowance for loan losses. The restatement of previously issued financial statements to conform with SFAS No. 114 is expressly prohibited.

Foreclosed real estate

Foreclosed real estate is held for sale and carried at the lower of cost or fair value less estimated costs to sell. Troubled loans are transferred to foreclosed real estate upon completion of formal foreclosure proceedings.

Real estate properties acquired through foreclosure are initially recorded at fair value at the date of foreclosure. Costs relating to development and improvement of property are capitalized, whereas costs relating to holding property are expensed. The portion of interest costs relating to development of real estate is capitalized.

Valuations are periodically performed by management and an allowance for losses is established through a charge to operations if the carrying value of a property exceeds its fair value less estimated costs to sell.

In prior years, the Bank classified certain loans meeting the in-substance foreclosure criteria as foreclosed real estate. Upon the adoption of SFAS No. 114, the Bank reclassified all in-substance foreclosed assets that were not in its possession to loans.

Banking premises and equipment

Land is carried at cost. Buildings and equipment are carried at cost, less accumulated depreciation computed on the straight-line method over the estimated useful lives of the assets.

It is general practice to charge the cost of maintenance and repairs to earnings when incurred; major expenditures for betterments are capitalized and depreciated.

Income taxes

Deferred tax assets and liabilities are reflected at currently enacted income tax rates applicable to the period in which the deferred tax assets or liabilities are expected to be realized or settled. As changes in tax laws or rates are enacted, deferred tax assets and liabilities are adjusted accordingly through the provision for income taxes. The Bank's allowance for loan losses for tax purposes that arose before 1987 remains a permanent difference without recognition of a deferred tax liability. However, the loan loss allowance maintained for financial reporting purposes is treated as a temporary difference with allowable recognition of a related deferred tax asset, if it is deemed realizable and allowable for regulatory capital purposes.

Retirement plan

The compensation cost of an employee's pension benefit is recognized on the net periodic pension cost method over the employee's approximate service period. The aggregate cost method is utilized for funding purposes.

Earnings per share

Earnings per share is computed based on the weighted average number of common and common equivalent shares outstanding during the year.

Stock options, when dilutive, are included as common stock equivalents using the treasury stock method.

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (concluded)

Recent accounting pronouncements

In March 1995, the Financial Accounting Standards Board ("FASB") issued SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed of." SFAS No. 121 requires that long-lived assets and certain identifiable intangibles be reviewed for impairment. If the carrying amount of the asset exceeds its fair value, an impairment loss shall be recognized. This Statement applies to financial statements for fiscal years beginning after December 15, 1995. Early adoption is permissible. It is anticipated that adoption of this accounting standard will not have a material impact on the Bank's consolidated financial statements.

In May 1995, the FASB issued SFAS No. 122, "Accounting for Mortgage Servicing Rights". SFAS No. 122 amends SFAS No. 65 to eliminate the accounting distinction between rights to service mortgage loans for others that are acquired through loan origination activities and those acquired through purchased transactions. A mortgage banking enterprise that acquires mortgage servicing rights through either the purchase or origination of mortgage loans and sells or securitizes those loans with servicing rights retained should allocate the total cost of the mortgage loans to the mortgage servicing rights and the loans based on their relative fair values. The Statement also requires that the capitalized mortgage servicing rights be evaluated for impairment based of the fair value of those rights.

This Statement applies prospectively in fiscal years beginning after December 15, 1995, to transactions in which a mortgage banking enterprise sells or securitizes mortgage loans with servicing rights retained and to impairment evaluations of all amounts capitalized as mortgage servicing rights, including those purchased before the adoption of this Statement. Earlier application is encouraged. Retroactive capitalization of mortgage servicing rights retained in transactions in which a mortgage banking enterprise originates mortgage loans and sells or securitizes those loans before the adoption of this Statement is prohibited.

In October 1995, the FASB issued SFAS No. 123, "Accounting for Stock-Based Compensation." This Statement encourages all entities to adopt a fair value based method of accounting for employee stock compensation plans, whereby compensation cost is measured at the grant date based on the value of the award and is recognized over the service period, which is usually the vesting period. However, it also allows an entity to continue to measure compensation cost for those plans using the intrinsic value based method of accounting prescribed by APB Opinion No. 25, "Accounting for Stock Issued to Employees," whereby compensation cost is the excess, if any, of the quoted market price of the stock at the grant date (or other measurement date) over the amount an employee must pay to acquire the stock. Entities electing to remain with the accounting in Opinion No. 25 must make pro forma disclosures of net income and earnings per share, as if the fair value based method of accounting had been applied.

Generally, stock options issued under the Bank's stock option plan have no intrinsic value at the grant date, and under Opinion No. 25 no compensation cost is recognized for them. The accounting requirements of this Statement are generally effective for transactions entered into in fiscal years that begin after December 15, 1995. The disclosure requirements of this Statement are generally effective for financial statements for fiscal years beginning after December 15, 1995. It is anticipated that the Bank will continue its current accounting treatment for stock options and make the pro forma disclosures required by this Statement.

2. CASH AND DUE FROM BANKS

The Bank is required to maintain cash reserve balances with the Federal Reserve Bank based upon a percentage of certain deposits. At December 31, 1995 and 1994, cash and due from banks included $275,000 and $257,000, respectively, to satisfy such reserve requirements.

3. INVESTMENT SECURITIES

The amortized cost and estimated fair value of investment securities, with gross unrealized gains and losses, follows:

	December 31, 1995			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(In Thousands)			
Securities Available for Sale				
U.S. Government and federal agency obligations	$ 8,714	$ 21	$ (27)	$ 8,708
Mortgage-backed - FHLMC	17,347	5	(161)	17,191
Mortgage-backed - FNMA	11,471	17	(90)	11,398
REMIC's - FNMA	1,897	—	(42)	1,855
Total securities available for sale	$ 39,429	$ 43	$ (320)	$ 39,152

	December 31, 1994			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(In Thousands)			
Securities Available for Sale				
U.S. Government and federal agency obligations	$ 8,582	$ —	$ (386)	$ 8,196
Mortgage-backed - FHLMC	1,773	—	(107)	1,666
Mortgage-backed - FNMA	2,527	—	(164)	2,363
REMIC's - FNMA	1,894	—	(253)	1,641
Total securities available for sale	$ 14,776	$ —	$ (910)	$ 13,866
Securities Held to Maturity				
U.S. Government and federal agency obligations	$ 5,043	$ —	$ (341)	$ 4,702
Mortgage-backed - FHLMC	13,426	2	(868)	12,560
Mortgage-backed - FNMA	10,595	—	(641)	9,954
Total securities held to maturity	$ 29,064	$ 2	$(1,850)	$ 27,216

INVESTMENT SECURITIES (concluded)

The amortized cost and estimated fair value of debt securities by contractual maturity at December 31, 1995 are shown below. Expected maturities will differ from contractual maturities because of prepayments and scheduled payments on mortgage-backed securities. Further, certain obligors have the right to call bonds and obligations without prepayment penalties.

	Available for Sale	
	Amortized Cost	Fair Value
	(In Thousands)	
Bonds and obligations:		
Over 1 year to 5 years	$ 5,182	$ 5,178
Over 5 years to 10 years	3,532	3,530
	8,714	8,708
Mortgage-backed securities:		
Within 1 year	958	959
Over 1 year to 5 years	15,790	15,665
Over 5 years to 10 years	1,925	1,914
Over 10 years	12,042	11,906
	30,715	30,444
Total debt securities	$ 39,429	$ 39,152

For the years ended December 31, 1995 and 1994, proceeds from the sale of securities available for sale amounted to $1,463,000 and $10,400,000, respectively. Gross realized gains of $0 and $10,000 and gross realized losses of $49,000 and $242,000 were realized during 1995 and 1994, respectively.

Proceeds from the sale of debt securities for the year ended December 31,1993 were $35,901,000. Gross gains of $633,000 and gross losses of $161,000 were realized during 1993.

In November 1995, the FASB issued guidance allowing a one-time reassessment of an entity's investment classifications during the period November 15, 1995 to December 31, 1995. As a result, the amortized cost of securities held to maturity that were transferred to securities available for sale on December 31, 1995 amounted to $26,301,000, and the related net unrealized loss amounted to $168,000.

4. LOANS

A summary of the balances of loans follows:

	December 31,	
	1995	1994
	(In Thousands)	
Mortgage loans:		
Residential	$ 63,895	$ 57,671
Commercial	43,734	33,763
Construction	7,030	6,404
Equity lines-of-credit	5,698	3,687
Second mortgages	279	249
	120,636	101,774
Less unadvanced loan funds	(1,593)	(1,755)
Total mortgage loans, net	119,043	100,019
Commercial loans:		
Secured	933	888
Unsecured	45	71
Total commercial loans	978	959
Consumer loans:		
Personal installment	934	934
Education	22	30
Revolving credit	65	81
Total consumer loans	1,021	1,045
Total loans	121,042	102,023
Less: Allowance for loan losses	(1,277)	(1,338)
Net deferred interest and loan fees	(293)	(287)
Loans, net	$119,472	$100,398

The Bank has sold mortgage loans in the secondary mortgage market and has retained the servicing responsibility and receives fees for the services provided. Loans sold and serviced for others amounted to $8,787,000, $10,087,000 and $10,896,000 at December 31, 1995, 1994 and 1993, respectively. All loans serviced for others were sold without recourse provisions and are not included in the accompanying consolidated balance sheets.

At December 31, 1995, the recorded investment in impaired loans (see Note 1) totaled $638,000, of which $495,000 related to loans with no valuation allowance and $143,000 related to loans with a corresponding valuation allowance of $58,000. No additional funds are committed to be advanced in connection with impaired loans.

For the year ended December 31, 1995, the average recorded investment in impaired loans amounted to $556,000. The Bank recognized $41,000 of interest income on impaired loans, during the period that they were impaired, on the cash basis.

Non-accrual loans totaled $638,000 and $505,000 at December 31, 1995 and 1994, respectively. Interest not accrued on such loans amounted to $14,000 and $9,000 at December 31, 1995 and 1994, respectively.

Notes to Consolidated Financial Statements

LOANS (concluded)

Restructured loans totaled $1,107,000 at December 31, 1994. Interest income that would have been recorded under the original terms of such loans and the interest income actually recognized for the years ended December 31, 1994 and 1993 are as follows:

	Years Ended December 31, 1994	1993
	(In Thousands)	
Interest income that would have been recorded	$101	$193
Interest income recognized	83	152
Interest income foregone	$ 18	$ 41

An analysis of the allowance for loan losses follows:

	Years Ended December 31, 1995	1994	1993
		(In Thousands)	
Balance at beginning of year	$1,338	$1,191	$1,501
Provision for loan losses	120	120	63
	1,458	1,311	1,564
Loans charged-off	(188)	(105)	(411)
Recoveries on loans previously charged-off	7	132	38
Balance at end of year	$1,277	$1,338	$1,191

5. FORECLOSED REAL ESTATE

Foreclosed real estate is comprised of the following:

	December 31, 1995	1994
	(In Thousands)	
Residential homes	$ —	$147
Land	100	190
Commercial real estate	—	179
	100	516
Less allowance for losses	(66)	(77)
	$ 34	$439

Notes to Consolidated Financial Statements

FORECLOSED REAL ESTATE (concluded)

An analysis of the allowance for losses is as follows:

	Years Ended December 31, 1995	1994	1993
		(In Thousands)	
Balance at beginning of year	$ 77	$ 51	$ 534
Provision for losses	20	142	391
Write-downs and losses, net	(31)	(116)	(874)
Balance at end of year	$ 66	$ 77	$ 51

An analysis of foreclosed and other real estate expense is as follows:

	Years Ended December 31, 1995	1994	1993
		(In Thousands)	
Provision for losses	$ 20	$ 142	$ 391
Recoveries, net	(4)	(63)	(20)
Foreclosure and holding costs, net	(1)	186	391
Real estate held for investment expenses	—	—	291
	$ 15	$ 265	$1,053

Real estate held for investment expenses relate to properties acquired by foreclosure or deed-in-lieu of foreclosure which were operated by the Bank for income-producing purposes and include depreciation expense for the year ended December 31, 1993 amounting to $13,000. During 1993, all real estate held for investment was transferred to foreclosed real estate.

6. BANKING PREMISES AND EQUIPMENT

A summary of the cost and accumulated depreciation of banking premises and equipment and their estimated useful lives follows:

	December 31, 1995	December 31, 1994	Estimated Useful Lives
	(In Thousands)		
Banking premises:			
Land	$ 548	$ 428	
Buildings	2,129	1,673	3 - 65 years
Equipment	1,203	849	3 - 25 years
	3,880	2,950	
Less accumulated depreciation	(1,384)	(1,251)	
	$2,496	$1,699	

Depreciation expense for the years ended December 31, 1995, 1994 and 1993 amounted to $133,000, $115,000 and $126,000, respectively.

7. DEPOSITS

A summary of deposit balances, by type, is as follows:

	December 31, 1995	December 31, 1994
	(In Thousands)	
Non-certificate accounts:		
Regular	$ 31,119	$ 32,888
Money market deposits	19,421	23,934
NOW	12,026	10,584
Demand	6,613	6,687
Total non-certificate accounts	69,179	74,093
Term certificates less than $100,000	50,422	34,679
Term certificates $100,000 or more	13,441	7,912
Total certificate accounts	63,863	42,591
Total deposits	$133,042	$116,684

DEPOSITS (concluded)

The maturity distribution of term certificates is as follows:

	December 31, 1995		December 31, 1994	
	Amount	Weighted Average Rate	Amount	Weighted Average Rate
	(Dollars in Thousands)			
Within 1 year	$45,271	5.79%	$27,199	4.51%
Over 1 year to 2 years	7,253	5.86	9,220	5.11
Over 2 years to 3 years	3,457	6.32	1,693	4.99
Over 3 years to 5 years	7,882	6.37	4,479	5.72
	$63,863	5.90%	$42,591	4.78%

A summary of interest expense on deposits is as follows:

	Years Ended December 31, 1995	1994	1993
		(In Thousands)	
Regular	$ 775	$ 929	$1,062
Money market deposits	603	795	1,065
NOW	157	171	246
Term certificates	3,104	1,630	1,548
	$4,639	$3,525	$3,921

8. FEDERAL HOME LOAN BANK ADVANCES

A summary of advances from the Federal Home Loan Bank of Boston follows:

		December 31, 1995		December 31, 1994	
Maturity Date	Rate	Amount	Interest Rate	Amount	Interest Rate
		(Dollars in Thousands)			
February 28, 1995	Fixed	$ —	—%	$ 2,000	6.17%
February 1, 1996	Fixed	2,000	6.18	2,000	6.18
February 20, 1996	Fixed	3,500	5.84	—	—
March 25, 1996	Fixed	2,500	5.62	—	—
April 25, 1996	Variable	—	—	5,000	5.09
September 20, 1996	Fixed	3,000	6.53	3,000	6.53
February 18, 1997	Variable	—	—	7,000	4.25
November 17, 1997	Fixed	3,500	5.78	—	—
December 26, 1997	Fixed	2,500	5.59	—	—
July 15, 1998	Fixed	5,000	6.03	—	—
		$22,000	5.94%	$19,000	5.24%

All borrowings from the Federal Home Loan Bank of Boston are secured by stock in the Federal Home Loan Bank of Boston and a blanket lien on "qualified collateral" defined principally as 95% of the fair value of certain U.S. Government and federal agency obligations and 75% of the carrying values of certain residential mortgage loans.

The Bank also has an available line of credit with the Federal Home Loan Bank of Boston at an interest rate that adjusts daily. Borrowings under this line are limited to $2,605,000.

9. INCOME TAXES

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

	Years Ended December 31, 1995	1994 (In Thousands)	1993
Current tax provision:			
Federal	$ 868	$ 18	$ —
State	310	27	3
Utilization of operating loss carryforwards	(382)	—	—
	796	45	3
Deferred tax provision:			
Federal	397	452	—
State	41	139	—
	438	591	—
Change in valuation reserve realization assumptions	(189)	(891)	(472)
	$1,045	$(255)	$(469)

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

	Years Ended December 31, 1995	1994	1993
Statutory rates	34.0%	34.0%	(34.0)%
Increase (decrease) resulting from:			
State taxes, net of federal tax benefit	7.8	.6	(62.9)
Change in valuation allowance	(6.4)	(46.5)	(82.8)
Other, net	—	.8	12.2
Effective tax rates	35.4%	(11.1)%	(167.5)%

INCOME TAXES (continued)

The components of the net deferred tax asset are as follows:

	December 31, 1995	1994
	(In Thousands)	
Deferred tax asset:		
Federal	$ 870	$1,344
State	393	485
	1,263	1,829
Valuation reserve on asset	(65)	(254)
	1,198	1,575
Deferred tax liability:		
Federal	(118)	(18)
State	(35)	—
	(153)	(18)
Net deferred tax asset	$1,045	$1,557

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

	December 31, 1995	1994
	(In Thousands)	
Loan loss reserve	$ 522	$ 591
Compensation expense	222	170
Federal tax net operating loss carryforwards	—	382
Other tax carryforwards	65	105
Net unrealized loss on securities available for sale	122	385
Other	179	178
	1,110	1,811
Valuation reserve	(65)	(254)
Net deferred tax asset	$1,045	$1,557

A summary of the change in the net deferred tax asset is as follows:

	Years Ended December 31, 1995	1994 (In Thousands)	1993
Balance at beginning of year	$1,557	$ 872	$ 400
Deferred tax (provision) benefit	(249)	300	472
Net unrealized loss on securities available for sale	(263)	385	—
Balance at end of year	$1,045	$1,557	$ 872

INCOME TAXES (concluded)

A summary of the change in the valuation reserve applicable to the net deferred tax asset is as follows:

	Years Ended December 31,		
	1995	1994	1993
		(In Thousands)	
Balance at beginning of year	$ 254	$1,145	$1,525
Benefit created on current years' operations	—	—	92
Change in assumptions due to anticipation of future income	(189)	(891)	(472)
Balance at end of year	$ 65	$ 254	$1,145

10. COMMITMENTS AND CONTINGENCIES

In the normal course of business, there are outstanding commitments and contingencies which are not reflected in the consolidated financial statements.

Loan commitments

The Bank is a party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include unused lines-of-credit, commitments to originate loans, and standby letters of credit. The instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the consolidated balance sheets.

The Bank's exposure to credit loss in the event of non-performance by the other party to its financial instruments is represented by the contractual amount of these commitments. The Bank uses the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments.

COMMITMENTS AND CONTINGENCIES (concluded)

At December 31, 1995 and 1994, the following financial instruments were outstanding whose contract amounts represent credit risk:

	Contract Amount	
	1995	1994
	(In Thousands)	
Unused lines-of-credit	$6,019	$3,146
Commitments to originate loans:		
Commercial Mortgages	3,330	2,728
Residential Mortgages	1,133	1,172
Standby letters of credit	—	125

Commitments to extend credit are agreements to lend to a customer provided there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments may expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Bank evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Bank upon extension of credit, is based on management's credit evaluation of the borrower. The commitments to originate loans and the majority of unused lines-of-credit are secured by real estate.

Standby letters of credit are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loans to customers.

Employment agreements

The Bank has entered into employment agreements with certain senior executives. The agreements generally provide for certain lump sum severance payments within a two-year period following a "change in control" as defined in the agreements.

11. LITIGATION

In February 1993, Robert H. Gaughen, a shareholder and Director of the Bank, notified the Bank of his intention to nominate an independent slate of nominees for the Board of Directors. Subsequent to this notification, the Board of Directors by an 8 to 7 vote, initiated litigation against Mr. Gaughen and three other Directors and substantial shareholders, which litigation sought to prevent the solicitation of proxies in support of the independent slate of nominees. Mr. Gaughen then initiated suit against existing management of the Bank and the majority of the Board of Directors alleging breach of fiduciary responsibility and other irregularities with regard to prior management's conduct of the affairs of the Bank. After a hearing in the United States District Court of Massachusetts, the Bank's request for injunctive relief preventing Mr. Gaughen's solicitation of proxies was denied by United States District Court Judge Edward Harrington. Subsequent to prior management's failure to obtain such an order, the foregoing litigation was concluded by the exchange of mutual releases and the agreement to allow shareholders to vote at the annual meeting.

The Bank contends that a substantial amount of the cumulative loan losses it has sustained resulted from former president Wilfred H. Creighton's alleged conduct. In February 1993, the Bank reached a settlement agreement with its insurance carrier in the amount of $515,000 to compensate the Bank for its losses suffered by the former president's con-

LITIGATION (concluded)

duct. The settlement allowed the Bank to maintain its lawsuit against its former president without competition from the insurance carrier to recover the amount paid under the claim. This recovery is reflected in the Statement of Income in 1993. In February of 1994, the Bank obtained four parcels of developed real estate from the former president as settlement of its lawsuit. This recovery of $282,000 is reflected in the Statement of Income in 1994.

Various legal claims also arise from time to time in the normal course of business, which, in the opinion of management, will have no material effect on the Bank's consolidated financial position.

12. STOCKHOLDERS' EQUITY

Minimum regulatory requirements

Federal banking regulators require that the Bank (on a consolidated basis) meet certain Tier 1 leverage capital and risk-based capital ratio requirements. Generally, all but the most financially sound institutions are required to maintain a minimum Tier 1 leverage capital ratio of not less than 4% and a risk-based capital ratio of not less than 8%. The Bank exceeded all minimum regulatory requirements at December 31, 1995 and 1994.

Tax reserve for loan losses

At December 31, 1995, the total reserve for loan losses for federal income tax purposes at the Bank's base year amounted to approximately $3,780,000. If any portion of the reserve is used for purposes other than to absorb the losses for which established, approximately 150% of the amount actually used (limited to the amount of the reserve) must be included in gross income for federal income tax purposes in the fiscal year in which used. As the Bank does not intend to use the reserves for purposes other than to absorb loan losses, a deferred income tax liability of approximately $1,550,000 has not been provided. (See Note 1)

Liquidation account

At the time of conversion from mutual to stock form, the Bank established a liquidation account for the benefit of eligible account holders. The liquidation account is reduced annually to the extent that eligible account holders reduce their qualifying deposit. In the event of a complete liquidation, eligible account holders will be entitled to receive a distribution from the liquidation account to the extent that funds are available. According to the Bank's transfer agent, the balance of the liquidation account at December 31, 1995 amounted to $1,151,000 (unaudited).

13. STOCK OPTION PLAN

Under the Bank's 1988 stock option plan, options may be granted to officers, other employees and certain directors as the Stock Option Committee of the Board may determine. A total of 125,000 shares of common stock were reserved for issuance pursuant to options granted under the plan. Both "incentive options" and "non-qualified options" may be granted under the plan. All options under the plan will have an exercise price per share equal to, or in excess of, the fair market value of a share of common stock at the date the option is granted and will have a maximum option term of 10 years. Non-qualified stock options granted during 1995 and 1993 are immediately exercisable and options granted prior to 1993 vest over a five-year period.

Stock option activity is as follows:

	Years Ended December 31,		
	1995	1994	1993
Shares under option:			
Outstanding at beginning of year	44,500	63,080	87,500
Granted	28,000	—	39,000
Forfeited	—	(2,920)	(39,080)
Exercised	(2,000)	(15,660)	(24,340)
Outstanding at end of year	70,500	44,500	63,080
Weighted average price of options exercised	$ 4.00	$ 7.79	$ 4.00
Exercisable at end of year	70,500	41,500	56,088

Options outstanding consist of the following:

	December 31,	
Option price	1995	1994
$12.750	28,000	—
8.875	39,000	39,000
4.000	3,500	5,500
	70,500	44,500

Notes to Consolidated Financial Statements

14. PENSION PLAN

The Bank provides pension benefits for all of its eligible officers and employees through membership in a defined benefit plan of the Savings Banks Employees Retirement Association ("SBERA"). Under the plan, retirement benefits are based on years of credited service, the highest average compensation (as defined), and the primary social security benefit. In addition, employees may make optional, voluntary contributions to the plan under several methods. The optional contributions provide retirement benefits to the employee in addition to those otherwise available under the Bank's plan. Annual contributions by the Bank are based on assessments from SBERA.

Net periodic pension cost is as follows:

	Plan Years Ended October 31,		
	1995	1994	1993
		(In Thousands)	
Service cost - benefits earned during year	$ 82	$ 81	$118
Interest cost on projected benefits	87	85	100
Actual return on plan assets	(221)	(71)	(185)
Net amortization and deferral	3	3	3
Amortization of net (gain) loss	99	(36)	86
Net periodic pension cost	$ 50	$ 62	$122

Pension expense shown in the accompanying financial statements for the years ended December 31, 1995, 1994 and 1993 amounted to $54,000, $51,000, and $445,000 respectively. The 1993 amount included $310,000 of unrecognized pension costs applicable to previous years.

According to SBERA, a reconciliation of the funded status of the plan is as follows:

	October 31,	
	1995	1994
	(In Thousands)	
Plan assets at fair value	$1,389	$1,176
Actuarial present value of projected benefit obligation	1,352	1,089
Plan assets greater than projected benefit obligation	37	87
Unamortized net obligation since adoption of SFAS No. 87	32	35
Unrecognized net gain	(586)	(593)
Pension liability	$ (517)	$ (471)

The accumulated benefit obligation (substantially all vested) at October 31, 1995 amounted to $1,007,000.

For the plan years ended October 31, 1995, 1994 and 1993, actuarial assumptions include an assumed discount rate on benefit obligations of 7.00%, 8.00% and 7.00%, respectively, and an expected long-term rate of return on plan assets of 8.00%, 7.00% and 7.00%, respectively. An annual salary increase of 6.00% was utilized for all years.

Notes to Consolidated Financial Statements

15. RELATED PARTY TRANSACTIONS

In the ordinary course of business, the Bank has granted loans to principal officers and directors and their affiliates amounting to $23,000 at December 31, 1995 and $24,000 at December 31, 1994. In 1993, the Bank established a policy whereby new loans (excluding passbook loans) cannot be granted to employees, officers or directors.

16. FAIR VALUE OF FINANCIAL INSTRUMENTS

SFAS No. 107, "Disclosures about Fair Value of Financial Instruments" requires disclosure of estimated fair values of all financial instruments where it is practicable to estimate such values. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. Accordingly, the derived fair value estimates cannot be substantiated by comparison to independent markets and, in many cases, could not be realized in immediate settlement of the instrument. Statement No. 107 excludes certain financial instruments and all nonfinancial instruments from its disclosure requirements. Accordingly, the aggregate fair value amounts presented do not represent the underlying value of the Bank.

The following methods and assumptions were used by the Bank in estimating fair value disclosures for financial instruments:

Cash and cash equivalents: The carrying amounts of cash, due from banks and interest-bearing deposits approximate fair values.

Investment securities: Fair values for investment securities are based on quoted market prices.

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

Federal Home Loan Bank stock: The carrying value of Federal Home Loan Bank stock is deemed to approximate fair value.

Deposits: The fair values of non-certificate accounts are, by definition, equal to the amount payable on demand at the reporting date which is their carrying amount. Fair values for certificates of deposit are estimated using a discounted cash flow calculation that applies interest rates currently being offered on certificates to a schedule of aggregated expected monthly maturities on time deposits.

Federal Home Loan Bank advances: The fair values of the Bank's borrowings are estimated using discounted cash flow analyses based on the Bank's current incremental borrowing rates for similar types of borrowing arrangements.

Accrued interest: The carrying amounts of accrued interest approximate fair value.

Off-balance-sheet instruments: Fair values for off-balance-sheet lending commitments are based on fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the counterparties' credit standing. At December 31, 1995, the fair value of commitments outstanding are not significant since fees charged are not material.

FAIR VALUE OF FINANCIAL INSTRUMENTS (concluded)

The estimated fair values, and related carrying amounts, of the Bank's financial instruments are as follows:

	December 31, 1995 Carrying Amount	Fair Value
	(In Thousands)	
Financial assets:		
Cash and cash equivalents	$ 10,586	$ 10,586
Securities available for sale	39,152	39,152
Loans, net	119,472	121,160
Accrued interest receivable	1,048	1,048
Federal Home Loan Bank stock	1,200	1,200
Financial liabilities:		
Deposits	133,042	133,368
Federal Home Loan Bank advances	22,000	22,048
Accrued interest payable	505	505

17. REGULATORY MATTERS

In March of 1992, the Bank entered into a Memorandum of Understanding ("Memorandum") with the FDIC and the Massachusetts Commissioner of Banks. Based on the December 27, 1994 Regulatory Report of Examination, the Bank was found to be in general compliance with the provisions contained in the Memorandum and material improvement in the Bank's financial condition was noted. As a result, the Commissioner of Banks and the FDIC removed the Memorandum effective May 8, 1995.

18. QUARTERLY FINANCIAL DATA (UNAUDITED)

Quarterly results of operations for the years ended December 31, 1995 and 1994 are as follows:

	Years Ended December 31, 1995 Fourth Quarter	Third Quarter	Second Quarter	First Quarter	1994 Fourth Quarter	Third Quarter	Second Quarter	First Quarter
	(In Thousands, Except Per Share Data)							
Interest and dividend income	$3,247	$3,048	$2,968	$2,811	$2,696	$2,566	$2,442	$2,259
Interest expense	1,653	1,527	1,454	1,237	1,131	1,081	1,073	1,039
Net interest income	1,594	1,521	1,514	1,574	1,565	1,485	1,369	1,220
Provision for loan losses	30	30	30	30	30	10	50	30
Net interest income, after provision for loan losses	1,564	1,491	1,484	1,544	1,535	1,475	1,319	1,190
Other income	162	129	138	80	23	95	103	421
Operating expenses	946	840	929	926	931	968	953	1,008
Income before income taxes	780	780	693	698	627	602	469	603
Income tax provision (benefit)	294	280	230	241	(29)	(46)	(90)	(90)
Net income	$ 486	$ 500	$ 463	$ 457	$ 656	$ 648	$ 559	$ 693
Earnings per common share	$ .37	$ .39	$ .36	$ .35	$ .51	$ .50	$ .44	$ .54
Cash dividends declared per share	$ .16(1)	$ .07	$ .07	$ .05	$ .05	$ .04	$ .04	$ .04

(1) Includes a special dividend of $0.08 per share declared on December 21, 1995.

Stockholder Information

Hingham Institution for Savings
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Hingham, MA 02043
(617) 749-2200

President and Chief Executive Officer
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Vice President - Administration

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Form F-2
A copy of the Bank's Annual Report on Form F-2 for the fiscal year ended December 31, 1995 as filed with the Federal Deposit Insurance Corporation, may be obtained without charge, by any stockholder of the Bank upon written request addressed to the Investor Relations Department.

STOCK DATA

Hingham Institution for Savings common shares are listed and traded on the NASDAQ National Market System under the symbol HIFS.

As of December 31, 1995 there were approximately 563 stockholders of record, holding 703,963 outstanding shares of common stock. These shares do not include the number of persons who hold their shares in nominee or street name through various brokerage firms.

The following table presents the quarterly high and low bid prices for the Bank's common stock reported by NASDAQ.

	High	Low
1995		
First Quarter	$12	$ 9 1/2
Second Quarter	12	10 1/2
Third Quarter	12 3/4	10 3/4
Fourth Quarter	14 3/4	12 1/4
1994		
First Quarter	$10 1/2	$ 9 1/4
Second Quarter	11 3/4	8 7/8
Third Quarter	12	10 1/2
Fourth Quarter	11 1/4	9

The closing sale price of the Bank's common stock at December 31, 1995 was $14.75 per share.

HINGHAM
INSTITUTION
FOR SAVINGS
ESTABLISHED 1834

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55 Main Street, Hingham, Massachusetts 02043
(617) 749-2200