BERKSHIRE BANCORP INC /DE/
Form 10-K
March 30, 2005

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

FORM 10-K

[X] ANNUAL REPORT PURSUANT TO SECTION 13 or 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2004

OR

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

For the transition period from ---------------- to -----------------

Commission File Number 0-13649

Berkshire Bancorp Inc.
(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	94-2563513 (I.R.S. employer identification number)
160 Broadway, New York, New York (Address of principal executive offices)	10038 (Zip Code)

Registrant's telephone number, including area code: (212) 791-5362

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

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

Common Stock, par value $.10 per share
(Title of Class)

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

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

Indicate by check mark whether the Registrant is an accelerated filer (as defined in Rule 12b-2 of the Act. Yes [ ] No [X]

Aggregate market value of voting and non-voting common stock held by non-affiliates of the Registrant as of June 30, 2004: $57,816,584.

Number of shares of Common Stock outstanding as of March 24, 2005: 6,759,675.

DOCUMENTS INCORPORATED BY REFERENCE:

None

Forward-Looking Statements. Statements in this Annual Report on Form 10-K that are not based on historical fact may be "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. Words such as "believe", "may", "will", "expect", "estimate", "anticipate", "continue" or similar terms identify forward-looking statements. A wide variety of factors could cause the Company's actual results and experiences to differ materially from the results expressed or implied by the Company's forward-looking statements. Some of the risks and uncertainties that may affect operations, performance, results of the Company's business, the interest rate sensitivity of its assets and liabilities, and the adequacy of its loan loss allowance, include, but are not limited to: (i) deterioration in local, regional, national or global economic conditions which could result, among other things, in an increase in loan delinquencies, a decrease in property values, or a change in the housing turnover rate; (ii) changes in market interest rates or changes in the speed at which market interest rates change; (iii) changes in laws and regulations affecting the financial services industry; (iv) changes in competition; (v) changes in consumer preferences, (vi) changes in banking technology; (vii) ability to maintain key members of management, (viii) possible disruptions in the Company's operations at its banking facilities, (ix) cost of compliance with new corporate governance requirements, and other factors referred to in the sections of this Annual Report entitled "Business" and "Management's Discussion and Analysis of Financial Condition and Results of Operations."

Certain information customarily disclosed by financial institutions, such as estimates of interest rate sensitivity and the adequacy of the loan loss allowance, are inherently forward-looking statements because, by their nature, they represent attempts to estimate what will occur in the future.

The Company cautions readers not to place undue reliance upon any forward-looking statement contained in this Annual Report. Forward-looking statements speak only as of the date they were made and the Company assumes no obligation to update or revise any such statements upon any change in applicable circumstances.

PART I

ITEM 1. Business

General. Berkshire Bancorp Inc., a Delaware corporation, is a bank holding company registered under the Bank Holding Company Act of 1956. As used in this Annual Report on Form 10-K, the term "Berkshire", the "Company" or "we" and similar pronouns shall mean Berkshire Bancorp Inc. and its consolidated

subsidiaries unless the context otherwise requires. Berkshire's principal activity is the ownership and management of our wholly-owned banking subsidiary, The Berkshire Bank (the "Bank"), a New York State chartered commercial bank.

We file annual, quarterly and current reports, proxy statements and other information with the Securities and Exchange Commission (the "SEC"). You may read and copy our reports or other filings made with the SEC at the SEC's Public Reference Room, located at 450 Fifth Street, N.W., Washington, DC 20549. You can also access information that we file electronically on the SEC's website at WWW.SEC.GOV.

We do not presently have a website. However, as soon as practicable after filing with or furnishing to the SEC, we will provide at no cost, paper or electronic copies of our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to those reports. Requests should be directed to:

Berkshire Bancorp Inc.
Investor Relations
160 Broadway
New York, NY 10038

Stock Split and Stock Dividend. At the Annual Meeting of Stockholders held on May 18, 2004, the Company's stockholders approved an amendment to the Company's Certificate of Incorporation effecting a one-for-ten reverse stock split of the Company's issued and outstanding Common Stock (the "Reverse Split"). Following the effectiveness of the Reverse Split, the Company's Board of Directors declared a thirty-for-one forward stock split in the form of a stock dividend in Common Stock (the "Stock Dividend) which became effective immediately. The Company paid approximately $463,000 to purchase fractional shares from stockholders as part of the Reverse Split. The Company's Common Stock began trading on May 19, 2004 giving effect to these transactions.

Trust Preferred Securities. As of May 18 2004, the Company established Berkshire Capital Trust I, a Delaware statutory trust, ("BCTI"). The Company owns all the common capital securities of BCTI. BCTI issued $15.0 million of preferred capital securities to investors in a private transaction and invested the proceeds, combined with the proceeds from the sale of BCTI's common capital securities, in the Company through the purchase of $15.464 million aggregate principal amount of Floating Rate Junior Subordinated Debentures (the "Debentures") issued by the Company. The Debentures, the sole assets of BCTI, mature on July 23, 2034 and bear interest at a floating rate, three month LIBOR plus 2.70%.

Business of the Bank - General. The Bank's principal business consists of gathering deposits from the general public and investing those deposits primarily in loans, debt obligations issued by the U.S. Government, its agencies, and business corporations, and mortgage-backed securities. The Bank currently operates from five deposit-taking offices in New York City and four deposit- taking offices in Orange and Sullivan Counties, New York. In July 1995, the Bank opened a branch in Brooklyn, in January 2001, the Bank opened a branch in downtown Manhattan and in March 2001, as a result of the merger with Goshen

Bank, the Bank acquired two branches in Goshen, NY, a branch in Harriman, NY and a branch in Bloomingburg, NY. These branches provide the Bank with customary retail banking offices. On March 22, 2001, the Company purchased a parcel of land and building located in mid-town Manhattan for a total purchase price of $3.49 million in cash. In January 2003, the Bank relocated its main office to and opened a branch at this mid-town Manhattan location. The Bank opened two additional branches in Brooklyn, New York during 2003.

The Bank's principal loan types are residential and commercial mortgage loans and commercial non-mortgage loans, both unsecured and secured by personal property. The Bank's revenues come principally from interest on loans and investment securities. The Bank's primary sources of funds are deposits and proceeds from principal and interest payments on loans and investment securities.

Operating Plan. The Bank's operating plan concentrates on obtaining deposits from a variety of businesses, professionals and retail customers and investing those funds in conservatively underwritten loans. Due to the Bank's underwriting criteria, its deposits have significantly exceeded the level of satisfactory loans available for investment in recent years. Hence, the Bank has, in recent years, invested a portion of its available funds in investment and mortgage-backed securities.

Market Area. The Bank draws its customers principally from the New York City metropolitan area and, since the merger with Goshen Bank in 2001, the Villages of Goshen and Harriman, New York and their surrounding communities, representing most of Orange County, NY. The Bank also has a branch in Bloomingburg, New York, just over the border between Orange and Sullivan Counties. Predominantly rural with numerous small towns, many residents of Orange and Sullivan Counties work in New York City. Consequently, the health of the economy in the New York City metropolitan area has, and will continue to have a direct effect on the economic well being of residents and businesses in these counties. From time to time, the Bank may make loans or accept deposits from outside these areas, but such transactions generally represent outgrowths of existing local customer relationships.

Competition. The Bank's principal competitors for deposits are other commercial banks, savings banks, savings and loan associations and credit unions in the Bank's market areas, as well as money market mutual funds, insurance companies, securities brokerage firms and other financial institutions, many of

which are substantially larger in size than the Company. The Bank's competition for loans comes principally from commercial banks, savings banks, savings and loan associations, mortgage bankers, finance companies and other institutional lenders. Many of the institutions which compete with the Bank have much greater financial and marketing resources than the Bank. The Bank's principal methods of competition include loan and deposit pricing, maintaining close ties with its local communities, the quality of the personal service it provides, the types of business services it provides, and other marketing programs.

Operations of the Bank. Reference is made to the information set forth in Item 7 herein ("Management's Discussion and Analysis of Financial Condition and Results of Operations") for information as to various aspects of the Bank's operations, activities and conditions.

In March, 2001, pursuant to the terms of an Agreement and Plan of Reorganization dated August 16, 2000 (the "Agreement"), we completed the merger with GSB Financial Corporation, a Delaware corporation, a savings and loan holding company ("GSB Financial"), and its wholly-owned subsidiary, Goshen Savings Bank, a federal savings bank, chartered and existing under the laws of the United States ("Goshen Bank"). GSB Financial was merged with and into Berkshire and Goshen Bank was merged with and into The Berkshire Bank. Holders of the common stock of GSB Financial received $20.75 in cash for each share of common stock of GSB Financial held by them, or, in the alternative, at their election, 0.6027 shares of Berkshire's common stock. As a result of this transaction, 978,032 shares of GSB Financial common stock were converted into 589,460 shares of Berkshire common stock, and 974,338 shares of GSB Financial common stock were purchased for $20.75 per share, totaling approximately $20.2 million.

This transaction was accounted for under the purchase method of accounting. Goodwill of $7.5 million was recorded in the transaction. Effective January 1, 2002, we adopted Statement of Financial Accounting Standard No. 142, Goodwill and Intangible Assets which eliminates the amortization of goodwill and requires an annual impairment test. As of December 31, 2004, we have completed the impairment testing of our intangible assets, including goodwill. We did not identify any impairment on our outstanding goodwill.

On November 7, 2002, we sold our 24.9% interest in a merchant credit card processing company for $285,000, which was the initial purchase price we paid for our interest in December 1999. We accounted for our interest in this company under the equity method of accounting and have recorded approximately $200,000 in net losses since December 1999. The final installment payment of $25,000 was received during 2003.

Subsidiary Activities. The Bank is permitted under New York State law and federal law to own subsidiaries for certain limited purposes, generally to engage in activities which are permissible for a subsidiary of a national bank. The Bank has one subsidiary, Berkshire Agency, Inc., a company engaged in the title insurance agency business.

Regulation. Berkshire is a bank holding company under federal law and registered as such with the Federal Reserve. The Bank is a commercial bank chartered under the laws of New York State. It is subject to regulation at the state level by the New York Superintendent of Banks and the New York Banking Board, while at the federal level its primary regulator is the FDIC.

Both Berkshire and the Bank are subject to extensive state and federal regulation of their activities. The following discussion summarizes certain banking laws and regulations that affect Berkshire and the Bank. Proposals to change these laws and regulations are frequently proposed in Congress, in the New York State legislature, and before state and federal bank regulatory agencies. The likelihood and timing of any changes and the impact such changes might have on the Company are impossible to determine with any certainty. A change in applicable laws or regulations, or a change in the way such laws or regulations are interpreted by regulatory agencies or courts, may have a material impact on the business, operations and earnings of the Company, the nature and effect of which cannot be predicted.

Bank Holding Company Regulation. The Federal Reserve is authorized to make regular examinations of the Company and its nonbank subsidiaries. Under federal law and Federal Reserve regulations, the activities in which the Company and its nonbank subsidiaries may engage are limited. The Company may not acquire direct or indirect ownership or control of more than 5% of the voting shares of any company, including a bank, without the prior approval of the Federal Reserve, except as specifically authorized under federal law and Federal Reserve regulations. The Company, subject to the approval of the Federal Reserve, may acquire more than 5% of the voting shares of non-banking corporations if those corporations engage in activities which the Federal Reserve deems to be so closely related to banking or managing or controlling banks as to be a proper incident thereto. These limitations also apply to activities in which the Company engages directly rather than through a subsidiary.

The Federal Reserve has enforcement powers over the Company and its non-bank subsidiaries. This allows the Federal Reserve, among other things, to stop activities that represent unsafe or unsound practices or constitute violations of law, rules, regulations, administrative orders or written agreements with a federal bank regulator. These powers may be exercised through the issuance of cease-and-desist orders, the imposition of civil money penalties or other actions.

Federal Reserve Capital Requirements. The Federal Reserve requires that the Company, as a bank holding company, must maintain certain minimum ratios of capital to assets. The Federal Reserve's regulations divide capital into two categories. Primary capital includes common equity, surplus, undivided profits, perpetual preferred stock, mandatory convertible instruments, the allowance for loan and lease losses, contingency and other capital reserves, and minority interests in equity accounts of consolidated subsidiaries. Secondary capital includes limited-life preferred stock, subordinated notes and debentures and certain unsecured long term debt.

The Federal Reserve requires that bank holding companies maintain a minimum ratio of primary capital to total assets of 5.5% and a minimum level of total capital (primary plus secondary capital) equal to 6% of total assets. In calculating capital ratios, the allowance for loan losses, which is a component of primary capital, is added back in determining total assets. Certain capital components, such as debt and perpetual preferred stock, are includable as capital only if they satisfy certain definitional tests.

The Company must also meet a risk-based capital standard. Capital, for the risk-based capital requirement, is divided into Tier I capital and Supplementary capital, determined as discussed below in connection with the FDIC capital requirements imposed on the Bank. The Federal Reserve requires that the Bank maintain a ratio of total capital (defined as Tier I plus Supplementary capital) to risk-weighted assets of at least 8%, of which at least 4% must be Tier I capital. Risk weighted assets are also determined in a manner comparable to the determination of risk-weighted assets under FDIC regulations as discussed below.

At December 31, 2004 and 2003, the Company met the definition of a "well capitalized" bank holding company.

Inter-state Banking. Bank holding companies may generally acquire banks in any state. Federal law also permits a bank to merge with an out-of-state bank and convert any offices into branches of the resulting bank if both states have not opted out of interstate branching; permits a bank to acquire branches from an out-of-state bank if the law of the state where the branches are located

permits the interstate branch acquisition; and permits banks to establish and operate new interstate branches whenever the host state opts-in to that authority. Bank holding companies and banks that want to engage in such activities must be adequately capitalized and managed.

The New York Banking Law generally authorizes interstate branching in New York as a result of a merger, purchase of assets or similar transaction. An out of state bank may not first enter New York by opening a new branch in New York, but once a branch is acquired as described in the preceding sentence, additional new branches may be opened state wide.

Regulation of the Bank. In general, the powers of the Bank are limited to the express powers described in the New York Banking Law and powers incidental to the exercise of those express powers. The Bank is generally authorized to accept deposits and make loans on terms and conditions determined to be acceptable to the Bank. Loans may be unsecured, secured by real estate, or secured by personal property. The Bank may also invest assets in bonds, notes or other debt securities which are not in default and certain limited classes of equity securities including certain publicly traded equity securities in an amount aggregating not more than 2% of assets or 20% of capital. The Bank may also engage in a variety of other traditional activities for commercial banks, such as the issuance of letters of credit.

The exercise of these state-authorized powers is limited by FDIC regulations and other federal laws and regulations. In particular, FDIC regulations limit the investment activities of state-chartered, FDIC-insured banks such as the Bank.

Under FDIC regulations, the Bank generally may not directly or indirectly acquire or retain any equity investment that is not permissible for a national bank. In addition, the Bank may not directly or indirectly through a subsidiary, engage as "principal" in any activity that is not permissible for a national bank unless the FDIC has determined that such activities would pose no risk to the applicable FDIC insurance fund and the Bank is in compliance with applicable regulatory capital requirements. FDIC regulations permit real estate investments under certain circumstances. The Bank does not engage in real estate investing activity.

Loans to One Borrower. With certain exceptions, the Bank may not make loans or other extensions of credit to a single borrower, or certain related groups of borrowers, in an aggregate amount in excess of 15% of the Bank's net worth, plus an additional 10% of the Bank's net worth if such amount is secured by certain types of readily marketable collateral. In addition, the Bank is not permitted to make a mortgage loan in excess of 15% of capital stock, surplus fund and undivided profits.

FDIC Capital Requirements. The FDIC requires that the Bank maintain certain minimum ratios of capital to assets. The FDIC's regulations divide capital into two tiers. The first tier ("Tier I") includes common equity, retained earnings, certain non-cumulative perpetual preferred stock (excluding auction rate issues) and minority interests in equity accounts of consolidated subsidiaries, minus goodwill and other intangible assets (except mortgage

servicing rights and purchased credit card relationships subject to certain limitations). Supplementary ("Tier II") capital includes, among other items, cumulative perpetual and long-term limited-life preferred stock, mandatory convertible securities, certain hybrid capital instruments, term subordinated debt and the allowance for loan, subject to certain limitations, less required deductions.

The FDIC requires that the highest rated banks maintain a Tier I leverage ratio (Tier I capital to adjusted total assets) of at least 3.0%. All other banks subject to FDIC capital requirements must maintain a Tier I leverage ration of 4.0% to 5.0% or more. As of December 31, 2004 and 2003, the Bank's Tier I leverage capital ratio was 8.6% and 7.0%, respectively.

The Bank must also meet a risk-based capital standard. The risk-based standard requires the Bank to maintain total capital (defined as Tier I and Supplementary capital) to risk-weighted assets of at least 8%, of which at least 4% must be Tier I capital. In determining the amount of risk-weighted assets, all assets, plus certain off-balance sheet assets, are multiplied by a risk-weight of 0% to 100%, based on the risks the FDIC believes are inherent in the type of asset. As of December 31, 2004 and 2003, the Bank maintained a 23.3% and 18.3% Tier I risk-based capital ratio and a 24.1% and 19.1% total risk-based capital ratio, respectively.

In addition to the foregoing regulatory capital requirements, the FDIC Improvements Act of 1991 created a "prompt corrective action" framework, under which decreases in a depository institution's capital category trigger various supervisory actions. Pursuant to implementing regulations adopted by the FDIC, for purposes of the prompt corrective action provisions, a state-chartered,

nonmember bank, such as the Bank, is deemed to be well capitalized if it has: a total risk-based capital ratio of 10% or greater; a Tier I risk-based capital ratio of 6% or greater; and a leverage ratio of 5% or greater. As of December 31, 2004 and 2003, the Bank met the definition of a "well capitalized" financial institution.

Community Reinvestment Act. The Bank must, under federal law, meet the credit needs of its community, including low and moderate income segments of its community. The FDIC is required, in connection with its examination of the Bank, to assess whether the Bank has satisfied this requirement. Failure to satisfy this requirement could adversely affect certain applications which the Bank may make, such as branch applications, merger applications, and applications for permission to purchase branches. In the case of Berkshire, the Federal Reserve will assess the record of each subsidiary bank in considering certain applications by Berkshire. The New York Banking Law contains similar provisions applicable to the Bank. As of the most recent Community Reinvestment Act examinations by the FDIC and the New York State Banking Department, the Bank received "satisfactory" ratings.

Dividends From the Bank to the Company. One source of funds for Berkshire to pay dividends to its stockholders is dividends from the Bank to Berkshire. Under the New York Banking Law, the Bank may pay dividends to Berkshire, without regulatory approval, equal to its net profits for the year in which the payment is made, plus retained net profits for the two previous years,

subject to certain limits not generally relevant. The Bank's retained net profits for the 2003 and 2004 calendar years totaled approximately $14.38 million. However, the ability of Berkshire to pay future dividends and meet its other financial obligations is not presently dependent upon the receipt of dividends from the Bank.

Under federal law, the Bank may not make any capital distribution to Berkshire, including any dividend or repurchase of the Bank's stock, if, after making such distribution, the Bank fails to meet the required minimum capital ratio requirements discussed below. The FDIC may prohibit the Bank from paying dividends if, in its opinion, the payment of dividends would constitute an unsafe or unsound practice.

Transactions With Related Parties. The Company, its direct non-banking subsidiaries and other companies controlled by shareholders who control the Company are affiliates, within the meaning of the Federal Reserve Act, of the Bank and its subsidiaries. The Bank's authority to engage in transactions with its "affiliates" is limited by Sections 23A and 23B of the Federal Reserve Act. Section 23A limits the aggregate amount of transactions with any individual affiliate to 10% of the capital and surplus of the Bank and also limits the aggregate amount of transactions with all affiliates to 20% of the Bank's capital and surplus. Extensions of credit to affiliates must be secured by certain specified collateral, and the purchase of low quality assets from affiliates is generally prohibited. Section 23B provides that certain transactions with affiliates, including loans and asset purchases, must be on terms and under circumstances, including credit standards, that are at least as favorable to the Bank as those prevailing at the time for comparable transactions with non-affiliated companies. In the absence of comparable transactions, such transactions may only occur under terms and circumstances, including credit standards, that in good faith would be offered to or would apply to non-affiliated companies.

The Bank may make loans to its and the Company's directors, executive officers, and 10% stockholders, as well as to entities controlled by them, subject to specific federal and state limits. Among other things, these loans must (a) be made on terms that are substantially the same as, and follow credit underwriting procedures that are not less stringent than, those prevailing for comparable transactions with unaffiliated persons and that do not involve more than the normal risk of repayment or present other unfavorable features and (b) not exceed certain limitations on the amount of credit extended to such persons, individually and in the aggregate, which limits are based, in part, on the amount of the Bank's capital. In addition, extensions of credit in excess of certain limits must be approved by the Bank's Board of Directors. However, the Bank may make loans to executive officers, directors and principal stockholders on preferential terms, provided the extension of credit is made pursuant to a benefit or compensation program of the Bank that is widely available to employees

of the Bank or its affiliates and does not give preference to any insider over other employees of the Bank or affiliate. The Bank has no such benefit or compensation programs (see Item. 2 - Properties for additional information).

Enforcement. The FDIC and the Banking Department have enforcement

authority over the Bank. The Superintendent may order the Bank to appear and explain an apparent violation of law, to discontinue unauthorized or unsafe practices and to keep prescribed books and accounts. If any director or officer of the Bank has violated any law, or has continued unauthorized or unsafe practices in conducting the business of the Bank after having been notified by the Superintendent to discontinue such practices, the New York Banking Board may remove the individual from office after notice and an opportunity to be heard. The Superintendent also may take over control of the Bank under specified statutory criteria.

The FDIC's enforcement authority includes, among other things, the ability to assess civil money penalties, to issue cease and desist orders and to remove directors and officers. As indicated above, the FDIC is required to take prompt action to correct deficiencies in banks which do not satisfy specified FDIC capital ratio requirements. Dividends, other capital distributions or the payment of management fees to any controlling person are prohibited if, following such distribution or payment, a bank would be undercapitalized. An undercapitalized bank must file a plan to restore its capital within 45 days after being notified that it is undercapitalized. Undercapitalized, significantly undercapitalized and critically undercapitalized institutions are subject to increasing prohibitions on permitted activities, and increasing levels of regulatory supervision, based upon the severity of their capital problems. The FDIC is required to monitor closely the condition of an undercapitalized bank. Enforcement action taken by the FDIC can escalate to the appointment of a conservator or receiver of a critically undercapitalized bank.

Insurance of Accounts. Deposit insurance premiums payable to the FDIC are based upon the perceived risk of the institution to the FDIC insurance fund. The FDIC assigns an institution to one of three capital categories: (a) well capitalized, (b) adequately capitalized or (c) undercapitalized. The FDIC also assigns an institution to one of three supervisory categories based on an evaluation by the institution's primary federal regulator and information that the FDIC considers relevant to the institution's financial condition and the risk posed to the deposit insurance funds. Deposit insurance premiums depend on an institution's capital and supervisory categories. At present, the Bank pays no deposit insurance premium based upon its risk-based categorization.

However, the Bank must pay a share of the cost of the bonds issued in the late 1980s to recapitalize the now defunct Federal Savings and Loan Insurance Corporation. The Bank must pay an annual assessment for this purpose, which for fiscal 2004 and 2003 was equal to 0.0154% and 0.0168%, respectively, of its insured deposits and which is recorded as a deposit insurance premium expense for financial statement purposes. Beginning in 2005, the assessment was revised to 0.0444% of the Bank's insured deposits.

Reserve Requirements. The Bank must maintain non-interest-earning reserves against its transaction accounts (primarily NOW and regular checking accounts). The Bank is generally able to satisfy reserve requirements with cash on hand and other non-interest bearing deposits which it maintains for other purposes, so the reserve requirements do not impose a material financial burden on the Bank.

Governmental Policies. Our earnings are significantly affected by the monetary and fiscal policies of governmental authorities, including the Federal Reserve. Among the instruments of monetary policy used by the Federal Reserve to implement these objectives are open-market operations in U.S. Government securities and Federal funds, changes in the discount rate on member bank borrowings and changes in reserve requirements against member bank deposits. These instruments of monetary policy are used in varying combinations to influence the overall level of bank loans, investments and deposits, and the interest rates charged on loans and paid for deposits. The Federal Reserve frequently uses these instruments of monetary policy, especially its open-market

operations and the discount rate, to influence the level of interest rates and to affect the strength of the economy, the level of inflation or the price of the dollar in foreign exchange markets. The monetary policies of the Federal Reserve

have had a significant effect on the operating results of banking institutions in the past and are expected to continue to do so in the future. It is not possible to predict the nature of future changes in monetary and fiscal policies, or the effect which they may have on our business and earnings.

Personal Holding Company Status. For the fiscal years ended December 31, 2004, 2003 and 2002, the Company has been deemed to be a Personal Holding Company (a "PHC"), as defined in the Internal Revenue Code. As a PHC, we may be required to pay an additional income tax or issue a dividend to our shareholders in an amount based upon the PHC Internal Revenue Code formulas, which is primarily based upon net income. No such dividend was required to be paid in fiscal 2004, 2003 and 2002. (See Dividends in Item 5).

Employees. On March 24, 2005, Berkshire had one full time employee and the Bank employed approximately 100 full time and 6 part time employees. The Bank's employees are not represented by a collective bargaining unit, and the Bank considers its relationship with its employees to be good.

ITEM 2. Properties.

The following are Berkshire's and the Bank's principal facilities as of March 24, 2005:

Location	Operations	Approximate Floor Area (Sq. Ft.)	Approximate Annual Rent	Lease Expiratio
New York, NY	Executive Offices	1,500	$ 18,000	(1)(3)
New York, NY	Main Bank Office and Bank Branch	9,700	Owned	Feb 2008
Brooklyn, NY	Bank Branch	4,500	$ 167,100	March 200
Brooklyn, NY	Bank Branch	1,433	$ 35,925	March 200
Brooklyn, NY	Bank Branch	2,592	$ 105,060	December
New York, NY	Bank Branch	9,924	$ 275,000	June 2010
Goshen, NY	Bank Branch	10,680	Owned	
Harriman, NY	Bank Branch	1,623	Owned	
Bloomingburg, NY	Bank Branch	1,530	$ 20,360	June 2005

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(1) Rented on a month to month basis from a company affiliated with Mr. Moses Marx, a director of the Company.

(2) Leased from a company affiliated with Mr. Marx, a director of the Company.

(3) Management believes the annual rent paid is comparable to the annual rent that would be paid to non-affiliated parties in a similar commercial transaction for similar commercial space.

ITEM 3. Legal Proceedings.

In the ordinary course of operations, the Bank is a party to routine litigation involving claims incidental to its banking business. Management believes that no current litigation, threatened or pending, to which the Bank or its assets is a party, poses a substantial likelihood of potential loss or exposure which would have a material adverse effect on the financial condition or results of operations of the Bank.

ITEM 4. Submission of Matters to a Vote of Security Holders.

Not Applicable.

PART II

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

The Company's Common Stock trades on the Nasdaq National Market System under the symbol BERK. The following table sets forth, for the periods indicated, the high and low sales prices for the Company's Common Stock, restated to reflect the one-for-ten reverse stock split and thirty-for-one forward stock split which occurred on May 18, 2004, as reported by NASDAQ.

Fiscal Year Ended December 31, 2004	High	Low
January 1, 2004 to March 31, 2004	19.67	16.33
April 1, 2004 to June 30, 2004	19.33	15.00
July 1, 2004 to September 30, 2004	17.40	15.02
October 1, 2004 to December 31, 2004	20.50	16.10

Fiscal Year Ended December 31, 2003	High	Low
January 1, 2003 to March 31, 2003	11.48	10.62
April 1, 2003 to June 30, 2003	13.17	10.83
July 1, 2003 to September 30, 2003	14.83	11.67
October 1, 2003 to December 31, 2003	17.00	13.83

As of the close of business on March 24, 2005, there were approximately 1,740 holders of record of the Company's Common Stock.

Dividends

For the fiscal years ended December 31, 2004, 2003 and 2002, the Company has been deemed to be a PHC, as defined in the Internal Revenue Code. As

a PHC, we may be required to pay an additional income tax or issue a dividend to our shareholders in an amount based upon applicable Internal Revenue Code formulas, which is primarily based upon net income. No such dividend was required to be paid in fiscal 2004, 2003 and 2002.

On March 23, 1999, the Board of Directors adopted a policy of paying regular cash dividends in respect of the Common Stock of the Company, payable in equal semi-annual installments. Pursuant to said policy, the Board of Directors declared and the Company paid cash dividends, restated to reflect the one-for-ten reverse stock split and thirty-for-one forward stock split which occurred on May 18, 2004, as follows:

Declaration Date	Record Date	Payment Date
April 8, 2002	April 23, 2002	April 30, 2002
October 4, 2002	October 21, 2002	October 29, 2002
April 8, 2003	April 23, 2003	April 30, 2003
October 3, 2003	October 21, 2003	October 29, 2003
April 1, 2004	April 19, 2004	April 28, 2004
October 5, 2004	October 22, 2004	October 29, 2004

The declaration, payment and amount of such dividends in the future are within the discretion of the Board of Directors and will depend upon our earnings, capital requirements, financial condition and other relevant factors.

Equity Compensation Plans

See Part III, Item 12 for information concerning the Company's equity compensation plans.

ITEM 6. Selected Financial Data.

BERKSHIRE BANCORP INC. AND SUBSIDIARIES

Five Year Financial Highlights (a)(b)

The following is a summary of certain financial information with respect to the Company at and for the fiscal years ended December 31, 2004, 2003, 2002, 2001 and 2000. This information is derived from and should be read in conjunction with the Company's financial statements and notes thereto included elsewhere in this Form 10-K.

December 31,

	2004	2003	2002	2001	
	(Dollars in thousands,except per share data)				
Balance Sheet Data:					
Total Assets	$972,649	$905,669	$683,738	$536,365	$24
Loans, net	284,052	292,163	273,182	250,010	7
Investment securities	631,592	569,848	371,458	242,579	11
Goodwill, net	18,549	18,549	18,549	18,438	1
Deposits	619,888	604,255	473,818	338,776	13
Stockholders' equity	107,619	103,490	98,525	95,992	7
Statement of Operations Data:					
Interest income	40,008	34,426	32,242	24,941	1
Interest expense	15,916	13,647	13,416	11,877	
Net interest income before provision for loan losses	24,092	20,779	18,826	13,064	
Provision for loan losses	180	240	387	287	
Net interest income	23,912	20,539	18,439	12,777	
Investment securities gains	793	2,746	1,539	637	1
Other income	1,026	1,237	748	786	
Other expenses	12,095	11,463	10,780	7,838	
Amortization of goodwill	--	--	--	935	
Income before income taxes	13,636	13,059	9,946	5,427	1
Provision for income taxes	6,134	5,644	4,349	2,128	
Net income	$ 7,502	$ 7,415	$ 5,597	$ 3,299	$ 1
Net income per share:					
Basic	$ 1.12	$ 1.12	$ .81	$ .47	$
Diluted	$ 1.10	$ 1.10	$ .81	$ .47	$
Cash dividends per common share	$ .11	$ .09	$ .07	$ .08	$
Selected Operating Ratios					
Return on average assets	0.8%	0.9%	0.9%	0.8%	
Return on average equity	7.2%	7.2%	5.9%	3.5%	
Net interest margin	2.6%	2.7%	3.3%	3.6%	
Average equity/average assets	11.0%	12.7%	15.6%	23.8%	
Allowance for loan losses/total loans	1.0%	0.9%	0.8%	0.8%	

(a) The prior years' amounts have been reclassified to conform to the current years' presentation.

(b) The prior years' net income per share and cash dividends per common share amounts have been retroactively restated to reflect the one-for-ten reverse stock split and thirty-for-one forward stock split which occurred on May 18, 2004.

ITEM 7. Managements' Discussion and Analysis of Financial Condition and Results of Operations.

The following discussion and analysis is intended to provide a better understanding of the consolidated financial condition and results of operations of Berkshire Bancorp Inc. and subsidiaries for the fiscal years ended December 31, 2004, 2003 and 2002. All references to earnings per share, unless stated otherwise, refer to earnings per diluted share. References to per share amounts for the fiscal years ended December 31, 2003 and 2002 have been revised to reflect the one-for-ten reverse stock split and thirty-for-one forward stock split in the form of a 3000% stock dividend which occurred on May 18, 2004. The discussion should be read in conjunction with the consolidated financial statements and related notes (Notes located in Item 8 herein). Reference is also made to Part I, Item 1 "Business" herein.

Segments

Management has determined that the Company through its wholly owned bank subsidiary, the Bank, operates in one business segment, community banking. The Bank's principal business activity consists of gathering deposits from the general public and investing those deposits in residential and commercial mortgage loans and commercial non-mortgage loans, both unsecured and secured by personal property. In addition, the Bank invests those deposits in debt obligations issued by the U.S. Government, its agencies, business corporations and mortgage-backed securities.

General

Stock Split and Stock Dividend. At the Annual Meeting of Stockholders held on May 18, 2004, the Company's stockholders approved an amendment to the Company's Certificate of Incorporation effecting a one-for-ten reverse stock split of the Company's issued and outstanding Common Stock (the "Reverse Split"). Following the effectiveness of the Reverse Split, the Company's Board of Directors declared a thirty-for-one forward stock split in the form of a stock dividend in Common Stock (the "Stock Dividend) which became effective immediately. The Company paid approximately $463,000 to purchase fractional shares from stockholders as part of the Reverse Split. The Company's Common Stock began trading on May 19, 2004 giving effect to these transactions.

Trust Preferred Securities. As of May 18 2004, the Company established Berkshire Capital Trust I, a Delaware statutory trust, ("BCTI"). The Company owns all the common capital securities of BCTI. BCTI issued $15.0 million of preferred capital securities to investors in a private transaction and invested the proceeds, combined with the proceeds from the sale of BCTI's common capital securities, in the Company through the purchase of $15.464 million aggregate principal amount of Floating Rate Junior Subordinated Debentures (the "Debentures") issued by the Company. The Debentures, the sole assets of BCTI, mature on July 23, 2034 and bear interest at a floating rate, three month LIBOR plus 2.70%.

Critical Accounting Policies, Judgments and Estimates

The accounting and reporting policies of the Company conform with accounting principles generally accepted in the United States of America and general practices within the financial services industry. The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and the

assumptions that affect the amounts reported in the financial statements and the accompanying notes. Actual results could differ from those estimates.

The Company considers that the determination of the allowance for loan losses involves a higher degree of judgment and complexity than any of its other significant accounting policies. The allowance for loan losses is calculated with the objective of maintaining a reserve level believed by management to be sufficient to absorb estimated credit losses. Management's determination of the adequacy of the allowance is based on periodic evaluations of the loan portfolio and other relevant factors. However, this evaluation is inherently subjective as it requires material estimates, including, among others, expected default probabilities, loss given default, the amounts and timing of expected future cash

flows on impaired loans, mortgages, and general amounts for historical loss experience. The process also considers economic conditions, uncertainties in estimating losses and inherent risks in the loan portfolio. All of these factors may be susceptible to significant change. To the extent actual outcomes differ from management estimates, additional provisions for loan losses may be required that would adversely impact earnings in future periods.

With the adoption of Statement of Financial Accounting Standards ("SFAS") No. 142 ("SFAS No. 142") on January 1, 2002, the Company discontinued the amortization of goodwill resulting from acquisitions. Goodwill is now subject to impairment testing at least annually to determine whether write-downs of the recorded balances are necessary. The Company tests for impairment based on the goodwill maintained at each defined reporting unit. A fair value is determined for each reporting unit based on at least one of three various market valuation methodologies. If the fair values of the reporting units exceed their book values, no write-down of recorded goodwill is necessary. If the fair value of the reporting unit is less, an expense may be required on the Company's books to write down the related goodwill to the proper carrying value. As of December 31, 2004, the Company completed its annual impairment testing, which determined that no impairment write-offs were necessary.

The Company recognizes deferred tax assets and liabilities for the future tax effects of temporary differences, net operating loss carryforwards and tax credits. Deferred tax assets are subject to management's judgment based upon available evidence that future realization is more likely than not. If management determines that the Company may be unable to realize all or part of net deferred tax assets in the future, a direct charge to income tax expense may be required to reduce the recorded value of the net deferred tax asset to the expected realizable amount.

Discussion of Financial Condition and Results of Operations

Overview

Fiscal Year Ended December 31, 2004 Compared to Fiscal Year Ended December 31, 2003. Net income was $7.50 million, or $1.10 per diluted share, for the fiscal year ended December 31, 2004, compared to $7.42 million, or $1.10 per diluted share, for the fiscal year ended December 31, 2003, an increase of $87,000 or 1.17%. Investment securities and total assets increased by 10.84% and

7.40%, respectively, and loans decreased by 2.78%.

	Fiscal Year Ended December 31,		
	2004	2003	% Inc/(Dec)
	(In millions, except per share data)		
Total Assets	$972.6	$905.7	7%
Loans, net	284.1	292.2	(3)%
Investment Securities	631.6	569.8	11%
Total Liabilities	865.0	802.2	8%
Deposits	619.9	604.3	3%
Borrowings	238.8	192.1	24%
Stockholders' Equity	107.6	103.5	4%
Total Income	41.8	38.4	9%
Interest Income	40.0	34.4	16%
Total Expense	28.0	25.4	10%
Interest Expense	15.9	13.6	17%
Net Interest Income	24.1	20.8	16%
Net Income	7.5	7.4	1%
Diluted Income Per Share	1.10	1.10	0%
Bank Branches	9	9	-

Fiscal Year Ended December 31, 2003 Compared to Fiscal Year Ended December 31, 2002. Net income was $7.42 million, or $1.10 per diluted share, for the fiscal year ended December 31, 2003, compared to $5.60 million, or $.81 per diluted share, for the fiscal year ended December 31, 2002, an increase of 32.48%. Investment securities, loans and total assets increased by 53.38%, 6.95% and 32.46%, respectively. Two new branches were opened in Brooklyn, New York during 2003 making a total of nine bank branches in operation at years' end.

	Fiscal Year Ended December 31,		
	2003	2002	% Inc.
	(In millions, except per share data)		
Total Assets	$905.7	$683.7	32%
Loans, net	292.2	273.2	7%
Investment Securities	569.8	371.5	53%
Total Liabilities	802.2	585.2	37%
Deposits	604.3	473.8	28%
Borrowings	192.1	104.4	84%
Stockholders' Equity	103.5	98.5	5%
Total Income	38.4	34.5	11%
Interest Income	34.4	32.2	7%
Total Expense	25.4	24.6	3%
Interest Expense	13.6	13.4	1%
Net Interest Income	20.8	18.8	11%
Net Income	7.4	5.6	32%

Diluted Income Per Share	1.10	0.81	36%
Bank Branches	9	7	-

Net Interest Income

Net interest income, represents the difference between total interest income earned on earning assets and total interest expense paid on interest-bearing liabilities. The amount of interest income is dependent upon many factors including: (i) the amount of interest-earning assets that the Company can maintain based upon its funding sources; (ii) the relative amounts of interest-earning assets versus interest-bearing liabilities; and (iii) the difference between the yields earned on those assets and the rates paid on those liabilities. Non-performing loans adversely affect net interest income because they must still be funded by interest-bearing liabilities, but they do not provide interest income. Furthermore, when we designate an asset as non-performing, all interest which has been accrued but not actually received is deducted from current period income, further reducing net interest income.

The Company's average balances, interest, and average yields are set forth on the following table (in thousands, except percentages):

	Twelve Months Ended December 31, 2004			Tw D
	Average Balance	Interest and Dividends	Average Yield/Rate	Average Balance
INTEREST-EARNING ASSETS:				
Loans (1)	$ 290,774	$ 18,825	6.47%	$ 291,586
Investment securities	620,511	21,120	3.40	470,412
Other (2)(5)	4,376	63	1.44	3,946
Total interest-earning assets	915,661	40,008	4.37	765,944
Noninterest-earning assets	40,592			37,844
Total Assets	$ 956,253			$ 803,788
INTEREST-BEARING LIABILITIES:				
Interest bearing deposits	272,219	3,809	1.39	201,817
Time deposits	309,968	6,024	1.94	333,112
Other borrowings	223,208	6,083	2.73	125,609
Total interest-bearing liabilities	805,395	15,916	1.98	660,538

Demand deposits	38,896			32,592
Noninterest-bearing liabilities	7,163			8,318
Stockholders' equity (5)	104,799			102,340
Total liabilities and stockholders' equity	$ 956,253			$ 803,788
Net interest income		$ 24,092		
Interest-rate spread (3)			2.39%	
Net interest margin (4)			2.63%	
Ratio of average interest-earning assets to average interest bearing liabilities	1.14			1.16

	Twelve Months Ended December 31, 2002		
	Average Balance	Interest and Dividends	Average Yield/Rate
INTEREST-EARNING ASSETS:			
Loans (1)	$ 265,961	$ 18,723	7.04%
Investment securities	298,008	13,383	4.49
Other (2)(5)	8,479	136	1.60
Total interest-earning assets	572,448	32,242	5.63
Noninterest-earning assets	36,541		
Total Assets	$ 608,989		
INTEREST-BEARING LIABILITIES:			
Interest bearing deposits	116,331	1,644	1.41
Time deposits	273,452	8,766	3.21
Other borrowings	86,210	3,006	3.49
Total interest-bearing liabilities	475,993	13,416	2.82
Demand deposits	30,102		
Noninterest-bearing liabilities	7,586		
Stockholders' equity (5)	95,308		
Total liabilities and stockholders' equity	$ 608,989		

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Net interest income		$ 18,826	
		========	
Interest-rate spread (3)			2.81%
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Net interest margin (4)			3.29%
			====
Ratio of average interest-earning assets to average interest bearing liabilities	1.20		
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(1) Includes nonaccrual loans.
(2) Includes interest-bearing deposits, federal funds sold and securities purchased under agreements to resell.
(3) Interest-rate spread represents the difference between the average yield on interest-earning assets and the average cost of interest bearing liabilities.
(4) Net interest margin is net interest income as a percentage of average interest-earning assets.
(5) Average balances for Berkshire Bancorp Inc. (parent only) have been calculated on a monthly basis.

Changes in net interest income may also be analyzed by segregating the volume and rate components of interest income and interest expense. The following tables set forth certain information regarding changes in interest income and interest expense of the Company for the years indicated. For each category of interest- earning assets and interest-bearing liabilities, information is provided on changes attributable to (1) changes in rate (change in rate multiplied by prior volume), (2) changes in volume (changes in volume multiplied by prior rate) and (3) changes in rate-volume (change in rate multiplied by change in volume) (in thousands):

	Twelve Months Ended December 31, 2004 Versus Twelve Months Ended December 31, 2003 Increase (Decrease) Due To		
	Rate	Volume	Total
Interest-earning assets:			
Loans	$ (204)	$ (32)	$ (236)
Investment securities	659	5,140	5,799
Other	13	6	19
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Total	468	5,114	5,582
Interest-bearing liabilities:			
Deposit accounts:			
Interest bearing deposits	222	994	1,216
Time deposits	(1,066)	(447)	(1,513)
Other borrowings	(88)	2,654	2,566
Total	(932)	3,201	2,269
Net interest income	$ 1,400	$ 1,913	$ 3,313

	Twelve Months Ended December 31, 2003 Versus Twelve Months Ended December 31, 2002 Increase (Decrease) Due To		
	Rate	Volume	Total
Interest-earning assets:			
Loans	$(1,330)	$ 1,668	$ 338
Investment securities	(3,278)	5,216	1,938
Other	(41)	(51)	(92)
Total	(4,649)	6,833	2,184
Interest-bearing liabilities:			
Deposit accounts:			
Interest bearing deposits	(151)	1,100	949
Time deposits	(2,598)	1,369	(1,229)
Other borrowings	(595)	1,106	511
Total	(3,344)	3,575	231
Net interest income	$(1,305)	$ 3,891	$ 1,953

Interest Rate Risk

Fluctuations in market interest rates can have a material effect on the Company's net interest income because the yields earned on loans and investments may not adjust to market rates of interest with the same frequency, or with the same speed, as the rates paid by the Bank on its deposits.

Most of the Bank's deposits are either interest-bearing demand deposits or short term certificates of deposit and other interest-bearing deposits with interest rates that fluctuate as market rates change. Management of the Bank seeks to reduce the risk of interest rate fluctuations by concentrating on loans and securities investments with either short terms to maturity or with adjustable rates or other features that cause yields to adjust based upon interest rate fluctuations. In addition, to cushion itself against the potential adverse effects of a substantial and sustained increase in market interest rates, the Bank has purchased off balance sheet interest rate cap contracts which generally provide that the Bank will be entitled to receive payments from the other party to the contract if interest rates exceed specified levels. These contracts are entered into with major financial institutions.

We seek to maximize our net interest margin within an acceptable level of interest rate risk. Interest rate risk can be defined as the amount of the forecasted net interest income that may be gained or lost due to favorable or unfavorable movements in interest rates. Interest rate risk, or sensitivity, arises when the maturity or repricing characteristics of assets differ significantly from the maturity or repricing characteristics of liabilities.

Provision for Loan Losses

The Company maintains an allowance for loan losses at a level deemed sufficient to absorb losses, which are inherent in the loan portfolio at each balance sheet date. Management reviews the adequacy of the allowance on at least a quarterly basis to ensure that the provision for loan losses has been charged against earnings in an amount necessary to maintain the allowance at a level that is appropriate based on management's assessment of estimated losses. The Company's methodology for assessing the appropriateness of the allowance for loan losses consists of several key elements. These elements include a specific allowance for loan watch list classified loans, an allowance based on historical trends, an additional allowance for special circumstances, and an unallocated portion. The Company consistently applies the following comprehensive methodology.

The allowance for loan watch list classified loans addresses those loans maintained on the Company's loan watch list which are assigned a rating of substandard, doubtful, or loss. Substandard loans are those with a well-defined weakness or a weakness, which jeopardizes the repayment of the debt. A loan may be classified as substandard as a result of impairment of the borrower's financial condition and repayment capacity. Loans for which repayment plans have not been met or collateral equity margins do not protect the Company may also be classified as substandard. Doubtful loans have the characteristics of substandard loans with the added characteristic that collection or liquidation in full, on the basis of presently existing facts and conditions, is highly improbable. Although the possibility of loss is extremely high for doubtful loans, the classification of loss is deferred until pending factors, which might improve the loan, have been determined. Loans rated as doubtful in whole or in part are placed in nonaccrual status. Loans which are classified as loss are considered uncollectible and are charged to the allowance for loan losses. There were $343,000, $109,000 and $59,000 of classified loans at December 31, 2004, 2003 and 2002, respectively.

Loans on the loan watch list may also be impaired loans, which are defined as nonaccrual loans or troubled debt restructurings, which are not in compliance with their restructured terms. Each of the classified loans on the loan watch list is individually analyzed to determine the level of the potential loss in the loan under the current circumstances. The specific reserve established for these criticized and impaired loans is based on careful analysis of the loan's performance, the related collateral value, cash flow considerations and the financial capability of any guarantor. The allowance for loan watch list classified loans is equal to the total amount of potential

unconfirmed losses for

the individual classified loans on the watch list. Loan watch list loans are managed and monitored by assigned Senior Management.

The allowance based on historical trends uses charge-off experience of the Company to estimate potential unconfirmed losses in the balances of the loan and lease portfolios. The historical loss experience percentage is based on the charge-off history. Historical loss experience percentages are applied to all non-classified loans to obtain the portion of the allowance for loan losses which is based on historical trends. Before applying the historical loss experience percentages, loan balances are reduced by the portion of the loan balances which are subject to guarantee by a government agency. Loan balances are also adjusted for unearned discount on installment loans.

The Company also maintains an unallocated allowance. The unallocated allowance is used to cover any factors or conditions which may cause a potential loan loss but are not specifically identifiable. It is prudent to maintain an unallocated portion of the allowance because no matter how detailed an analysis of potential loan losses is performed these estimates by definition lack precision. Management must make estimates using assumptions and information, which is often subjective and changing rapidly.

Since all identified losses are immediately charged off, no portion of the allowance for loan losses is restricted to any individual loan or groups of loans, and the entire allowance is available to absorb any and all loan losses.

A loan is placed in a nonaccrual status at the time when ultimate collectibility of principal or interest, wholly or partially, is in doubt. Past due loans are those loans which were contractually past due 90 days or more as to interest or principal payments but are well secured and in the process of collection. Renegotiated loans are those loans which terms have been renegotiated to provide a reduction or deferral of principal or interest as a result of the deteriorating financial position of the borrower.

Results of Operations Fiscal Year Ended December 31, 2004 Compared to Fiscal Year Ended December 31, 2003.

General.

References to per share amounts below, unless stated otherwise, refer to diluted shares. References to per share amounts for the fiscal years ended December 31, 2003 have been revised to reflect the one-for-ten reverse stock split and thirty-for-one forward stock split in the form of a stock dividend which occurred on May 18, 2004.

Net Income. Net income for the fiscal year ended December 31, 2004 was $7.50 million, or $1.10 per share, as compared to $7.42 million, or $1.10 per share, for the fiscal year ended December 31, 2003.

The Company's net income is largely dependent on interest rate levels, the demand for the Company's loan and deposit products and the strategies employed to manage the interest rate and other risks inherent in the banking business. From June 2003 through June 30, 2004, interest rates, as measured by

the prime rate, remained constant at 4.00%. On July 1, 2004, inflation fighting actions taken by the Federal Reserve Board resulted in a 25 basis point increase in the prime rate to 4.25%, the first such increase in more than four years. Similar 25 basis point moves taken by the Federal Reserve Board in August, September, November and December of 2004, and February 2005 have moved the prime rate to its present level of 5.50%.

Net Interest Income. The Company's primary source of revenue is net interest income, or the difference between interest income on earning assets, such as loans and investment securities, and interest expense on interest-bearing liabilities such as deposits and borrowings.

For the fiscal year ended December 31, 2004, net interest income increased by $3.31 million, or 15.94%, to $24.09 million from $20.78 million for the fiscal year ended December 31, 2003. The increase in net interest income was the result of a 19.55% growth in the average amount of interest-earning assets to $915.66 million at the end of 2004 from $765.94 million at the end of 2003, partially

offset by the 21.93% growth in the average amount of interest-bearing liabilities to $805.40 million from $660.54 million at December 31, 2004 and 2003, respectively, as well as the interest-rate spread or the difference between the average yield on interest-earning assets and the average cost of interest-bearing liabilities.

During fiscal 2004, the average yield on interest-earning assets fell to 4.37% from 4.49% in fiscal 2003, a decline of 2.67%, while the average cost of interest-bearing liabilities fell to 1.98% from 2.07%, a decline of 4.35% The interest-rate spread decreased to 2.39% during fiscal 2004 from 2.42% during fiscal 2003.

If interest rates remain at current levels or increase slowly over time, we expect to see only moderate pressure on the Company's interest-rate spread and net interest income. Investment securities in our portfolio that have been sold, matured or called by the issuer during fiscal 2003 and 2004 have been replaced with securities carrying somewhat lower yields and, by design, shorter maturities to hedge against a rising interest rate environment. Rates paid on deposit accounts are likely to increase in a rising rate environment due to competition for deposits in the market place. The cost of borrowed funds with floating rather than fixed interest rates will increase as well.

Net Interest Margin. Net interest margin, or annualized net interest income as a percentage of average interest-earning assets, declined to 2.63% in fiscal 2004 from 2.71% in fiscal 2003. We seek to secure and retain customer deposits with competitive products and rates, while making strategic use of the prevailing interest rate environment to borrow funds at what we believe to be attractive rates. We invest such deposits and borrowed funds in a prudent mix of fixed rate and adjustable rate loans, investment securities and short-term interest-earning assets which provided an aggregate average yield of 4.37% and 4.49% in fiscal 2004 and 2003, respectively.

The average amount of loans decreased slightly to $290.77 million in fiscal 2004 from $291.59 million in fiscal 2003, as did the average yield on the

loan portfolio which declined to 6.47% in fiscal 2004 from 6.54% in fiscal 2003. During periods of low and stable interest rates, as was the case during 2003, borrowers gravitate towards fixed-rate loans to lock in a low interest rate, whereas adjustable rate loans are generally preferred when interest rates are trending higher. One-to-four family mortgage loans, approximately 54% and 57% of our loan portfolio at December 31, 2004 and 2003, respectively, are particularly sensitive to changes in interest rates.

The average amount of investment securities increased by $150.10 million to $620.51 million in fiscal 2004 from $470.41 million in fiscal 2003. The average yield on investment securities improved by 14 basis points, to 3.40% in 2004 from 3.26% in 2003 and are likely to continue to increase in a rising interest rate environment.

Interest Income. Total interest income for the fiscal year ended December 31, 2004 increased by $5.58 million, or 16.21%, to $40.01 million from $34.43 million for the fiscal year ended December 31, 2003. The increase in interest income was primarily due to the growth in the average amount of total interest-earning assets. Loans contributed $18.83 million of interest income in fiscal 2004, a decline of $236,000 from the $19.06 million of interest income contributed in fiscal 2003. Investment securities contributed $21.12 million of interest income in fiscal 2004, an increase of 37.85% over the $15.32 million of interest income earned on loans in fiscal 2003.

	Fiscal 2004		Fiscal 2003	
	Interest Income	% of Total	Interest Income	% of Total
	(In thousands, except percentages)			
Loans	$18,825	47.05%	$19,061	55.37%
Investment Securities	21,120	52.79	15,321	44.50
Other	63	0.16	44	0.13
Total Interest Income	$40,008	100.00%	$34,426	100.00%

Loans, which are inherently risky and therefore command a higher return than our conservative portfolio of investment securities, declined to 31.76% of our total average interest-earning assets in fiscal 2004 from 38.07% in fiscal 2003. While we actively seek to originate new loans with qualified borrowers who meet the Bank's underwriting standards, our strategy has been to maintain those standards, sacrificing some current income to avoid possible large future losses in the loan portfolio.

	Fiscal 2004		Fiscal 2003	
	Average Amount	% of Total	Average Amount	% of Total
	(In thousands, except percentages)			
Loans	$290,774	31.76%	$291,586	38.07%
Investment Securities	620,511	67.77	470,412	61.42

Other	4,376	0.47	3,946	0.51
Total Interest-Earning Assets	$915,661	100.00%	$765,944	100.00%

Interest Expense. Total interest expense for the fiscal year ended December 31, 2004 increased by $2.27 million, or 16.63%, to $15.92 million from $13.65 million for the fiscal year ended December 31, 2003. The increase in interest expense was due primarily to the growth in the average amount of interest-bearing liabilities, partially offset by the decline in the average rate paid on such liabilities, 1.98% and 2.07% in fiscal years 2004 and 2003, respectively. As rates move higher, interest expense will increase as we price our deposit products to meet the competition and the adjustable rates paid on other borrowings increase as well. In May 2004, we sold $15.46 million of floating rate junior subordinated debentures which mature in 2034 and used the net proceeds to augment the Bank's capital. The additional interest expense on these debentures, which are included in other borrowings, was $463,000 during fiscal 2004.

	Fiscal 2004		Fiscal 2003	
	Interest Income	% of Total	Interest Income	% of Total
	(In thousands, except percentages)			
Interest-Bearing Deposits	$ 3,809	23.93%	$ 2,593	19.00%
Time Deposits	6,024	37.85	7,537	55.23
Other Borrowings	6,083	38.22	3,517	25.77
Total Interest Expense	$15,916	100.00%	$13,647	100.00%

	Fiscal 2004		Fiscal 2003	
	Average Amount	% of Total	Average Amount	% of Total
	(In thousands, except percentages)			
Interest-Bearing Deposits	$272,219	33.80%	$201,817	30.55%
Time Deposits	309,968	38.49	333,112	50.43
Other Borrowings	223,208	27.71	125,609	19.02
Total Interest-Bearing Liabilities	$805,395	100.00%	$660,538	100.00%

Non-Interest Income. Non-interest income consists primarily of realized gains on sales of marketable securities and service fee income. For the fiscal year ended December 31, 2004, total non-interest income decrease by $2.16 million to $1.82 million from $3.98 million for the fiscal year ended December 31, 2003. In 2003, we recorded gains of $2.75 million on the sales and issuer redemptions of investment securities. In 2004, such gains amounted to $793,000. Service charges on deposit accounts decreased by $120,000 to $520,000 in fiscal 2004 from $640,000 in fiscal 2003. The decline is primarily due to marketing efforts introducing new deposit products, which includes the waiver of such fees for a period of time to attract new customers.

	Fiscal 2004		Fiscal 2003	
	Non-Interest Income	% of Total	Non-Interest Income	% of Total
	(In thousands, except percentages)			
Service Charges on Deposits	$ 520	28.59%	$ 640	16.07%
Investment Securities gains	793	43.60	2,746	68.94
Other	506	27.81	597	14.99
Total Non-Interest Income	$1,819	100.00%	$3,983	100.00%

Non-Interest Expense. Non-interest expense includes salaries and employee benefits, occupancy and equipment expenses, legal and professional fees and other operating expenses associated with the day-to-day operations of the Company. Total non-interest expense for the year ended December 31, 2004 increased by $632,000, or 5.51%, to $12.10 million from $11.46 million for the year ended December 31, 2003. The largest component of non-interest expense are salaries and employee benefits which increased by $1.01 million, or 17.25%, to $6.89 million in fiscal 2004 from $5.87 million in fiscal 2003. The increase is due to the additional staffing of our two new Brooklyn branches which opened in April and June of 2003 and the addition of personnel in our internal control and compliance departments.

	Fiscal 2004		Fiscal 2003	
	Non-Interest Expense	% of Total	Non-Interest Expense	% of Total
	(In thousands, except percentages)			
Salaries and Employee Benefits	$ 6,886	56.93%	$ 5,873	51.24%
Net Occupancy Expense	1,538	12.72	1,611	14.05
Equipment Expense	357	2.95	397	3.46
FDIC Assessment	115	0.95	80	0.70
Data Processing Expense	157	1.30	183	1.60
Other	3,042	25.15	3,319	28.95
Total Non-Interest Expense	$12,095	100.00%	$11,463	100.00%

Provision for Income Tax. During the years ended December 31, 2004 and 2003, we recorded recorded income tax expense of $6.13 million and $5.64 million, respectively. The tax provisions for federal, state and local taxes recorded for 2004 and 2003 represent effective tax rates of 44.98% and 43.22%, respectively.

Common Stock Repurchases

On May 15, 2003, The Company's Board of Directors authorized the purchase of up to an additional 450,000 shares of its Common Stock in the open market, from time to time, depending upon prevailing market conditions, thereby increasing the maximum number of shares which may be purchased by the Company from 1,950,000 shares of Common Stock to 2,400,000 shares of Common Stock. Since 1990 through December 31, 2003, the Company has purchased a total of 1,844,646 shares of its Common Stock. During fiscal year 2004, we purchased a total of 4,263 shares and at December 31, 2004, there were 551,091 shares of Common Stock which may yet be purchased under our stock repurchase plan. The following table sets forth information with respect to such purchases during the periods indicated.

Fiscal Year 2004

	Number of Shares Purchased	Average Price Paid Per Share
January	4,263	$ 16.33
February - March	--	--
April - June	--	--
July - September	--	--
October - December	--	--

Results of Operations Fiscal Year Ended December 31, 2003 Compared to Fiscal Year Ended December 31, 2002.

General.

References to per share amounts below, unless stated otherwise, refer to diluted shares. References to per share amounts for the fiscal years ended December 31, 2003 and 2002 have been revised to reflect the one-for-ten reverse stock split and thirty-for-one forward stock split in the form of a 3000% stock dividend which occurred on May 18, 2004.

Net Income. Net income for the fiscal year ended December 31, 2003 was $7.42 million, or $1.10 per share, as compared to $5.60 million, or $.81 per share, for the fiscal year ended December 31, 2002.

Interest rates, as measured by the prime rate, began the year at 4.25%, declined by 25 basis points in late June to 4.00% and remained at that level through December 31, 2003. We have operated in a consistently declining interest rate environment since May 2000 when the prime rate peaked at 9.50%, which has also been a period of low inflation, stock market uncertainties, recession and the aftermath of September 11, 2001.

Net Interest Income. The Company's primary source of revenue is net interest income, or the difference between interest income on earning assets, such as loans and investment securities, and interest expense on interest-bearing liabilities such as deposits and borrowings.

For the fiscal year ended December 31, 2003, net interest income increased by $1.95 million, or 10.37%, to $20.78 million from $18.83 million for the fiscal year ended December 31, 2002. The increase in net interest income was the result of a 33.80% growth in the average amount of interest-earning assets to $765.94 million at the end of 2003 from $572.45 million at the end of 2002, partially offset by the 38.77% growth in the average amount of interest-bearing liabilities to $660.54 million from $475.99 million at December 31, 2003 and 2002, respectively, as well as the difference between the yield on assets compared to the cost of liabilities.

During fiscal 2003, the average yield on interest-earning assets fell to 4.49% from 5.63% in fiscal 2002, a decline of 20.25%, while the average cost of interest-bearing liabilities fell to 2.07% from 2.82%, a decline of 26.60% The interest-rate spread, the difference between the average yield on interest-

earning assets and the average cost of interest bearing liabilities, eased by 39 basis points to 2.42% during fiscal 2003 from 2.81% during fiscal 2002.

Net Interest Margin. Net interest margin, or annualized net interest income as a percentage of average interest-earning assets, declined to 2.71% in fiscal 2003 from 3.29% in fiscal 2002. We seek to secure and retain customer deposits with competitive products and rates, while making strategic use of the prevailing interest rate environment to borrow funds at what we believe to be attractive rates, and to invest such funds in a prudent mix of loans and investment securities. The average amounts of loans and investment securities increased by $25.63 million and $172.40 million, respectively, to $291.59 million and $470.41 million, respectively, in the year ended December 31, 2003, from $265.96 million and $298.01 million, respectively, in the year ended December 31, 2002.

The average yield on loans declined to 6.54% in 2003 from 7.04% in 2002 as older loans with higher rates, commercial and residential mortgage loans, were paid off, matured, and/or refinanced at lower rates. During periods of low and stable interest rates, as was the case during 2003, borrowers gravitate towards fixed-rate loans to lock in a low interest rate, whereas adjustable rate loans are generally preferred when interest rates are high. One-to-four family mortgage loans, approximately 57% of our loan portfolio at December 31, 2003, are particularly sensitive to changes in interest rates.

The average amounts of interest-bearing deposits and time deposits increased by $85.49 million and $59.66 million, respectively, to $201.82 million and $333.11 million, respectively, in fiscal year 2003, from $116.33 million and $273.45 million, respectively, in fiscal year 2002. Borrowed funds increased by

$39.40 million to $125.61 million in 2003 from $86.21 million in the 2002. During fiscal year 2003, the average rates paid on interest-bearing deposits, time deposits and borrowed funds declined to 1.28%, 2.26% and 2.80%, respectively, from 1.41%, 3.21% and 3.49%, respectively in fiscal year 2002.

Interest Income. Total interest income for the fiscal year ended December 31, 2003 increased by $2.18 million, or 6.77%, to $34.43 million from $32.24 million for the fiscal year ended December 31, 2002. The increase was the result of the 33.80% increase in the average amount of total interest-earning assets to $765.94 million in fiscal year 2003 from $572.45 million in fiscal 2002. Interest income on loans and investment securities increased to $19.06 million and $15.32 million, respectively, in fiscal year 2003, from $18.72 million and $13.38 million, respectively in fiscal year 2003.

Interest Expense. Total interest expense for the fiscal year ended December 31, 2003 increased by $231,000, or 1.72%, to $13.65 million from $13.42 million for the fiscal year ended December 31, 2002. The increase in interest expense was due primarily to the 38.77% increase in the average amount of total interest-bearing liabilities, all but offset by the 26.60% decline in the average rate paid on such balances. Interest expense increased to $2.59 million on interest-bearing deposits and decreased to $7.54 million on time deposits during fiscal year 2003, from $1.64 million and $8.77 million, respectively, during fiscal year 2002. Interest expense on borrowings, which are generally invested in earning assets of similar maturities, increased to $3.52 million in fiscal year 2003 from $3.01 million in fiscal year 2002.

Non-Interest Income. Non-interest income consists primarily of realized gains on sales of marketable securities and service fee income. For the fiscal year ended December 31, 2003, total non-interest income increase by $1.70 million, or 74.16%, to $3.98 million from $2.29 million for the fiscal year ended December 31, 2002. Investment securities gains increased to $2.75 million in fiscal year 2003 from $1.54 million in fiscal 2002, as we sold securities during 2003, realizing gains, and purchased new securities with shorter maturities. Service charges on deposit accounts increased by $92,000 to $640,000 in fiscal year 2003 from $548,000 in fiscal year 2002.

Non-Interest Expense. Non-interest expense includes salaries and employee benefits, occupancy and equipment expenses, legal and professional fees and other operating expenses associated with the day-to-day operations of the Company. Total non-interest expense for the year ended December 31, 2003 increased by $683,000, or 6.34%, to $11.46 million from $10.78 million for the year ended December 31, 2002. The increase was largely due to the $690,000 increase in salaries and employee benefits resulting from the additional personnel required to operate our expanding business.

Provision for Income Tax. During the years ended December 31, 2003 and 2002, we recorded income tax expense of $5.64 million and $4.35 million, respectively. The tax provisions for federal, state and local taxes recorded for 2003 and 2002 represent effective tax rates of 43.22% and 43.73%, respectively.

Investment Activities

General. The investment policy of the Bank is designed primarily to provide satisfactory yields while maintaining adequate liquidity, a balance of high quality, diversified investments, and minimal risk. The Bank does not as a rule invest in equity securities. The largest component of the Bank's securities investments, representing more than 50% of total investment securities, are debt securities issued by the Federal Home Loan Mortgage Corporation (Freddie Mac), the Federal National Mortgage Association (Fannie Mae) or the Government National Mortgage Association (Ginnie Mae). The remainder of the Bank's debt securities investments are primarily short term debt securities issued by the United States or its agencies. The Bank maintains a small portfolio of less than $4 million of high-yield corporate debt securities. Recognizing the higher credit risks of these securities, the Bank underwrites these securities in a manner similar to its loan underwriting procedures.

As required by the Statement of Financial Accounting Standard No. 115 ("SFAS No. 115"), securities are classified into three categories: trading, held-to-maturity and available-for-sale. Securities that are bought and held principally for the purpose of selling them in the near term are classified as trading securities and are reported at fair value with unrealized gains and losses included in trading account activities in the statement of income. Securities that the Bank has the positive intent and ability to hold to maturity are classified as held-to-maturity and reported at amortized cost. All other securities are classified as available-for-sale. Available-for-sale securities are reported at fair value with unrealized gains and losses included, on an after-tax basis, as a separate component of net worth. The Bank does not have a trading securities portfolio and has no current plans to maintain such a

portfolio in the future. The Bank generally classifies all newly purchased debt securities as available for sale in order to maintain the flexibility to sell those securities if the need arises. The Bank has a limited portfolio of securities classified as held to maturity, represented principally by securities purchased a number of years ago.

Federal Home Loan Bank Stock. The Bank owns stock of the Federal Home Loan Bank of New York (the "FHLBNY") which is necessary for it to be a member of the FHLBNY. Membership requires the purchase of stock equal to 1% of the Bank's residential mortgage loans. If the Bank borrows from the FHLBNY, the Bank must own stock at least equal to 5% of its borrowings.

The following table sets forth the cost and fair value of available-for- sale and held-to-maturity securities as of the dates indicated:

	December 31,			
	2004		2003	
	Cost	Fair Value	Cost	Fair Value
			(In thousands)	
Available-For-Sale				
U.S. Treasury Notes	$ 24,896	$ 24,722	$ 39,941	$ 39,847
U.S. Government Agencies	471,018	467,271	419,175	416,753
Mortgage-backed securities	109,822	109,330	93,875	97,448
Corporate notes	21,089	21,627	1,570	1,662
Municipal securities	1,307	1,441	991	1,061
Marketable equity securities and other	6,363	6,577	12,305	12,366
Total	$634,495	$630,968	$567,857	$569,137
Held-To-Maturity				
U.S. Government Agencies	$ 624	$ 633	$ 711	$ 715
Total	$ 624	$ 633	$ 711	$ 715

The following tables summarize the Company's available-for-sale and held- to-maturity securities:

	December 31, 2004	
	Weighted Average Yield	Cost
	(Dollars in thousand	
Available-For-Sale		
U.S. Treasury Notes		
Due within one year	1.63%	$ 9,968
Due after one year through five years	1.76	14,928
		24,896
U.S. Government Agencies Obligations		
Due within one year	2.36	14,973
Due after one year through five years	3.25	170,493
Due after five years through ten years	4.26	184,348
Due after ten years	3.71	101,204
		471,018
Municipal Obligations		
Due after ten years	9.32	1,307
		1,307
Mortgage-backed securities		
Due after five years through ten years	4.16	22,571
Due after ten years	4.10	87,251
		109,822
Corporate Notes		
Due after one year through five years	7.18	3,036
Due after five years through ten years	6.54	6,210
Due after ten years	7.61	11,842
		21,088
Common Stocks	2.43	329
Preferred Stocks	9.45	454
Money market funds	1.78	800
Federal Home Loan Bank Stock	0.00	4,780
		6,363
		$634,494
Held-To-Maturity		
U.S. Government Agencies Obligations		
Due after one year through five years	3.11	58
Due after five years through ten years	2.41	93
Due after ten years	6.18	473
		$ 624

Loan Portfolio

Loan Portfolio Composition. The Company's loans consist primarily of mortgage loans secured by residential and non-residential properties as well as commercial loans which are either unsecured or secured by personal property collateral. Most of the Company's loans are either made to individuals or personally guaranteed by the principals of the business to which the loan is made. At December 31, 2004, 2003 and 2002, the Company had total loans, net of unearned income of $286.98 million, $294.76 million and $275.50 million, respectively, and an allowance for loan losses of $2.93 million, $2.59 million, and $2.32 million, respectively. From time to time, the Bank may originate residential mortgage loans, sell them on the secondary market, normally recognizing fee income in connection with the sale.

Interest rates on loans are affected by the demand for loans, the supply of money available for lending, credit risks, the rates offered by competitors and other conditions. These factors are in turn affected by, among other things, economic conditions, monetary policies of the federal government, and legislative tax policies.

In order to manage interest rate risk, the Bank focuses its efforts on loans with interest rates that adjust based upon changes in the prime rate or changes in United States Treasury or similar indices. Generally, credit risks on adjustable-rate loans are somewhat greater than on fixed-rate loans primarily because, as interest rates rise, so do borrowers' payments, increasing the potential for default. The Bank seeks to impose appropriate loan underwriting standards in order to protect against these and other credit related risks associated with its lending operations.

In addition to analyzing the income and assets of its borrowers when underwriting a loan, the Bank obtains independent appraisals on all material real estate in which the Bank takes a mortgage. The Bank generally obtains title insurance in order to protect against title defects on mortgaged property.

Commercial and Mortgage Loans. The Bank originates commercial mortgage loans secured by office buildings, retail establishments, multi-family residential real estate and other types of commercial property. Substantially all of the properties are located in the New York City metropolitan area.

The Bank generally makes commercial mortgage loans with loan to value ratios not to exceed 75% and with terms to maturity that do not exceed 15 years. Loans secured by commercial properties generally involve a greater degree of risk than one- to four-family residential mortgage loans. Because payments on such loans are often dependent on successful operation or management of the properties, repayment may be subject, to a greater extent, to adverse conditions in the real estate market or the economy. The Bank seeks to minimize these risks through its underwriting policies. The Bank evaluates the qualifications and financial condition of the borrower, including credit history, profitability and expertise, as well as the value and condition of the underlying property. The factors considered by the Bank include net operating income; the debt coverage ratio (the ratio of cash net income to debt service); and the loan to value ratio. When evaluating the borrower, the Bank considers the financial resources and income level of the borrower, the borrower's experience in owning or

managing similar property and the Bank's lending experience with the borrower. The Bank's policy requires borrowers to present evidence of the ability to repay the loan without having to resort to the sale of the mortgaged property. The Bank also seeks to focus its commercial mortgage loans on loans to companies with operating businesses, rather than passive real estate investors.

Commercial Loans. The Bank makes commercial loans to businesses for inventory financing, working capital, machinery and equipment purchases, expansion, and other business purposes. These loans generally have higher yields than mortgages loans, with maturities of one year, after which the borrower's financial condition and the terms of the loan are re-evaluated.

Commercial loans tend to present greater risks than mortgage loans because the collateral, if any, tends to be rapidly depreciable, difficult to sell at full value and is often easier to conceal. In order to limit these risks, the Bank evaluates these loans based upon the borrower's ability to repay the loan

from ongoing operations. The Bank considers the business history of the borrower and perceived stability of the business as important factors when considering applications for such loans. Occasionally, the borrower provides commercial or residential real estate collateral for such loans, in which case the value of the collateral may be a significant factor in the loan approval process.

Residential Mortgage Loans (1 to 4 family loans). The Bank makes residential mortgage loans secured by first liens on one-to-four family owner-occupied or rental residential real estate. At December 31, 2004 and 2003, approximately $151.20 million and $169.59 million, respectively, or 52.69% and 57.4%, respectively, of the Company's total loan portfolio consisted of such loans. The Company offers both adjustable rate mortgages ("ARMS") and fixed-rate mortgage loans. The relative proportion of fixed-rate loans versus ARMs originated by the Bank depends principally upon current customer preference, which is generally driven by economic and interest rate conditions and the pricing offered by the Bank's competitors. At December 31, 2004 and 2003, approximately 13% and 12%, respectively, of the Bank's residential one-to-four family owner-occupied first mortgage portfolio were ARMs and approximately 87% and 88%, respectively, were fixed-rate loans. The percentage represented by fixed-rate loans tends to increase during periods of low interest rates. The ARMs generally carry annual caps and life-of-loan ceilings, which limit interest rate adjustments.

The Bank's residential loan underwriting criteria are generally comparable to those required by the Federal National Mortgage Association ("FNMA") and other major secondary market loan purchasers. Generally, ARM credit risks are somewhat greater than fixed-rate loans primarily because, as interest rates rise, the borrowers' payments rise, increasing the potential for default. The Bank's teaser rate ARMs (ARMs with low initial interest rates that are not based upon the index plus the margin for determining future rate adjustments) were underwritten based on the payment due at the fully-indexed rate.

In addition to verifying income and assets of borrowers, the Bank obtains independent appraisals on all residential first mortgage loans and title insurance is required at closing. Private mortgage insurance is required on all

loans with a loan-to-value ratio in excess of 80% and the Bank requires real estate tax escrows on such loans. Real estate tax escrows are voluntary on residential mortgage loans with loan-to-value ratios of 80% or less.

Fixed-rate residential mortgage loans are generally originated by the Bank for terms of 15 to 30 years. Although 30 year fixed-rate mortgage loans may adversely affect our net interest income in periods of rising interest rates, the Bank originates such loans to satisfy customer demand. Such loans are generally originated at initial interest rates which exceed the fully indexed rate on ARMs offered at the same time. Fixed-rate residential mortgage loans originated by the Bank generally include due-on-sale clauses, which permit the Bank to demand payment in full if the borrower sells the property without the Bank's consent. Due-on-sale clauses are an important means of adjusting the rates on the Bank's fixed-rate mortgage loan portfolio, and the Bank will generally exercise its rights under these clauses if necessary to maintain market yields.

ARMs originated in recent years have interest rates that adjust annually based upon the movement of the one year treasury bill constant maturity index, plus a margin of 2.00% to 2.75%. These loans generally have a maximum interest rate adjustment of 2% per year, with a lifetime maximum interest rate adjustment, measured from the initial interest rate, of 5.5% or 6.0%.

The Bank offers a variety of other loan products including residential single family construction loans to persons who intend to occupy the property upon completion of construction, home equity loans secured by junior mortgages on one-to-four family owner-occupied residences, and short-term fixed-rate consumer loans either unsecured or secured by monetary assets such as bank deposits and marketable securities or personal property.

Origination of Loans. Loan originations can be attributed to depositors, retail customers, phone inquiries, advertising, the efforts of the Bank's loan officers, and referrals from other borrowers, real estate brokers and builders. The Bank originates loans primarily through its own efforts, occasionally obtaining loan opportunities as a result of referrals from loan brokers.

At December 31, 2004, the Bank's total capital, net of goodwill and loan loss reserves, was approximately $82.97 million and thus it was generally not permitted to make loans to one borrower in excess of approximately $12.4 million, with an additional amount of approximately $8.3 million being permitted if secured by readily marketable collateral. The Bank was also not permitted to make any single mortgage loan in an amount in excess of approximately $12.4 million. At December 31, 2004, the Bank was in compliance with these standards.

Delinquency Procedures. When a borrower fails to make a required payment on a loan, the Bank attempts to cause the deficiency to be cured by contacting the borrower. The Bank reviews past due loans on a case by case basis, taking the action it deems appropriate in order to collect the amount owed. Litigation may be necessary if other procedures are not successful. Judicial resolution of a past due loan can be delayed if the borrower files a bankruptcy petition because collection action cannot be continued unless the

Bank first obtains relief from the automatic stay provided by the Bankruptcy Code.

If a non-mortgage loan becomes delinquent and satisfactory arrangements for payment cannot be made, the Bank seeks to realize upon any personal property collateral to the extent feasible and collect any remaining amount owed from the borrower through legal proceedings, if necessary.

It is the Bank's policy to discontinue accruing interest on a loan when it is 90 days past due or if management believes that continued interest accruals are unjustified. The Bank may continue interest accruals if a loan is more than 90 days past due if the Bank determines that the nature of the delinquency and the collateral are such that collection of the principal and interest on the loan in full is reasonably assured. When the accrual of interest is discontinued, all accrued but unpaid interest is charged against current period income. Once the accrual of interest is discontinued, the Bank records interest as and when received until the loan is restored to accruing status. If the Bank determines that collection of the loan in full is in reasonable doubt, then amounts received are recorded as a reduction of principal until the loan is returned to accruing status.

The following tables set forth information concerning the Company's loan portfolio by type of loan at the dates indicated:

	December 31,				
	2004		2003		200
	Amount	% of Total	Amount	% of Total	Amou
	(Dollars in thousands)				
Commercial and professional loans	$ 16,498	5.7 %	$ 22,228	7.5 %	$ 16,7
Secured by real estate					
1 - 4 family	155,079	53.9	169,589	57.4	180,7
Multi family	4,600	1.6	6,608	2.2	8,9
Non-residential (commercial)	109,597	38.1	94,956	32.2	65,8
Consumer	1,989	0.7	2,239	0.7	4,0
Total loans	287,763	100.0 %	295,620	100.0 %	276,2
Less:					
Allowance for loan losses	(2,927)		(2,593)		(2,3
Unearned fees	(784)		(864)		(7
Loans, net	$284,052		$292,163		$273,1

	December 31, 2001		December 31, 2000	
	Amount	% of Total	Amount	% of Total
	(Dollars in thousands)			
Commercial and professional loans	$ 19,130	7.6%	$ 9,419	12.5%
Secured by real estate				
1 - 4 family	165,195	65.5	25,677	34.0
Multi family	11,186	4.4	4,765	6.3
Non-residential (commercial)	51,893	20.6	34,968	46.2
Consumer	4,689	1.8	229	0.3
Other	140	0.1	565	0.7
Total loans	252,233	100.0%	75,623	100.0%
Less:				
Allowance for loan losses	(2,030)		(1,108)	
Unearned fees	(193)		(275)	
Loans, net	$250,010		$ 74,240	

Impaired loan balance, nonaccrual loans and loans greater than 90 days still accruing

The following table sets forth certain information regarding nonaccrual loans, including the ratio of such loans to total assets as of the dates indicated, and certain other related information. The Bank had no foreclosed real estate during these periods and loans past due more than 90 days still accruing were $50,000 and $0 at December 31, 2004 and 2003, respectively.

	December 31,			
	2004	2003	2002	2001
	(Dollars in Thousands)			
Nonaccrual loans:				
Commercial and professional loans	$ --	$ --	$ --	$
Consumer	1	--	--	-
Secured by real estate	342	109	59	-
Total nonaccrual loans	343	109	59	
Accruing loans delinquent 90 days or more	50	--	--	-
Total nonperforming loans	$ 393	$ 109	$ 59	$

Total nonperforming loans to total assets	.04%	.01%	--	-

The following tables present information regarding the Company's total allowance for loan losses as well as the allocation of such amounts to the various categories of loans at the dates indicated (dollars in thousands):

	December 31, 2004		
	Allowance for Loan Losses	Percent of Allowance	Percent of Total Loans
Commercial and professional loans	$ 223	7.6%	0.08%
Secured by real estate			
1 - 4 family	775	26.5	0.27
Multi family	62	2.1	0.02
Non-residential	1,398	47.8	0.49
Consumer and other	27	0.9	0.01
General allowance (1)	442	15.1	0.15
Total allowance for loan losses	$ 2,927	100.0%	1.02%

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(1) The allowance for loan losses is allocated to specific loans as necessary.

	December 31, 2003		
	Allowance for Loan Losses	Percent of Allowance	Percent of Total Loans
Commercial and professional loans	$ 300	11.6%	0.10%
Secured by real estate			
1 - 4 family	424	16.3	0.14
Multi family	89	3.4	0.03
Non-residential	1,198	46.2	0.41
Consumer and other	30	1.2	0.01
General allowance (1)	552	21.3	0.19

Total allowance for loan losses	$ 2,593	100.0%	0.88%

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(1) The allowance for loan losses is allocated to specific loans as necessary.

	December 31, 2002		
	Allowance for Loan Losses	Percent of Allowance	Percent of Total Loans
Commercial and professional loans	$ 225	9.7%	0.08%
Secured by real estate			
1 - 4 family	452	19.5	0.16
Multi family	121	5.2	0.04
Non-residential	888	38.4	0.32
Consumer and other	55	2.4	0.02
General allowance (1)	574	24.8	0.21
Total allowance for loan losses	$ 2,315	100.0%	0.83%

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(1) The allowance for loan losses is allocated to specific loans as necessary.

	December 31, 2002		
	Allowance for Loan Losses	Percent of Allowance	Percent of Total Loans
Commercial and professional loans	$ 188	9.3%	0.07%
Secured by real estate			
1 - 4 family	804	39.6	0.32
Multi family	84	4.1	0.03
Non-residential	790	38.9	0.32
Consumer and other	24	1.2	0.06
General allowance (1)	140	6.9	0.06
Total allowance for loan losses	$ 2,030	100.0%	0.79%

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(1) The allowance for loan losses is allocated to specific loans as necessary.

	December 31, 2002		
	Allowance for Loan Losses	Percent of Allowance	Percent of Total Loans
Commercial and professional loans	$ 89	8.0%	0.12%
Secured by real estate	654	59.0	0.86
Personal and other	13	1.2	0.02
General allowance (1)	352	31.8	0.47%
Total allowance for loan losses	$ 1,108	100.0%	1.47%

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(1) The allowance for loan losses is allocated to specific loans as necessary.

The following tables set forth information regarding the aggregate maturities of the Company's loans in the specified categories and the amount of such loans which have fixed and variable rates.

	December 31, 2002			
	Within 1 Year	1 to 5 Years	After 5 Years	Total
	(In thousands)			
Fixed Rate				
Commercial and professional	$ 657	$ 3,961	$ 128,193	$ 132,81
Non-residential	5,453	31,755	30,885	68,09
Total fixed rate	$ 6,110	$ 35,716	$ 159,078	$ 200,90
Adjustable Rate				
Commercial and professional	1,407	10,459	15,002	26,86
Non-residential	25,396	11,298	23,297	59,99

Total adjustable rate	$ 26,803	$ 21,757	$ 38,299	$ 86,85
Total	$ 32,913	$ 57,473	$ 197,377	$ 287,76

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The following table sets forth information with respect to activity in the Company's allowance for loan losses during the periods indicated (in thousands, except percentages):

	Years Ended December 31,				
	2004	2003	2002	2001	
Average loans outstanding	$290,774	$291,586	$265,961	$195,296	$
Allowance at beginning of period	2,593	2,315	2,030	1,108	
Charge-offs:					
Commercial and other loans	24	4	199	97	
Real estate loans	--	13	--	--	
Total loans charged-off	24	17	199	97	
Recoveries:					
Commercial and other loans	178	55	97	41	
Real estate loans	--	--	--	--	
Total loans recovered	178	55	97	41	
Net recoveries (charge-offs)	154	38	(102)	(56)	
Provision for loan losses charged to operating expenses	180	240	387	287	
Acquisition of GSB	--	--	--	691	
Allowance at end of period	$ 2,927	$ 2,593	$ 2,315	$ 2,030	$
Ratio of net recoveries (charge-offs) to average loans outstanding	.05%	0.01%	(.03)%	(.02)%	
Allowance as a percent of total loans	1.02%	0.88%	0.83%	0.80%	

Total loans at end of period	$287,763	$295,620	$276,252	$252,233	$

Deposits

The Bank concentrates on obtaining deposits from a variety of businesses, professionals and retail customers. The Bank offers a number of different deposit programs, including statement savings accounts, NOW accounts, money market deposits accounts, checking accounts and certificates of deposits with terms from seven days to five years. Deposit account terms vary according to the minimum balance required, the time period the funds must remain on deposit and the interest rate, among other factors. The Bank prices its deposit offerings competitively within the market it serves. These products are designed to attract new customers, retain existing customers and create opportunities to offer other bank products or services. While the market and pricing for deposit funds are very competitive, the Bank believes that personalized, quality service is also an important element in retaining core deposit customers.

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The following table summarizes the composition of the average balances of major deposit categories:

	December 31,				
	2004		2003		
	Average Amount	Average Yield	Average Amount	Average Yield	Avera Amou
	(Dollars in thousands)				
Demand deposits	$ 38,896	--	$ 32,592	--	$ 30,
NOW and money market	47,677	0.65%	58,723	1.02%	60,
Savings deposits	224,542	1.55	143,094	1.95	56,
Time deposits	309,968	1.94	333,112	2.26	273,
Total deposits	$621,083	1.58%	$567,521	1.78%	$419,

The aggregate amount of jumbo certificates of deposit, each with a minimum denomination of $100,000, was approximately $109.74 million, $110.08 million and $108.72 million December 31, 2004, 2003 and 2002, respectively.

The following table summarizes the maturity distribution of time deposits of $100,000 or more as of December 31, 2004:

	(In thousands)
3 months or less	$ 48,987
Over 3 months but within 6 months	25,160
Over 6 months but within 12 months	10,375
Over 12 months	25,219
Total	$109,741

Short-Term Borrowings

Securities sold under agreements to repurchase generally mature within 30 days from the date of the transactions. Short-term borrowings consist of Treasury Tax and Loan Note Options and various other borrowings which generally have maturities of less than one year. The details of these categories are presented below:

	Years Ended December 31,		
	2004	2003	2002
	(Dollars in thousands)		
Securities sold under repurchase agreements and federal funds purchased			
Balance at year-end	$127,747	$114,391	$ 46,673
Average during the year	$129,794	$ 57,554	$ 38,443
Maximum month-end balance	$148,753	$114,391	$ 47,407
Weighted average rate during the year	1.87%	1.68%	1.79%
Rate at December 31	2.27%	1.73%	1.46%

Capital Resources and Liquidity

Liquidity

The management of the Company's liquidity focuses on ensuring that sufficient funds are available to meet loan funding commitments, withdrawals from deposit accounts, the repayment of borrowed funds, and ensuring that the Bank and the Company comply with regulatory liquidity requirements. Liquidity needs of The Berkshire Bank have historically been met by deposits, investments in federal funds sold, principal and interest payments on loans, and maturities of investment securities.

For the parent company, Berkshire Bancorp Inc., liquidity means having cash available to fund operating expenses and to pay shareholder dividends, when and if declared by our Board of Directors. We paid cash dividends per share of $.11, $.08 and $.07 in fiscal 2004, 2003 and 2002, respectively. The ability to fund our operations and to pay dividends is not dependent upon the receipt of dividends from The Berkshire Bank. At December 31, 2004, we had cash of approximately $7.4 million and investment securities with a fair market value of $9.0 million.

Contingent Liabilities and Commitments

The Bank maintains financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit and stand-by letters of credit. The following table presents the Company's commitments at December 31, 2004.

	Expiration By Period			
	Total	Less Than 1 Year	1-3 Years	3-5 Years
	(In thousands)			
Lines of Credit	$ 15,859	$ 9,555	$ 3,730	$ 958
Standby Letters of Credit	750	706	44	--
Loan Commitments	--	--	--	--
Total	$ 16,609	$ 10,261	$ 3,774	$ 958

Contractual Obligations

The following table presents the Company's contractual obligations at December 31, 2004.

	Payments Due By Periods			
	Total	Less Than 1 Year	1-3 Years	3-5 Years
	(In thousands)			
Long-Term Debt	$ 95,605	$ 2,638	$ 43,296	$ 35,671
Operating Leases	3,695	712	1,440	1,012
Time Deposits	274,309	218,691	53,538	2,080
Total Contractual Obligations	$373,609	$222,041	$ 98,274	$ 38,763

The Company currently has one unconsolidated subsidiary and no special purpose entities.

Capital

The capital ratios of the Bank and Berkshire are presently in excess of the requirements necessary to meet the "well capitalized" capital category established by bank regulators. See Note P to the Consolidated Financial Statements.

Interest Rate Risk

Fluctuations in market interest rates can have a material effect on the Bank's net interest income because the yields earned on loans and investments may not adjust to market rates of interest with the same frequency, or with the same speed, as the rates paid by the Bank on its deposits.

Most of the Bank's deposits are either interest-bearing demand deposits or short term certificates of deposit and other interest-bearing deposits with interest rates that fluctuate as market rates change. Management of the Bank seeks to reduce the risk of interest rate fluctuations by concentrating on loans and securities investments with either short terms to maturity or with adjustable rates or other features that cause yields to adjust based upon interest rate fluctuations. In addition, to cushion itself against the potential adverse effects of a substantial and sustained increase in market interest rates, the Bank has purchased off balance sheet interest rate cap contracts which generally provide that the Bank will be entitled to receive payments from the other party to the contract if interest rates exceed specified levels. These contracts are entered into with major financial institutions.

The Company seeks to maximize its net interest margin within an acceptable level of interest rate risk. Interest rate risk can be defined as the amount of the forecasted net interest income that may be gained or lost due to favorable or unfavorable movements in interest rates. Interest rate risk, or sensitivity, arises when the maturity or repricing characteristics of assets differ significantly from the maturity or repricing characteristics of liabilities.

In the banking industry, a traditional measure of interest rate sensitivity is known as "gap" analysis, which measures the cumulative differences between the amounts of assets and liabilities maturing or repricing at various time intervals. The following table sets forth the Company's interest rate repricing gaps for selected maturity periods:

Berkshire Bancorp Inc.
Interest Rate Sensitivity Gap at December 31, 2
(in thousands, except for percentages)

		3 Months or Less	3 Through 12 Months	1 Throug 3 Years
Federal funds sold		7,500		
	(Rate)	2.25%		
Interest bearing deposits in banks		372	--	--
	(Rate)	1.40%		
Loans (1)(2)				
Adjustable rate loans		46,352	16,394	7,989
	(Rate)	6.35%	5.06%	7.56%
Fixed rate loans		546	5,564	16,732
	(Rate)	7.35%	7.37%	6.84%
Total loans		46,898	21,958	24,721
Investments (3)(4)		25,587	34,963	187,503
	(Rate)	4.64%	2.11%	2.95%
Total rate-sensitive assets		72,857	56,921	212,224
Deposit accounts (5)				
Savings and NOW		277,616	--	--
	(Rate)	1.59%		
Money market		25,772	--	--
	(Rate)	0.73%		
Time Deposits		113,377	105,314	53,538
	(Rate)	1.83%	1.92%	2.78%
Total deposit accounts		416,765	105,314	53,538
Repurchase Agreements		57,297	37,450	33,000
	(Rate)	1.92%	2.49%	2.92%
Other borrowings			2,638	43,296
	(Rate)	%	3.34%	3.61%
Total rate-sensitive liabilities		474,062	145,402	129,834
Interest rate caps		20,000		(10,000)
Gap (repricing differences)		(421,205)	(88,481)	92,390
Cumulative Gap		(421,205)	(509,686)	(417,296)

Cumulative Gap to Total Rate Sensitive Assets		(45.84)%	(55.47)%	(45.42)%

Berkshire Bancorp Inc.
Interest Rate Sensitivity Gap at December 31, 2
(in thousands, except for percentages)

		Over 3 Years	Total	Fair Val
Federal funds sold			7,500	7,500
	(Rate)			
Interest bearing deposits in banks		--	372	372
	(Rate)		1.40%	
Loans (1)(2)				
Adjustable rate loans		16,124	86,859	91,219
	(Rate)	6.41%	6.13%	
Fixed rate loans		178,062	200,904	200,241
	(Rate)	6.29%	6.82%	
Total loans		194,186	287,763	291,460
Investments (3)(4)		382,620	630,673	631,601
	(Rate)	4.39%	3.85%	
Total rate-sensitive assets		576,806	918,808	
Deposit accounts (5)				
Savings and NOW		--	277,616	277,616
	(Rate)		1.59%	
Money market		--	25,772	28,882
	(Rate)		0.73%	
Time Deposits		2,080	274,309	273,397
	(Rate)	1.97%	2.05%	
Total deposit accounts		2,080	577,697	
Repurchase Agreements		--	127,747	127,422
	(Rate)	--	2.35%	
Other borrowings		65,135	111,069	112,598
	(Rate)	4.17%	3.94%	
Total rate-sensitive liabilities		67,215	816,513	
Interest rate caps		(10,000)		26
Gap (repricing differences)		519,591	102,295	
Cumulative Gap		102,295		

Cumulative Gap to Total Rate Sensitive Assets	11.13%

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(1) Adjustable-rate loans are included in the period in which the interest rates are next scheduled to adjust rather than in the period in which the loans mature. Fixed-rate loans are scheduled according to their maturity dates.

(2) Includes nonaccrual loans.

(3) Investments are scheduled according to their respective repricing (variable rate loans) and maturity (fixed rate securities) dates.

(4) Investments are stated at book value.

(5) NOW accounts and savings accounts are regarded as readily accessible withdrawal accounts. The balances in such accounts have been allocated among maturity/repricing periods based upon The Berkshire Bank's historical experience. All other time accounts are scheduled according to their respective maturity dates.

Impact of Inflation and Changing Prices

The Company's financial statements measure 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 impact of inflation is reflected in the increasing cost of the Company's operations. The assets and liabilities of the Company are largely monetary. As a result, interest rates have a greater impact on the Company's performance than do the effects of general levels of inflation. In addition, interest rates do not necessarily move in the direction, or to the same extent as the price of goods and services. However, in general, high inflation rates are accompanied by higher interest rates, and vice versa.

New Accounting Pronouncements

Loan Commitments

In March 2004, the Securities and Exchange Commission (the "SEC") staff issued Staff Accounting Bulletin ("SAB") 105 ("SAB 105"), "Application of Accounting Principles to Loan Commitments." The SEC staff does not believe an asset results from the expected future cash flows of servicing a committed loan until the servicing assets have been contractually separated from the underlying loan by sale or securitization of the loan with the servicing retained. SAB 105 is effective for all new loan commitments entered into beginning April 1, 2004. We have followed an accounting methodology consistent with the guidance in SAB 105; accordingly, the adoption of SAB 105 has not had a material effect on our consolidated financial statements.

Stock-Based Compensation

In December 2004, the Financial Accounting Standards Board (the "FASB") issued Statement No. 123 (Revised), Share-based Payment, ("FAS 123(R)"). FAS 123(R) requires that the compensation cost relating to share-based payment

transactions be recognized in financial statements. That cost will be measured based on the fair value of the equity or liability instruments issued. We will be required to apply FAS 123(R) in the third quarter of 2005. The scope of FAS 123(R) includes a wide range of share-based compensation arrangements including share options, restricted share plans, performance-based awards, share appreciation rights and employee share purchase plans. FAS 123(R) replaces FASB Statement 123, Accounting for Stock-Based Compensation ("FAS 123"), and supersedes the Accounting Principles Board (the "APB") Opinion No. 25, Accounting for Stock Issued to Employees ("APB Opinion No. 25"). FAS 123, as originally issued in 1995, established as preferable a fair-value-based method of accounting for share-based payment transactions with employees. However, FAS 123 permitted entities the option of continuing to apply the guidance in APB Opinion No. 25, as long as the footnotes to financial statements disclosed what net income would have been had the had the preferable fair-value-based method been used.

FAS 123(R) provides three methods for companies to transition to the new standard requiring the expensing of options. Companies may elect to (i) restate results for prior quarters in the fiscal year of adoption of FAS 123(R) to reflect the FAS 123 proforma compensation costs, or (ii) restate results for prior periods, whether annual or quarterly, to reflect the FAS 123 proforma compensation costs. We are in the process of determining which transition approach to use and the effect, if any, such transition approach will have on our financial statements.

Accounting for Loans or Certain Debt Securities Acquired in a Transfer

In October 2003, the American Institute of Cetified Public Accountants (the "AICPA") issued SOP 03-3, Accounting for Loans or Certain Debt Securities Acquired in a Transfer. SOP 03-3 applies to a loan with the evidence of deterioration of credit quality since origination acquired by completion of a transfer for which it is probable at acquisition, that the Company will be unable to collect all contractually required payments receivable. SOP 03-3 requires that the Company recognize the excess of all cash flows expected at acquisition over the investor's initial investment in the loan as interest income on a level-yield basis over the life of the loan as the accretable yield. The loan's

contractual required payments receivable in excess of the amount of its cash flows excepted at acquisition (nonaccretable difference) should not be recognized as an adjustment to yield, a loss accrual or a valuation allowance for credit risk. SOP 03-3 is effective for loans acquired in fiscal years beginning after December 31, 2004. Early adoption is permitted. Management is currently evaluating the provisions of SOP 03-3.

Variable Interest Entities

In January 2003, the FASB released Interpretation No. 46, Consolidation of Variable Interest Entities ("FIN 46"). Fin 46 requires that all primary beneficiaries of Variable Interest Entities ("VIE") consolidate that entity. FIN 46 is effective immediately for VIEs created after January 31, 2003 and to VIEs to which an enterprise obtains an interest after that date. It applies in the first fiscal year or interim period beginning after June 15, 2003, to VIEs in

which an enterprise holds a variable interest it acquired before February 1, 2003. In December 2003, the FASB published a revision to FIN 46 ("FIN 46R") to clarify some of the provisions of the interpretation and to defer the effective date of implementation for certain entities. Under the guidance of FIN 46R, entities that do not have interests in structures that are commonly referred to as special purpose entities are required to apply the provisions of the interpretation in financial statements for periods ending after March 14, 2004. We do not have interests in special purpose entities and, accordingly, applied the provisions of FIN 46R with our first quarter 2004 financial statements.

The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments

In November 2003, the Emerging Issues Task Force (the "EITF") of the FASB issued EITF Abstract 03-1, "The Meaning of Other-Than-Temporary Impairment and its Application to Certain Investments" (EITF 03-1). The quantitative and qualitative disclosure provisions of EITF 03-1 are effective for years ending after December 15, 2003 and were included in the Company's 2003 Form 10-K. In March 2004, the EITF issued a Consensus on Issue 03-1 requiring that the provisions of EITF 03-1 be applied for reporting periods beginning after June 15, 2004 to investments accounted for under SFAS Nos. 115 and 124. EITF 03-1 establishes a three-step approach for determining whether an investment is considered impaired, whether that impairment is other-than-temporary, and the measurement of an impairment loss. In September 2004, the FASB issued a proposed Board-directed FASB Staff Position, FSP EITF Issue 03-1-a, "Implementation Guidance for the Application of Paragraph 16 of EITF 03-1." The proposed FSP would provide implementation guidance with respect to debt securities that are impaired solely due to interest rates and/or sector spreads and analyzed for other-than-temporary impairment under paragraph 16 of EITF 03-1. The Board has directed the FASB staff to delay the effective date for the measurement and recognition guidance contained in paragraphs 10-20 of EITF Issue No. 03-1, including steps two and three of the three-step approach for determining whether an investment is other-than-temporarily impaired. However, step one of that approach must still be initially applied for impairment evaluations in reporting periods beginning after June 15, 2004. The delay of the effective date for paragraphs 10-20 of EITF Issue 03-1 will be superseded with the final issuance of proposed FSP EITF Issue 03-1-a, "Implementation Guidance for the Application of Paragraph 16 of EITF Issue No. 03-1." The Company is in the process of determining the impact that this EITF will have on its financial statements.

Internal Control Over Financial Reporting

The current objective of the Bank's Internal Control Program is to allow management to comply with FDICIA requirements and with Section 302 of the Sarbanes-Oxley Act of 2002 (the "Act"). Section 302 of the Act requires the CEOs and CFOs of the Company to (i) certify that the annual and quarterly reports filed with the Securities and Exchange Commission are accurate and (ii) acknowledge that they are responsible for establishing, maintaining and periodically evaluating the effectiveness of the disclosure controls and procedures. Section 404 of the Act requires management to report on internal control over financial reporting. The SEC requires us to comply with Section 404 by the year ending December 31, 2006.

The Committee of Sponsoring Organizations (COSO) methodology may be used to document and test the internal controls pertaining to the accuracy of Company issued financial statements and related disclosures. COSO requires a review of the control environment (including anti-fraud and audit committee effectiveness), risk assessment, control activities, information and communication, and ongoing monitoring.

ITEM 7A. Quantitative and Qualitative Disclosure About Market Risk.

See Item 7. Managements' Discussion and Analysis of Financial Condition and Results of Operations - Interest Rate Risk

ITEM 8. Financial Statements and Supplementary Data.

Report of Independent Registered Public Accounting Firm

Board of Directors and Shareholders
of Berkshire Bancorp Inc.

We have audited the accompanying consolidated statements of financial position of Berkshire Bancorp Inc. and subsidiaries as of December 31, 2004 and 2003, and the related consolidated statements of operations, changes in stockholders' equity and cash flows for each of the three years in the period ended December 31, 2004. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the 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, 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 financial statements referred to above present fairly, in all material respects, the consolidated financial position of Berkshire Bancorp Inc. and Subsidiaries as of December 31, 2004 and 2003, and the consolidated results of their operations and their consolidated cash flows for each of the three years in the period ended December 31, 2004, in conformity with accounting principles generally accepted in the United States of America.

We have also audited, in accordance with the interim standards adopted by the Public Company Accounting Oversight Board (United States), the effectiveness of The Berkshire Bank's (a subsidiary of Berkshire Bancorp Inc.) internal control over financial reporting as of December 31, 2004, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) and our report dated March 29, 2005 expressed an unqualified opinion on management's assertion that The Berkshire Bank maintained effective internal control over financial reporting.

/s/ GRANT THORNTON LLP

Philadelphia, Pennsylvania
March 29, 2005

BERKSHIRE BANCORP INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(Dollars in Thousands)

	December 31, 2004	December 31, 2003
ASSETS		
Cash and due from banks	$ 9,511	$ 7,478
Interest bearing deposits	372	1,832
Federal funds sold	7,500	--
Total cash and cash equivalents	17,383	9,310
Investment Securities:		
Available-for-sale	630,968	569,137
Held-to-maturity, fair value of $633 in 2004 and $715 in 2003	624	711
Total investment securities	631,592	569,848
Loans, net of unearned income	286,979	294,756
Less: allowance for loan losses	(2,927)	(2,593)
Net loans	284,052	292,163
Accrued interest receivable	6,014	5,298
Premises and equipment, net	8,677	8,665
Goodwill, net	18,549	18,549
Other assets	6,382	1,836
Total assets	$ 972,649	$ 905,669
LIABILITIES AND STOCKHOLDERS' EQUITY		
Deposits:		
Non-interest bearing	$ 42,191	$ 38,422
Interest bearing	577,697	565,833
Total deposits	619,888	604,255
Securities sold under agreements to repurchase	127,747	114,391
Long term borrowings	95,605	77,745
Subordinated debt	15,464	--
Accrued interest payable	2,516	2,208
Other liabilities	3,810	3,580

Total liabilities	865,030	802,179
Stockholders' equity		
Preferred stock - $.10 Par value: 2,000,000 shares authorized - none issued	--	--
Common stock - $.10 par value Authorized -- 10,000,000 shares Issued -- 7,698,285 shares Outstanding -- December 31, 2004, 6,748,675 shares December 31, 2003, 6,614,094 shares	770	256
Additional paid-in capital	89,543	89,866
Retained earnings	28,983	22,960
Accumulated other comprehensive (loss) income, net	(2,602)	775
Treasury Stock December 31, 2004, 949,610 shares December 31, 2003, 1,084,191 shares	(9,075)	(10,367)
Total stockholders' equity	107,619	103,490
	$ 972,649	$ 905,669

The accompanying notes are an integral part of these statements

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BERKSHIRE BANCORP INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
(In Thousands, Except Per Share Data)

	For The Years Ended December	
	2004	2003
INTEREST INCOME		
Federal funds sold and interest bearing deposits	$ 63	$ 44
Investments securities	21,120	15,321
Loans, including related fees	18,825	19,061
Total interest income	40,008	34,426
INTEREST EXPENSE		
Deposits	9,833	10,130
Short-term borrowings	2,422	794
Long-term borrowings	3,661	2,723

Total interest expense	15,916	13,647
Net interest income	24,092	20,779
PROVISION FOR LOAN LOSSES	180	240
Net interest income after provision for loan losses	23,912	20,539
NON-INTEREST INCOME		
Service charges on deposit accounts	520	640
Investment securities gains	793	2,746
Other income	506	597
Total non-interest income	1,819	3,983
NON-INTEREST EXPENSE		
Salaries and employee benefits	6,886	5,873
Net occupancy expense	1,538	1,611
Equipment expense	357	397
FDIC assessment	115	80
Data processing expense	157	183
Other	3,042	3,319
Total non-interest expense	12,095	11,463
Income before provision for taxes	13,636	13,059
Provision for income taxes	6,134	5,644
Net income	$ 7,502	$ 7,415
Net income per share:		
Basic	$ 1.12	$ 1.12
Diluted	$ 1.10	$ 1.10
Dividends per share	$ .11	$ .09

The accompanying notes are an integral part of these statements

BERKSHIRE BANCORP INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY

For The Years Ended December 31, 2004, 2003 and 2002
(In Thousands)

Accumul

	Common Shares	Stock Par value	Additional paid-in capital	othe comprehe (loss)
Balance at January 1, 2002	2,566	$256	$89,914	$ (28
Net income				
Acquisition of treasury shares				
Exercise of stock options			(24)	
Other comprehensive income net of reclassification adjustment and taxes				1,76
Comprehensive income				
Cash dividends				
Balance at December 31, 2002	2,566	$256	$89,890	$1,48
Net income				
Acquisition of treasury shares				
Exercise of stock options			(24)	
Other comprehensive (loss) net of reclassification adjustment and taxes				(70
Comprehensive income				
Cash dividends				
Balance at December 31, 2003	2,566	$256	$89,866	$ 77
Net income				
Exercise of stock options			(90)	
Acquisition of treasury shares				
Effect of reverse one-for-ten stock split	(2,309)	(230)	(233)	
Effect of thirty-for-one stock dividend	7,441	744		
Other comprehensive (loss) net of reclassification adjustment and taxes				(3,37
Comprehensive income				
Cash dividends				
Balance at December 31, 2004	7,698	$770	$89,543	$(2,60

	Retained earnings	Treasury stock	Comprehensive income
Balance at January 1, 2002	$ 11,053	$(4,950)	
Net income	5,597		5,597
Acquisition of treasury shares		(4,422)	
Exercise of stock options		126	
Other comprehensive income net of reclassification adjustment and taxes			1,761
Comprehensive income			$ 7,358

			=======
Cash dividends	(505)		
	--------	-------	
Balance at December 31, 2002	$ 16,145	$(9,246)	
Net income	7,415		7,415
Acquisition of treasury shares		(1,350)	
Exercise of stock options		229	
Other comprehensive (loss) net of reclassification adjustment and taxes			(705)

Comprehensive income			$ 6,710
			=======
Cash dividends	(600)		
	--------	--------	
Balance at December 31, 2003	$ 22,960	$(10,367)	
Net income	7,502		7,502
Exercise of stock options		1,361	
Acquisition of treasury shares		(69)	
Effect of reverse one-for-ten stock split			
Effect of thirty-for-one stock dividend	(744)		
Other comprehensive (loss) net of reclassification adjustment and taxes			(3,377)

Comprehensive income			$ 4,125
			=======
Cash dividends	(735)		
Balance at December 31, 2004	$ 28,983	$ (9,075)	
	========	========	

The accompanying notes are an integral part of these statements

BERKSHIRE BANCORP INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)

	For The Years Ended December		
	2004	2003	
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net income	$ 7,502	$ 7,415	$
Adjustments to reconcile net income to net cash provided by (used in)			

operating activities:		
Realized gains on investment securities	(793)	(4,151)
Net amortization of premiums of investment securities	2,282	1,405
Depreciation and amortization	590	605
Provision for loan losses	180	240
Increase in deferred taxes	--	204
CHANGES IN ASSETS AND LIABILITIES:		
(Increase) in accrued interest receivable	(716)	(1,192)
(Increase) decrease in other assets	(3,873)	(1,064)
Increase (decrease) in accrued interest payable and other liabilities	538	(1,054)
Net cash provided by operating activities	5,710	2,408
CASH FLOWS FROM INVESTING ACTIVITIES:		
Investment securities available for sale		
Purchases	(1,740,889)	(1,837,653)
Sales, maturities and calls	1,674,188	1,641,186
Investment securities held to maturity		
Purchases	91	--
Maturities	--	118
Net decrease (increase) in loans	7,931	(19,221)
Acquisition of premises and equipment	(602)	(294)
Net cash (used in) investing activities	(59,281)	(215,864)

BERKSHIRE BANCORP INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)

	For The Years Ended December	
	2004	2003
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net increase in non interest bearing deposits	3,769	7,102
Net increase in interest bearing deposits	11,864	123,335
Increase (decrease) in securities sold under agreements to repurchase	13,356	67,718
Proceeds from long term debt	37,164	20,046
Repayment of long term debt	(19,304)	--
Proceeds from issuance of		

subordinated debentures, net	14,791	--	
Acquisition of treasury stock	(69)	(1,350)	
Proceeds from exercise of common stock options	1,271	205	
Cash paid for fractional shares	(463)	--	
Dividends paid	(735)	(600)	
Net cash provided by financing activities	61,644	216,456	
Net increase (decrease) in cash and cash equivalents	8,073	3,000	
Cash and cash equivalents at beginning of year	$ 9,310	$ 6,310	$
Cash and cash equivalents at end of year	$ 17,383	$ 9,310	$
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:			
Cash used to pay interest	$ 15,608	$ 14,787	$
Cash used to pay income taxes, net of refunds	$ 5,960	$ 2,015	$

The accompanying notes are an integral part of these statements

BERKSHIRE BANCORP INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
December 31, 2004 and 2003

Note A - ORGANIZATION AND CAPITALIZATION

Organization

Berkshire Bancorp Inc. ("Berkshire" or the "Company" or "we" and similar pronouns), a Delaware corporation, is a bank holding company registered under the Bank Holding Company Act of 1956. Berkshire's principal activity is the ownership and management of its wholly owned subsidiary, The Berkshire Bank (the "Bank"), a New York State chartered commercial bank.

The Bank was established in 1989 to provide highly personalized services to high net worth individuals and to small and mid-sized commercial businesses primarily from the New York City metropolitan area. In March 2001, the Company expanded its customer base and market area with the acquisition of GSB Financial Corporation. The Bank's main office and branch is in mid-town Manhattan. The Bank has one other branch in lower Manhattan, three branches in Brooklyn, New York, and four branches in Orange and Sullivan Counties in New York State.

The Bank competes with other banking and financial institutions in its markets. Commercial banks, savings banks, savings and loan associations, mortgage bankers and brokers, and credit unions actively compete for deposits and loans. Such institutions, as well as consumer finance, mutual funds, insurance companies, and brokerage and investment banking firms may be considered to be competitors of the Bank with respect to one or more of the services provided by the Bank.

The Company and the Bank are subject to the regulations of certain state and federal agencies and, accordingly, are periodically examined by those regulatory authorities. As a consequence of such regulation of banking activities, the Bank's business may be affected by state and federal legislation.

Stock Split and Stock Dividend

At the Annual Meeting of Stockholders held on May 18, 2004, the Company's stockholders approved an amendment to the Company's Certificate of Incorporation effecting a one-for-ten reverse stock split of the Company's issued and outstanding Common Stock (the "Reverse Split"). Following the effectiveness of the Reverse Split, the Company's Board of Directors declared a thirty-for-one forward stock split in the form of a stock dividend in Common Stock (the "Stock Dividend) which became effective immediately. The Company paid approximately $463,000 to purchase fractional shares from stockholders as part of the Reverse Split. The Company's Common Stock began trading on May 19, 2004 giving effect to these transactions.

Trust Preferred Securities

As of May 18 2004, the Company established Berkshire Capital Trust I, a Delaware statutory trust, ("BCTI"). The Company owns all the common capital securities of BCTI. BCTI issued $15.0 million of preferred capital securities to investors in a private transaction and invested the proceeds, combined with the proceeds from the sale of BCTI's common capital securities, in the Company through the purchase of $15.464 million aggregate principal amount of Floating Rate Junior Subordinated Debentures (the "Debentures") issued by the Company. The Debentures, the sole assets of BCTI, mature on July 23, 2034 and bear interest at a floating rate, three month LIBOR plus 2.70%.

Based on current interpretations of the banking regulators, the Debentures qualify under the risk-based capital guidelines of the Federal Reserve as Tier 1 capital, subject to certain limitations. The Debentures are callable by the Company, subject to any required regulatory approvals, at par, in whole or in part, at any time after five years from the date of issuance. The Company's obligations under the Debentures and related documents, taken together, constitute a full, irrevocable and unconditional guarantee on a subordinated basis by the Company of the obligations of BCTI under the preferred capital securities sold by BCTI to investors. FIN46(R) precludes consideration of the

Notes to Consolidated Financial Statements (continued)

Note A - (continued)

call option embedded in the preferred capital securities when determining if the Company has the right to a majority of BCTI expected residual returns. Accordingly, BCTI is not included in the consolidated balance sheet of the Company.

The Federal Reserve has issued guidance on the regulatory capital treatment for the trust-preferred securities issued by BCTI as a result of the adoption of FIN 46(R). This rule would retain the current maximum percentage of total capital permitted for Trust Preferred Securities at 25%, but would enact other changes to the rules governing Trust Preferred Securities that affect their use as part of the collection of entities known as "restricted core capital elements." The rule would take effect March 31, 2009; however, a five year transition period starting March 31, 2004 and leading up to that date would allow bank holding companies to continue to count Trust Preferred Securities as Tier 1 Capital after applying FIN-46(R). Management has evaluated the effects of this rule and does not anticipate a material impact on its capital ratios when the proposed rule is finalized.

Note B - SUMMARY OF ACCOUNTING POLICIES

1. Basis of Financial Statement Presentation

The consolidated financial statements include the accounts of Berkshire Bancorp Inc. and its wholly owned subsidiaries, Greater American Finance Group, Inc. ("GAFG"), East 39, LLC and the Bank, (collectively, the "Company"). All significant intercompany accounts and transactions have been eliminated.

In preparing the financial statements in conformity with accounting principles generally accepted in the United States of America, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the balance sheets, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

The principal estimate that is susceptible to significant change in the near term relates to the allowance for loan losses and goodwill. The evaluation of the adequacy of the allowance for loan losses includes an analysis of the individual loans and overall risk characteristics and size of the different loan portfolios, and takes into consideration current economic and market conditions, the capability of specific borrowers to pay specific loan obligations, as well as current loan collateral values. However, actual losses on specific loans, which also are encompassed in the analysis, may vary from estimated losses.

Substantially all outstanding goodwill resulted from the acquisition of The Berkshire Bank and Goshen Savings Bank, depository institutions concentrating in the New York City and Orange and Sullivan County communities, respectively. As the result of the market penetration in these New York areas, the Company had formulated its own strategy to create such a market role. Accordingly, implicit in the purchase of these franchises was the acquisition of that role. However, if such benefits, including new business, are not derived or the Company changes its business plan an impairment may be recognized.

BERKSHIRE BANCORP INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements (continued)

Note B - (continued)

The Company provides disclosures under Statement of Financial Accounting Standards ("SFAS") 131, "Disclosures About Segments of an Enterprise and Related Information." Operating segments are components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and assess performance. The Company has one operating segment and, accordingly, one reportable segment, "Community Banking." All of the Company's activities are interrelated, and each activity is dependent and assessed based on how each of the activities of the Company supports the others. For example, commercial lending is dependent upon the ability of the Bank to fund itself with retail deposits and other borrowings and to manage interest rate and credit risk. This situation is also similar for consumer and residential mortgage lending. Accordingly, all significant operating decisions are based upon analysis of the Company as one operating segment or unit.

2. Investment Securities

The Company accounts for its investment securities in accordance with SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities". Investments in securities are classified in one of three categories: held to maturity, trading or available for sale. Investments for which management has both the ability and intent to hold to maturity, are carried at cost, adjusted for the amortization of premiums and accretion of discounts computed by the interest method. Investments which management believes may be sold prior to maturity due to changes in interest rates, prepayment risk and equity, liquidity requirements or other factors, are classified as available for sale. Available- for-sale securities are carried at fair value, with the unrealized gains and losses, net of tax, reported as a separate component of stockholders' equity and excluded from the determination of net income. Gains or losses on disposition are based on the net proceeds and cost of the securities sold, adjusted for amortization of premiums and accretion of discounts, using the specific identification method.

In November 2003, the Financial Accounting Standards Board ("FASB") Emerging Issues Task Force ("EITF") reached consensus opinion on EITF Issue 03-1, "The Meaning of Other Than Temporary Impairment and Its Application to Certain Investments. The Company adopted EITF 03-1 as of December 31, 2003. EITF 03-1 includes certain disclosures regarding quantitative and qualitative disclosures for investment securities accounted for under SFAS No. 115 that are impaired at the balance sheet date, but an other-than-temporary impairment has not been recognized. The disclosures under EITF 03-1 are required for financial statements for years ending after December 15, 2003 and are included in these financial statements.

Other-Than-Temporary Impairment - EITF 03-1

In November 2003, the Emerging Issues Task Force (EITF) of the FASB issued EITF Abstract 03-1, "The Meaning of Other-Than-Temporary Impairment and its Application to Certain Investments" (EITF 03-1). The quantitative and qualitative disclosure provisions of EITF 03-1 are effective for years ending after December 15, 2003 and were included in the Company's 2003 Form 10-K. In March 2004, the EITF issued a Consensus on Issue 03-1 requiring that the

provisions of EITF 03-1 be applied for reporting periods beginning after June 15, 2004 to investments accounted for under SFAS Nos. 115 and 124. EITF 03-1 establishes a three-step approach for determining whether an investment is considered impaired, whether that impairment is other-than-temporary, and the measurement of an impairment loss. In September 2004, the FASB issued a proposed Board-directed FASB Staff Position, FSP EITF Issue 03-1-a, "Implementation Guidance for the Application of Paragraph 16 of EITF 03-1." The proposed FSP would provide implementation guidance with respect to debt securities that are impaired solely due to interest rates and/or sector spreads and analyzed for other-than-temporary impairment under paragraph 16 of EITF 03-1. The Board has directed the FASB staff to delay the effective date for the measurement and recognition guidance contained in paragraphs 10-20 of EITF Issue No. 03-1,

Note B - (continued)

including steps two and three of the three-step approach for determining whether an investment is other-than-temporarily impaired. However, step one of that approach must still be initially applied for impairment evaluations in reporting periods beginning after June 15, 2004. The delay of the effective date for paragraphs 10-20 of EITF Issue 03-1 will be superseded with the final issuance of proposed FSP EITF Issue 03-1-a, "Implementation Guidance for the Application of Paragraph 16 of EITF Issue No. 03-1." The Company is in the process of determining the impact that this EITF will have on its financial statements.

3. Loans and Allowance for Loan Losses

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are stated at the amount of unpaid principal and are net of unearned discount, unearned loan fees and an allowance for credit losses. The allowance for loan losses is established through a provision for loan losses charged to expense. Loan principal considered to be uncollectible by management is charged against the allowance for credit losses. The allowance is an amount that management believes will be adequate to absorb losses on existing loans that may become uncollectible based upon an evaluation of known and inherent risks in the loan portfolio. The evaluation takes into consideration such factors as changes in the nature and size of the loan portfolio, overall portfolio quality, specific problem loans, and current economic conditions which may affect the borrowers' ability to pay. The evaluation details historical losses by loan category, the resulting loss rates for which are projected at current loan total amounts.

Interest income is accrued as earned on a simple interest basis. Accrual of interest is discontinued on a loan when management believes, after considering economic and business conditions and collection efforts, that the borrower's financial condition is such that collection of interest is doubtful. When a loan is placed on such non-accrual status, all accumulated accrued interest receivable applicable to periods prior to the current year is charged off to the allowance for loan losses. Interest which had accrued in the current

year is reversed out of current period income. Loans 90 days or more past due and still accruing interest must have both principal and accruing interest adequately secured and must be in the process of collection.

The Company accounts for its impaired loans in accordance with SFAS No. 114, "Accounting by Creditors for Impairment of a Loan," as amended by SFAS No. 118, "Accounting by Creditors for Impairment of a Loan - Income Recognition and Disclosures." This standard requires that a creditor measure impairment based on the present value of expected future cash flows discounted at the loan's effective interest rate, except that as a practical expedient, a creditor may measure impairment based on a loan's observable market price, or the fair value of the collateral if the loan is collateral-dependent. Regardless of the measurement method, a creditor must measure impairment based on the fair value of the collateral when the creditor determines that foreclosure is probable.

The Company follows the provisions of SFAS No. 140 "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities," SFAS No. 140 is based on consistent application of a financial-components approach that recognizes the financial and servicing assets it controls and the liabilities it has incurred, derecognizes financial assets when control has been surrendered and derecognizes liabilities when extinguished. SFAS No. 140 provides consistent guidelines for distinguishing transfers of financial assets from transfers that are secured borrowings. The Company adopted SFAS 140 on April 1, 2001 and the adoption did not have a material impact upon the Company's consolidated financial statements.

Note B - (continued)

Staff Accounting Bulletin (SAB) No. 102, "Selected Loan Loss Allowance Methodology and Documentation Issues" (SAB No. 102), codified in SAB No. 103, provides guidance on the development, documentation, and application of a systematic methodology for determining the allowance for loans and leases in accordance with US GAAP. The adoption of SAB No. 102 is not expected to have a material impact on the Company's financial position or results of operations.

In October 2003, the AICPA issued SOP 03-3 Accounting for Loans or Certain Debt Securities Acquired in a Transfer. SOP 03-3 applies to a loan with the evidence of deterioration of credit quality since origination acquired by completion of a transfer for which it is probable at acquisition, that the Company will be unable to collect all contractually required payments receivable. SOP 03-3 requires that the Company recognize the excess of all cash flows expected at acquisition over the investor's initial investment in the loan as interest income on a level-yield basis over the life of the loan as the accretable yield. The loan's contractual required payments receivable in excess of the amount of its cash flows excepted at acquisition (nonaccretable difference) should not be recognized as an adjustment to yield, a loss accrual or a valuation allowance for credit risk. SOP 03-3 is effective for loans acquired in fiscal years beginning after December 31, 2004. Early adoption is permitted. Management is currently evaluating the provisions of SOP 03-3.

Loan Commitments Accounted for as Derivative Instruments

The SEC staff recently released Staff Accounting Bulletin (SAB) 105, "Loan Commitments Accounted for as Derivative Instruments." SAB 105 provides guidance about the measurement of loan commitments recognized at fair value under FASB Statement No. 133, Accounting for Derivative Instruments and Hedging Activities. SAB 105 also requires companies to disclose their accounting policy for those loan commitments including methods and assumptions used to estimate fair value and associated hedging strategies. SAB 105 is effective for all loan commitments accounted for as derivatives that are entered into after March 31, 2004. The adoption of SAB 105 did not have a material effect on our consolidated financial statements.

The Company adopted SFAS No. 149 ("SFAS No. 149"), Amendment of SFAS No. 133 on Derivative Instruments and Hedging Activities, on July 1, 2003. SFAS No. 149 clarifies and amends SFAS No. 133 for implementation issues raised by constituents or includes the conclusions reached by the FASB on certain FASB Staff Implementation Issues. Statement No. 149 also amends SFAS No. 133 to require a lender to account for loan commitments related to mortgage loans that will be held for sale as derivatives. SFAS No. 149 is effective for contracts entered into or modified after September 30, 2003. The Company periodically enters into commitments with its customers, which it intends to sell in the future. The adoption of SFAS No. 149 did not have a material impact on the Company's financial position or results of operations.

4. Bank Premises and Equipment

Bank premises and equipment, including leasehold improvements, are stated at cost less accumulated depreciation. Depreciation expense is computed on the straight-line method over the estimated useful lives of the assets. Leasehold improvements are amortized over the shorter of the estimated useful lives of the improvements or the terms of the related leases.

On January 1, 2002 the Company adopted SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." SFAS No. 144 retains the existing requirements to recognize and measure the impairment of long-lived assets to be held and used or to be disposed of by sale. However, SFAS No. 144 makes changes to the scope and certain measurement requirements of existing accounting guidance. The adoption of this statement did not have a significant impact on the financial condition or results of operations of the Company.

Note B - (continued)

5. Other Real Estate Owned

Other real estate owned, representing property acquired through foreclosure, is recorded at the lower of cost or estimated fair market value, less costs of disposal. When property is acquired, the excess, if any, of the

loan balance over fair market value is charged to the allowance for loan losses. Periodically thereafter, the asset is reviewed for subsequent declines in the estimated fair market value. Subsequent declines, if any, and holding costs, as well as gains and losses on subsequent sale, are included in the consolidated statements of operations.

6. Goodwill

Goodwill resulted from the acquisition of The Berkshire Bank in 1999 and GSB Financial Corporation in 2001. The Company adopted SFAS No. 142, Goodwill and Intangible Assets, on January 1, 2002. SFAS No. 142 includes requirements to test goodwill and indefinite lived intangible assets for impairment rather than amortize them. The Company did not identify any impairment on its outstanding goodwill and its identifiable intangible assets from its most recent testing, performed at December 31, 2004.

7. Income Taxes

The Company accounts for income taxes under the liability method of accounting for income taxes. Deferred tax assets and liabilities are determined based on the difference between the financial statement and tax bases of assets and liabilities as measured by the enacted tax rates that will be in effect when these differences reverse. Deferred tax expense is the result of changes in deferred tax assets and liabilities. The principal types of differences between assets and liabilities for financial statement and tax return purposes are allowance for loan losses, deferred loan fees, deferred compensation and securities available for sale.

8. Net Income Per Share

The Company follows the provisions of SFAS No. 128, "Earnings Per Share." Basic earnings per share excludes dilution and is computed by dividing income available to common shareholders by the weighted-average common shares outstanding during the period. Diluted earnings per share takes into account the potential dilution that could occur if securities or other contracts to issue common stock were exercised and converted into common stock. All weighted average share and per share information in 2003 and 2002 have been retroactively restated to reflect the stock split and stock dividend discussed in Note A.

9. Stock Based Compensation

In December 2004, the Financial Accounting Standards Board (the "FASB") issued Statement No. 123 (Revised), Share-based Payment, ("FAS 123(R)"). FAS 123(R) requires that the compensation cost relating to share-based payment transactions be recognized in financial statements. That cost will be measured based on the fair value of the equity or liability instruments issued. We will be required to apply FAS 123(R) in the third quarter of 2005. The scope of FAS 123(R) includes a wide range of share-based compensation arrangements including share options, restricted share plans, performance-based awards, share appreciation rights and employee share purchase plans. FAS 123(R) replaces FASB Statement 123, Accounting for Stock-Based Compensation ("FAS 123"), and supersedes APB Opinion No. 25, Accounting for Stock Issued to Employees. FAS 123, as originally issued in 1995, established as preferable a fair-value-based method of accounting for share-based payment transactions with employees. However, FAS 123 permitted entities the option of continuing to apply the guidance in APB Opinion No. 25, as long as the footnotes to financial statements disclosed what net income would have been had the had the preferable fair-value-based method been used.

BERKSHIRE BANCORP INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements (continued)

Note B - (continued)

The Company follows the disclosure provisions of FAS 123 which introduced a method of accounting for employee stock-based compensation plans based upon the fair value of the awards on the date they are granted. Under this fair-value- based method, public companies estimate the fair value of stock options using a pricing model, such as the Black-Scholes model, which requires inputs such as the expected volatility of the stock price and an estimate of the dividend yield over the option's expected life. The FASB, however, does not require the use of this method until the first quarter of our 2006 fiscal year. Entities that continue to account for stock option plans under the existing method (APB No. 25) are required to disclose proforma net income and earnings per share, as if the fair value method had been used.

At December 31, 2004, the Company has one stock-based employee compensation plan, which is more fully described in Note K. The Company accounts for that plan under the recognition and measurement principles of APB No. 25, "Accounting for Stock Issued to Employees," and related interpretations. Stock-based employee compensation costs are not reflected in net income, as all options granted under the plan had an exercise price equal to the market value of the underlying common stock on the date of the grant. The following table illustrates the effect on net income and earnings per share if the Company had applied the fair value recognition provisions of SFAS No. 123, "Accounting for Stock-Based Compensation," to stock-based employee compensation.

		For The Years Ended December 31,		
		2004	2003	2002
		(In thousands, except per share amounts)		
Net income	As Reported:	$ 7,502	$ 7,415	$ 5,597
Less: Stock based compensation costs determined under fair value methods for all awards		--	32	680
	Pro Forma:	$ 7,502	$ 7,383	$ 4,917
Basic earnings per share	As Reported:	$ 1.12	$ 1.12	$ .81
	Pro Forma:	1.12	1.11	.72
Diluted earnings per share	As Reported:	1.10	1.10	.81
	Pro Forma:	1.10	1.09	.71

The fair value of each option is estimated on the date of grant using the Black-Scholes options-pricing model using weighted-average assumptions for

expected volatility, risk-free interest and expected life of the option. The Company did not grant stock options in 2004, 2003 and 2002.

10. Cash Equivalents

The Company considers all highly liquid debt investments purchased with an original maturity of three months or less, and amounts due from brokers to be cash equivalents.

11. Restrictions on Cash and Due From Banks

The Bank is required to maintain reserves against customer demand deposits by keeping cash on hand or balances with the Federal Reserve Bank in a non-interest bearing account. The amounts of those reserve and cash balances was approximately $2,763,000, $1,032,000 and $1,155,000 at December 31, 2004, 2003 and 2002, respectively.

BERKSHIRE BANCORP INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements (continued)

Note B - (continued)

12. Comprehensive Income

The Company follows the provisions of SFAS No. 130, "Reporting Comprehensive Income" which includes net income as well as certain other items, which results in a change to equity during the period. (In thousands.)

	Year Ended December 31, 2004		
	Before tax amount	Tax (expense) benefit	N
Unrealized gains (losses) on investment securities:			
Unrealized holding gains arising during period	$ (4,014)	$ 1,711	
Less reclassification adjustment for gains realized in net income	793	(317)	
Unrealized (loss) on investment securities	(4,807)	2,028	
Change in minimum pension liability	(598)		
Other comprehensive income (loss), net	$ (5,405)	$ 2,028	

Year Ended December 31, 2003

	Before tax amount	Tax (expense) benefit	Ne
Unrealized gains (losses) on investment securities:			
Unrealized holding gains arising during period	$ 1,231	$ (491)	
Less reclassification adjustment for gains realized in net income	2,746	(1,097)	
Unrealized (loss) on investment securities	(1,515)	606	
Change in minimum pension liability	340	(136)	
Other comprehensive income (loss), net	$ (1,175)	$ 470	

	Year Ended December 31, 2002		
	Before tax amount	Tax (expense) benefit	Net A
Unrealized gains on investment securities:			
Unrealized holding gains arising during period	$ 4,760	$ (1,872)	
Less reclassification adjustment for gains realized in net income	1,539	(616)	
Unrealized gain on investment securities	3,221	(1,256)	
Minimum pension liability	(340)	136	
Other comprehensive income, net	$ 2,881	$ (1,120)	

13. Reclassifications

Certain amounts in the December 31, 2003 and 2002 financial statements have been reclassified to conform to the current period's presentation.

BERKSHIRE BANCORP INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements (continued)

Note C - INVESTMENT SECURITIES

The following is a summary of held to maturity investment securities:

	December 31, 2004			
	Amortized Cost	Gross unrealized gains	Gross unrealized losses	v
	(In thousands)			
Investment securities				
U.S. Government Agencies	$ 624	$ 10	$ (1)	$
Totals	$ 624	$ 10	$ (1)	$

	December 31, 2004			
	Amortized Cost	Gross unrealized gains	Gross unrealized losses	v
	(In thousands)			
Investment securities				
U.S. Government Agencies	$ 711	$ 4	$ --	$
Totals	$ 711	$ 4	$ --	$

The following is a summary of available-for-sale investment securities:

	December 31, 2004			
	Amortized Cost	Gross unrealized gains	Gross unrealized losses	v
	(In thousands)			
Investment securities				
U.S. Treasury and Notes	$ 24,896	$ --	$ (174)	$ 2
U.S. Government Agencies	471,018	97	(3,844)	46
Mortgage-backed securities	109,822	504	(996)	10
Corporate notes	21,089	692	(154)	2
Municipal securities	1,307	134	--	
Marketable equity securities and other	6,363	279	(65)	
Totals	$634,495	$ 1,706	$(5,233)	$63

BERKSHIRE BANCORP INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements (continued)

Note C - (continued)

	December 31, 2004			
	Amortized Cost	Gross unrealized gains	Gross unrealized losses	v
	(In thousands)			
Investment securities				
U.S. Treasury and Notes	$ 39,941	$ --	$ (94)	$ 3
U.S. Government Agencies	419,175	637	(3,059)	41
Mortgage-backed securities	93,875	3,838	(265)	9
Corporate notes	1,570	214	(122)	
Municipal securities	991	70	--	
Marketable equity securities and other	12,305	177	(116)	1
Totals	$567,857	$ 4,936	$(3,656)	$56

The Company has investments in certain debt and equity securities that have unrealized losses or may be otherwise impaired, but an other-than-temporary impairment has not been recognized in the financial statements. The following table indicates the length of time individual securities have been in a continuous unrealized loss position at December 31, 2004 (in thousands):

	Less than 12 months		12 months or longer	
Description of Securities	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. Treasury and Notes	$ 14,796	$ 132	$ 9,926	$ 42
U.S. Government Agencies	253,526	1,586	192,661	2,259
Mortgage-backed securities	73,271	897	8,924	99
Corporate notes	4,941	58	--	96
Municipal securities	--	--	--	--
Subtotal, debt securities	346,534	2,673	211,511	2,496
Marketable equity	--	--	78	65
securities and other				
Total temporarily impaired securities	$346,534	$ 2,673	$211,589	$ 2,561

The Company had a total of 97 debt securities with a fair market value of $558.05 million which were temporarily impaired at December 31, 2004. The total unrealized loss on these securities was $5.17 million, all but $96,000 of such unrealized loss being attributable to interest rate movements. We have the

ability to hold these securities, all but 2 of which are US Government and US Government Agency securities to maturity, therefore, the unrealized losses associated with these securities are not considered to be other than temporary.

We also had 4 equity securities with an aggregated fair market value of $78,000 which were temporarily impaired at December 31, 2004. The total unrealized loss on these securities was $65,000. Based upon our review of the available information, such unrealized losses are not considered to be other than temporary.

BERKSHIRE BANCORP INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements (continued)

NOTE C - (continued)

The amortized cost and fair value of investment securities available for sale and held to maturity, by contractual maturity, at December 31, 2004 and 2003 are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	December 31, 2004		
	Available for Sale		Held
	Amortized Cost	Fair Value	Amortized Cost
	(In thousands)		
Due in one year or less	$ 24,941	$ 24,862	$ --
Due after one through five years	185,421	184,416	58
Due after five through ten years	211,919	209,806	93
Due after ten years	198,440	197,192	473
Marketable equity securities and other	13,774	14,692	--
Totals	$634,495	$630,968	$ 624

	December 31, 2003		
	Available for Sale		Held
	Amortized Cost	Fair Value	Amortized Cost
	(In thousands)		

Due in one year or less	$ --	$ --	$ --
Due after one through five years	102,626	102,654	74
Due after five through ten years	196,934	195,168	70
Due after ten years	255,992	258,949	567
Marketable equity securities and other	12,305	12,366	--
Totals	$567,857	$569,137	$ 711

Gross gains realized on the sales of investment securities for the years ended December 31, 2004, 2003 and 2002 were $965,000, $2.91 million and $1.54 million, respectively. Gross losses were $172,000 and $163,000 for the years ended December 31, 2004 and 2003. Gross losses were not material for the year ended December 31, 2002.

As of December 31, 2004 and 2003, securities sold under agreements to repurchase with a book value of approximately $127.75 million and $114.39 million, respectively, were outstanding. As of December 31, 2004 and 2003, the Company did not have any investment securities of any one issuer where the carrying value exceeded 10% of shareholders' equity.

On November 7, 2002, we sold our 24.9% interest in a merchant credit card processing company for $285,000, which represents our initial purchase price in December 1999. We accounted for our interest in this company under the equity method of accounting and have recorded approximately $200,000 in net losses since December 1999. In addition, the Bank had loans outstanding totaling $295,000 to this company which are being repaid as a result of this transaction. At December 31, 2003, the purchase price to Berkshire had been paid in full.

NOTE D - LOANS

Major classifications of loans are as follows:

	December 31, 2004	December 31, 2003
	(In thousands)	
Commercial and professional loans	$ 16,498	$ 22,228
Secured by real estate		
1 - 4 family	155,079	169,589
Multi family	4,600	6,608

Non-residential	109,597	94,956
Consumer	1,989	2,239
	287,763	295,620
Deferred loan fees	(784)	(864)
Allowance for loan losses	(2,927)	(2,593)
	$284,052	$292,163

Changes in the allowance for loan losses are as follows:

	For The Years Ended December 31,		
	2004	2003	2002
	(In thousands)		
Balance at beginning of year	$ 2,593	$ 2,315	$ 2,030
Provision charged to operations	180	240	387
Loans charged off	24	17	199
Recoveries	178	55	97
Balance at end of year	$ 2,927	$ 2,593	$ 2,315

The Company had $343,000, $109,000 and $59,000 non accrual loans as of December 31, 2004, 2003 and 2002, respectively, and $50,000 of loans delinquent more than ninety days and still accruing interest at December 31, 2004. The Company did not have any impaired loans or loans past due more than 90 days and still accruing interest as of December 31, 2003 and 2002.

The Company, from time to time, enters into lending transactions in the ordinary course of business with directors, executive officers, principal stockholders and affiliates of such persons on the same terms as those prevailing for comparable transactions with other borrowers. At December 31, 2004, loans to these related parties amounted to $10.4 million, were current as to principal and interest payments, and do not involve more than normal risk of collectibility. An analysis of activity in loans to related parties at December 31, 2004, resulted in new loans of $5.7 million and repayments of approximately $5.7 million.

NOTE E - PREMISES AND EQUIPMENT

Major classifications of premises and equipment are summarized as follows:

	Estimated useful lives	December 31, 2004	December 2003
		(In thousands)	
Land	Indefinite	$ 3,817	$ 3,
Buildings	39 years	4,059	4,
Furniture and equipment	3 to 10 years	2,573	2,
Leasehold improvements	2 to 10 years	968	
		11,417	10,
Accumulated depreciation and amortization		(2,740)	(2,
Total		$ 8,677	$ 8,

Depreciation and amortization expense was approximately $591,000, $605,000 and $279,000 for the years ended December 31, 2004, 2003 and 2002, respectively.

NOTE F - DEPOSITS

The aggregate amount of jumbo certificates of deposits greater than $100,000 were approximately $109.74 million and $110.08 million as of December 31, 2004 and 2003, respectively.

The scheduled maturities of all certificates of deposit are as follows:

	December 31, 2004
	(In thousands)
2005	$218,680
2006	51,673
2007	1,877
2008	2,026
2009	53
	$ 274,309

NOTE G - BORROWINGS

Short-Term Borrowings Securities sold under agreements to repurchase generally mature within 30 days from the date of the transactions. Short-term borrowings consist of various borrowings which generally have maturities of less than one year. The details of these categories are presented below:

Year Ended December 31,

	2004	2003
	(Dollars in Thousands)	
Securities sold under repurchase agreements and federal funds purchased		
Balance at year-end	$127,747	$114,391
Average during the year	$129,794	$ 57,554
Maximum month-end balance	$148,753	$114,391
Weighted average rate during the year	1.87%	1.68%
Rate at December 31	2.27%	1.73%

BERKSHIRE BANCORP INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements (continued)

Note G - (continued)

Long-Term Borrowings At December 31, 2004, advances from the Federal Home Loan Bank ("FHLB") totaling $95.6 million will mature within one to ten years and are reported as long-term borrowings. The advances are collateralized by FHLB stock and certain first mortgage loans. The advances had a weighted average rate of 3.83%. Unused lines of credit at the FHLB were $46.5 million at December 31, 2004.

Outstanding long-term borrowings mature as follows (in thousands):

Year	Amount
2005	$ 2,638
2006	8,719
2007	34,578
2008	19,976
2009	15,694
Thereafter	14,000
Total	$ 95,605

NOTE H - EARNINGS PER SHARE

The Company's calculation of earnings per share in accordance with SFAS No. 128 is as follows:

	Year Ended December 31, 2004 (In thousands, except per share data)		
	Income (numerator)	Shares (denominator)	Per share amount

Basic earnings per share			
Net income available to common stockholders	$ 7,502	6,672	$ 1.12
Effect of dilutive securities			
Options	--	176	(.02)
Diluted earnings per share			
Net income available to common stockholders plus assumed conversions	$ 7,502	6,848	$ 1.10

	Year Ended December 31, 2003 (In thousands, except per share data)		
	Income (numerator)	Shares (denominator)	Per share amount
Basic earnings per share			
Net income available to common stockholders	$ 7,415	6,636	$ 1.12
Effect of dilutive securities			
Options	--	111	(.02)
Diluted earnings per share			
Net income available to common stockholders plus assumed conversions	$ 7,415	6,747	$ 1.10

BERKSHIRE BANCORP INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements (continued)

NOTE H - (continued)

	Year Ended December 31, 2002 (In thousands, except per share data)		
	Income (numerator)	Shares (denominator)	Per share amount
Basic earnings per share			
Net income available to common stockholders	$ 5,597	6,876	$ .81

Effect of dilutive securities			
Options	--	33	.--
Diluted earnings per share			
Net income available to common stockholders plus assumed conversions	$ 5,597	6,909	$ .81

Options to purchase 115,375 shares of common stock for $30.00 to $38.00 per share were outstanding during the year ended December 31, 2002. These options were not included in the computation of diluted earnings per share because the option exercise price was greater than the average market price for the Company's common stock during this period.

NOTE I - INCOME TAXES

The components of income tax expense are as follows:

	Years Ended December 31,		
	2004	2003	2002
Current	$ 6,515,000	$ 5,848,000	$ 4,216,000
Deferred Taxes (Benefit)	(381,000)	(204,000)	133,000
	$ 6,134,000	$ 5,644,000	$ 4,349,000

A reconciliation of the provision for income taxes for the years ended December 31, 2004, 2003 and 2002 and the amount computed by applying the statutory Federal income tax rate to income from continuing operations follows:

	Years Ended December 31,		
	2004	2003	2002
Effective Tax Reconciliation			
Tax at statutory rate	$ 4,636,000	$ 4,439,000	$ 3,381,000
State and City, net of federal income tax benefit	1,423,000	1,211,000	940,000
Tax exempt income	--	(76,000)	(53,000)
Other	75,000	70,000	81,000
Actual provision for income taxes	$ 6,134,000	$ 5,644,000	$ 4,349,000

BERKSHIRE BANCORP INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements (continued)

Note I - (continued)

The tax effect of the principal temporary differences at December 31, 2004 and 2003 are as follows:

	December 31, 2004	December 31, 2003
Net deferred tax assets		
Loan loss provision	$1,359,000	1,215,000
Depreciation	92,000	9,000
Other	234,000	80,000
Unrealized (gain) loss on investment securities	1,528,000	(500,000)
Net deferred tax asset included in other assets	$3,213,000	$ 804,000

NOTE J - STOCK PLANS

In March 1999, the stockholder's of the Company approved the 1999 Stock Incentive Plan (the "1999 Stock Incentive Plan"). The 1999 Stock Incentive Plan permits the granting of awards in the form of nonqualified stock options, incentive stock options, restricted stock, deferred stock, and other stock-based incentives. Up to 600,000 shares of common stock of the Company may be issued pursuant to the 1999 Stock Incentive Plan. Officers, directors and other key employees of the Company or any subsidiary are eligible to receive awards under the 1999 Stock Incentive Plan. Options outstanding under the 1999 Stock Incentive Plan were 314,250 and 337,125 as of December 31, 2004 and 2003, respectively. As of December 31, 2004 and 2003, 50,834 options and 171,294 options, respectively, were also outstanding as a result of the GSB acquisition. The Company did not grant options in 2004, 2003 and 2002.

A summary of activity with respect to the Stock Option Plan follows:

	December 31, 2004		December 31, 2003		December 31, 2
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price	Shares
Outstanding at beginning of	508,419	$10.12	532,503	$10.10	574,788

year					
Granted	--	$ --	--	$ --	--
Cancelled	(1,500)	$10.00	--	$ --	(19,527)
Exercised	(141,835)	$ 8.95	(24,084)	$ 8.61	(22,758)
Outstanding at end of year	365,084	$10.65	508,419	$10.12	532,503
Exercisable at end of year	365,084	$10.65	497,394	$10.16	502,500
Weighted average fair value of options granted during the year		$ --		$ --	

BERKSHIRE BANCORP INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements (continued)

Note J - (continued)

The following table summarizes information about options outstanding at December 31, 2004:

	Options Outstanding			Option
Range of exercise prices	Number outstanding at December 31, 2004	Weighted average remaining contractual life (years)	Weighted average exercise price	Number outstanding at December 31, 2004
$ 5.98 - 8.78	50,834	3.21	$ 8.53	50,834
10.00 - 12.67	314,250	1.53	10.99	314,250
	365,084			365,084

NOTE K - EMPLOYEE BENEFIT PLANS

1. Retirement Income Plan

The Company has a Retirement Income Plan (the "Retirement Plan"), a noncontributory plan covering substantially all full-time, non-union United

States employees of the Company. Benefits were based upon a combination of employee compensation and years of service. The Company paid the entire cost of the plan for its employees and funded such costs as they accrued. The Company's funding policy was to make annual contributions within minimum and maximum levels required by applicable regulations. The Company's customary contributions were designed to fund normal cost on a current basis and fund over 30 years the estimated prior service cost of benefit improvements (15 years of annual gains and losses). The projected unit cost method was used to determine the annual cost.

Benefit accruals were frozen as of September 15, 1988, resulting in a plan curtailment. As a result of such curtailment, the Company did not accrue benefits for future services; however, the Company did continue to contribute as necessary for any unfunded liabilities. In 2000, the Company reinstated the Retirement Plan to cover substantially all full-time, non-union United States employees of the Company.

The following table summarizes the major categories of Plan assets as of the dates indicated:

	December 31,			
	2004		2003	
	Fair Value	% of Total	Fair Value	%
	(In thousands, except percentages			
Mutual Funds				
International Equity Fund	$ 120	6.64%	$ 127	
Large Cap Equity Growth Fund	793	43.94	831	
International Investment Grade Bond Fund	550	30.47	570	
Small Cap Equity Growth Fund	118	6.54	122	
Corporate Common Stocks(1)	216	11.97	157	
Cash and cash equivalents	8	0.44	9	
Total Plan Assets	$ 1,805	100.00%	$ 1,816	

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(1) Includes 4,500 shares of the Company's Common Stock with a market value of $92,250 and $75,000 at December 31, 2004 and 2003, respectively.

BERKSHIRE BANCORP INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements (continued)

Note K - (continued)

The assets of the plan are primarily invested in well diversified common stock and fixed income funds designed to minimize risk while maximizing expected portfolio returns. To achieve the long term rate of return, plan assets will be invested in a mixture of instruments, including but not limited to, corporate common stock, investment grade bond funds, small and large cap equity funds and international equity funds. The allocation of assets will be determined by the Investment Manager, and will typically include 50% to 70% equities, with the remainder invested in fixed income and a minimal amount of cash. Presently, this diversified portfolio is expected to return approximately 8.50% in the long run.

The expected rate of return on plan assets was determined based upon a review of historical returns, both for our Retirement Plan and for medium to large-sized defined benefit pension funds with similar asset allocations. This review generated separate expected future long-term returns for each asset class listed in the above table. These expected future returns were then blended based upon our plan's target asset allocation.

Assumptions

Weighted-average assumptions used to determine benefit obligations were as follows at the dates indicated:

	December 31,	
	2004	2003
Discount rate	5.75%	6.60%
Rate of compensation increase	5.00%	5.00%

Weighted-average assumptions used to determine net periodic benefit cost for the years ended December 31, 2004 and 2003 were as follows:

	December 31,	
	2004	2003
Discount rate	6.60%	7.25%
Rate of compensation increase	5.00%	5.00%
Expected return on plan assets	8.50%	8.50%
Measurement date	1/1/2004	1/1/2003

A summary of the components of net periodic pension cost for the years ended December 31, 2004, 2003 and 2002 is as follows:

	December 31,		
	2004	2003	2002
Service cost-benefits earned during the period	$ 243,916	$ 195,162	$ 48,883
Interest cost on projected benefit obligation	121,005	107,211	98,897
Expected return on plan assets	(150,145)	(123,482)	(148,973)
Net amortization and deferral	37,428	43,208	18,370

Net pension cost of defined benefit plan	$ 252,204	$ 222,099	$ 17,177

BERKSHIRE BANCORP INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements (continued)

NOTE K - (continued)

The following table sets forth the funded status and amounts recognized in the Company's balance sheet for its defined benefit plan at December 31, 2004 and 2003:

	December 31,	
	2004	2003
Actuarial present value of vested accumulated benefit obligations	$ 2,316,075	$ 1,807,366
Actuarial present value of accumulated benefit obligations	2,316,075	1,814,032
Projected benefit obligations	$(2,316,075)	$(1,814,032)
Fair value of plan assets	1,804,866	1,815,905
Excess of projected benefit obligation over fair value of plan assets	(511,209)	1,873
Unrecognized prior service cost	139,244	157,614
Unrecognized net loss	597,925	318,677
Prepaid pension cost, included in other assets	$ 225,960	$ 478,164

Estimated Future Benefit Payments

We estimate future benefit payments to be as follows:

Years	Benefit Payments
2005	139,230
2006	144,405
2007	176,105
2008	161,432
2009	263,881

Years 2010-2014	1,042,795

Company Contributions

During the fiscal year ending December 31, 2005, the Company expects to contribute approximately $58,000 to its Retirement Plan.

BERKSHIRE BANCORP INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements (continued)

NOTE K - (continued)

2. Former Goshen Bank Pension Plan

The Bank, as successor to Goshen Bank, had a non-contributory defined benefit pension plan covering substantially all of its employees. In the fourth quarter of 2000, the Goshen Bank froze its defined benefit pension plan and provided that there would be no further accruals under the plan. On October 24, 2002, the Board of Directors of the Bank approved the termination of this plan. In 2003, we paid out approximately $600,000 to complete the termination of this plan and purchase annuity contracts. Upon the notice of termination, all participant benefits vest 100%.

	December 31, 2002
Change in benefit obligation	(In thousands)
Benefit obligation at beginning of year	$ 1,193
Service cost	--
Interest cost	84
Actual loss	85
Benefits paid	(91)
Benefits obligations at end of year	1,271
Change in plan assets	
Fair value of plan assets at beginning of year	1,309
Actual return on plan assets	(917)
Employer contribution	--
Benefits paid	(91)
Fair value of plan assets at end of year	1,127
Funded status	(144)
Unrecognized net actuarial loss	340
Prepaid benefit cost (included in other assets)	$ 196

Net pension cost included the following components:

	Year Ended December 31,		
	2004	2003	2002
	(In thousands)		
Service cost	$ --	$ --	$ --
Interest cost on projected benefit obligation	--	--	84
Expected return on plan assets	--	--	(88)
Purchase accounting change	--	--	--
Net periodic benefit cost	$ --	$ --	$ 4

The assumed discount rate and rate of increase in future compensation levels used in determining the actuarial present value of the projected benefit obligation was 7.25% in 2002.

BERKSHIRE BANCORP INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements (continued)

NOTE K - (continued)

3. Postretirement Welfare Plan

In addition to pension benefits, the Bank, as successor to Goshen Bank provides certain health care and life insurance benefits for retired employees and their spouses. The postretirement health care and life insurance benefits plan was terminated for persons retiring after December 31, 1998. Eligible employees retired on or before that date will have benefits paid through the plan under the agreed upon terms existing at the employee's retirement date.

	December 31,	
	2004	2003
	(In thousands)	
Change in benefit obligation		
Benefit obligation at beginning of year	$ 715	$ 718
Service cost	--	--
Interest cost	43	47
Actual loss	10	2
Benefits paid	(49)	(52)
Benefits obligation at end of year	719	715

Change in plan assets		
Fair value of plan assets at beginning of year	--	--
Actual return on plan assets	--	--
Employer contribution	49	52
Benefits paid	(49)	(52)
Fair value of plan assets at end of year	--	--
Funded status	(719)	(715)
Unrecognized net actuarial loss	25	15
Accrued benefit cost (included in other liabilities)	$ 694	$ 700

Net benefit cost included the following components:

	Year Ended December 31,	
	2004	2003
	(In thousands)	
Service cost	$ --	$ --
Interest cost on projected benefit obligation	43	47
Actual return on plan assets	--	--
Net periodic benefit cost	$ 43	$ 47

The assumed discount rate used in determining the actuarial present value of the projected benefit obligation was 6.125% and 6.75% in 2004 and 2003, respectively.

NOTE K - (continued)

4. 401(k) Plans

The Bank has a 401(k) plan in which employees can contribute up to 15% of their salary. The Bank also matches 50% of the employee contribution up to a maximum of 3% of the employee's salary. The matching expense was $89,000, $76,000 and $105,000 for the years ended December 31, 2004, 2003 and 2002,

respectively.

5. Deferred Compensation Arrangements

GSB Financial and Goshen Bank established deferred compensation arrangements for certain directors and executives. These deferred compensation arrangements were terminated as a result of the acquisition. At December 31, 2004 and 2003, the balance accumulated under these arrangements was approximately $241,000 and will be paid out when the individual (i) ceases to be a director and/or executive of the Company; (ii) attains the age of 75; or (iii) specifies a particular date.

NOTE L - COMMITMENTS AND CONTINGENCIES

1. Leases and Other Commitments

The Company leases certain of its operating facilities under non-cancelable operating leases expiring in 2005 through 2012. The leases require payment by the Company of the real estate taxes and insurance on the leased properties. Approximate future minimum annual rental payments are as follows:

Year Ending December 31,	(In thousands)
2005	$ 712
2006	713
2007	727
2008	537
2009	475
Thereafter	531
	$ 3,695

Rental expense was approximately $964,000, $699,000 and $811,000 for the fiscal years ended December 31, 2004, 2003 and 2002, respectively. Included in rental expense was approximately $298,000, $270,000 and $255,000 for the fiscal years ended December 31, 2004, 2003 and 2002, respectively, which was paid to a company affiliated with a director of the Company.

NOTE M - FAIR VALUE OF FINANCIAL INSTRUMENTS

SFAS No. 107 requires disclosure of the estimated fair value of an entity's assets and liabilities considered to be financial instruments. For the Company, as for most financial institutions, the majority of its assets and liabilities are considered financial instruments as defined in SFAS No. 107. However, many such instruments lack an available trading market, as characterized by a willing buyer and seller engaging in an exchange transaction. Also, it is the Company's general practice and intent to hold its financial instruments to maturity and not to engage in trading or sales activities, except for certain loans. Therefore, the Company had to use significant estimations and present value calculations to prepare this disclosure.

BERKSHIRE BANCORP INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements (continued)

Note M - (continued)

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

Estimated fair values have been determined by the Company using the best available data and an estimation methodology suitable for each category of financial instruments. The estimation methodologies used, the estimated fair values, and recorded book balances at December 31, 2004 and 2003 are outlined below.

For cash and cash equivalents, the recorded book values of $17.38 million and $9.31 million at December 31, 2004 and 2003, respectively, approximate fair values. The estimated fair values of investment securities are based on quoted market prices, if available. Estimated fair values are based on quoted market prices of comparable instruments if quoted market prices are not available.

	December 31,		
	2004		2003
	Carrying amount	Estimated fair value	Carrying amount
	(In thousands)		
Investment securities	$631,592	$631,601	$569,848
Loans, net of unearned income	286,979	291,460	294,756
Time Deposits	274,309	273,397	317,480
Repurchase Agreements	127,747	127,442	114,391
Long-term Debt	111,069	112,598	77,745

The net loan portfolio at December 31, 2004 and 2003 has been valued using a present value discounted cash flow where market prices were not available. The discount rate used in these calculations is the estimated current market rate adjusted for credit risk. The carrying value of accrued interest approximates fair value.

The estimated fair values of demand deposits (i.e. interest (checking) and non-interest bearing demand accounts, savings and certain types of money market accounts) are, by definition, equal to the amount payable on demand at the reporting date (i.e. their carrying amounts). The carrying amount of accrued interest payable approximates its fair value.

The fair value of commitments to extend credit is estimated based upon the amount of unamortized deferred loan commitment fees. The fair value of letters of credit is based upon the amount of unearned fees plus the estimated cost to terminate letters of credit. Fair values of unrecognized financial

instruments, including commitments to extend credit, and the fair value of letters of credit are considered immaterial.

The fair value of interest rate caps are based upon the estimated amount the Company would receive or pay to terminate the contracts or agreements, taking into account current interest rates and, when appropriate, the current creditworthiness of the counterparties. The aggregate fair value for the interest rate caps were approximately $132,000 and $180,000 at December 31, 2004 and 2003, respectively.

NOTE N - FINANCIAL INSTRUMENTS WITH OFF-BALANCE-SHEET RISK AND CONCENTRATIONS OF CREDIT RISK

The Bank is party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of their customers. These financial instruments include commitments to extend credit and standby letters of credit. Such financial instruments are recorded in the financial statements when they become payable. Those instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the consolidated balance sheets. The contract or notional amounts of those instruments reflect the extent of involvement the Banks have in particular classes of financial instruments.

The Bank's exposure to credit loss in the event of non-performance by the other party to the financial instrument for commitments to extend credit and standby letters of credit is represented by the contractual or notional amount of those instruments. The Bank uses the same credit policies in making commitments and conditional obligations as they do for on-balance-sheet instruments.

Unless noted otherwise, the Bank does not require collateral or other security to support financial instruments with credit risk. The approximate contract amounts are as follows:

	December 31,	
	2004	2003
	(In thousands)	
Unused lines of credit	$ 15,859	$ 11,243
Commitments to extend credit	--	2,011
Standby letters of credit and financial guarantees written	750	775
	$ 16,609	$ 14,029
Interest rate caps-notional amount	$ 25,000	$ 30,000

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The 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.

Standby letters of credit are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. Those guarantees are primarily issued to support public and private borrowing arrangements, including commercial paper, bond financing and similar transactions. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. The Bank holds residential or commercial real estate, accounts receivable, inventory and equipment as collateral supporting those commitments for which collateral is deemed necessary. The extent of collateral held for those commitments at December 31, 2004 varies up to 100%.

The Company defines the initial fair value of these letters of credit as the fee received from the customer. The maximum potential undiscounted amount of future payments of these letters of credit as of December 31, 2004 are $750,000 and they expire through 2006. Amounts due under these letters of credit would be reduced by any proceeds that the Company would be able to obtain in liquidating the collateral for the loans, which varies depending on the customer.

NOTE N - (continued)

The Bank grants loans primarily to customers in New York and its immediately adjacent suburban communities. Although the Bank has a diversified loan portfolio, a large portion of their loans are secured by commercial or residential real property. The Bank does not generally engage in non-recourse lending and typically will require the principals of any commercial borrower to obligate themselves personally on the loan. Although the Bank has diversified loan portfolios, a substantial portion of their debtors' ability to honor their contracts is dependent upon the economic sector. Commercial and standby letters of credit were granted primarily to commercial borrowers.

The Bank has entered into interest rate cap agreements in order to hedge its exposure to interest rate fluctuations. The Company adopted the provisions of SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" ("SFAS No. 133"), as amended, as of January 1, 2001. The statement requires the Company to recognize all derivative instruments at fair value as either assets or liabilities. Financial derivatives are reported at fair value in other assets or other liabilities. For derivatives not designated as hedges, the gain or loss is recognized in current earnings. Amounts reclassed into earnings, when the hedged transaction culminates, are included in interest

income.

NOTE O - REGULATORY MATTERS

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

Quantitative measures established by regulations to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the table below) of total and Tier 1 capital (as defined in the regulations) to risk-weighted assets, and of Tier 1 capital to average assets. Management believes that, as of December 31, 2004, the Bank meets all capital adequacy requirements to which it is subject.

As of December 31, 2004, the Bank met all regulatory requirements for classification as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, the Bank must maintain minimum total risk-based, Tier 1 risk-based and Tier 1 leverage ratios as set forth in the following table. There are no conditions or events since that date that management believes have changed the institution's category.

Note O - (continued)

The following table sets forth the actual and required regulatory capital amounts and ratios of, the Company and the Bank as of December 31, 2004 and 2003 (dollars in thousands):

	Actual		For capital adequacy purposes	
	Amount	Ratio	Amount	Ra
December 31, 2004				
Total Capital (to Risk-Weighted Assets)				

Company	110,063	30.1%	29,234	>=8
Bank	82,970	24.1%	27,533	>=8
Tier I Capital (to Risk-Weighted Assets)				
Company	107,136	29.3%	14,617	>=4
Bank	80,042	23.3%	13,766	>=4
Tier I Capital (to Average Assets)				
Company	107,136	11.2%	38,250	>=4
Bank	80,042	8.6%	37,240	>=4

	Actual		For capital adequacy purposes	
	Amount	Ratio	Amount	Ra
December 31, 2003				
Total Capital (to Risk-Weighted Assets)				
Company	86,759	26.1%	26,630	>=8
Bank	60,675	19.1%	25,417	>=8
Tier I Capital (to Risk-Weighted Assets)				
Company	84,166	25.3%	13,315	>=4
Bank	58,082	18.3%	12,709	>=4
Tier I Capital (to Average Assets)				
Company	84,166	10.7%	31,410	>=4
Bank	58,082	7.0%	33,391	>=4

BERKSHIRE BANCORP INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements (continued)

NOTE P - CONDENSED FINANCIAL INFORMATION - PARENT COMPANY ONLY

The condensed financial information for Berkshire Bancorp Inc. (parent company only) is as follows:

CONDENSED BALANCE SHEETS
(In Thousands)

	December 31,	
	2004	2003
ASSETS		

Cash	$ 7,415	$ 12,035
Equity investment in subsidiaries	101,004	82,532
Investment in securities available for sale	9,022	2,901
Loans	6,059	6,244
Accrued interest receivable	284	74
Other assets	892	499
Total assets	$ 124,676	$ 104,285
LIABILITIES AND STOCKHOLDERS' EQUITY		
Subordinated debt	$ 15,464	$ --
Other liabilities	1,593	795
Total liabilities	17,057	795
Stockholders' equity		
Common stock	770	256
Additional paid-in capital	89,543	89,866
Retained earnings	28,983	22,960
Accumulated other comprehensive income, net	(2,602)	775
Common stock in treasury, at cost	(9,075)	(10,367)
Total stockholders' equity	107,619	103,490
	$ 124,676	$ 104,285

BERKSHIRE BANCORP INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements (continued)

NOTE P - (continued)

CONDENSED STATEMENTS OF INCOME
(In Thousands)

	For The Years Ended December 31,		
	2004	2003	2002
INCOME			
Interest income from the Bank	$ 71	$ 106	$ 207
Interest income	1,090	795	1,149
Gain on sales of investment securities	734	1,131	7
Other income (loss)	96	407	(73)

Total income	1,991	2,439	1,290
EXPENSES			
Salaries and employee benefits	489	442	243
Interest expense	463	--	--
Other expenses	1,058	759	505
Total expenses	2,010	1,201	748
Income (loss) before income taxes and equity in undistributed net income of the Bank	(19)	1,238	542
Equity in undistributed net income of the Bank	7,668	6,710	5,405
Income before taxes	7,649	7,948	5,947
Provision for income taxes	147	533	350
Net income	$ 7,502	$ 7,415	$ 5,597

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BERKSHIRE BANCORP INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements (continued)

NOTE P - (continued)

CONDENSED STATEMENTS OF CASH FLOWS
(In Thousands)

	For The Years Ended Decembe	
	2004	2003
Operating activities:		
Net income	$ 7,502	$ 7,415
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Gain on sales of investment securities	(734)	(1,131)
Equity in undistributed net income of the Bank	(7,668)	(6,843)
Dividends received from the Bank	500	--
Increase in other liabilities	798	294
Decrease in other assets	69	151
Net cash provided by (used in) operating activities	467	(114)

Investing activities:		
Investment securities available for sale		
Purchases	(9,150)	(5,172)
Sales	3,874	9,451
Net decrease (increase) in loans	185	2,176
Contribution to the Bank	(14,791)	--
Transfer of premises and equipment	--	--
Net cash provided by (used in) investing activities	(19,882)	6,455
Financing activities:		
Proceeds from exercise of common stock options	1,271	205
Acquisition of treasury stock	(69)	(1,350)
Cash paid for fractional shares	(463)	--
Issuance of subordinated debentures	14,791	--
Dividends paid	(735)	(600)
Net cash provided by (used in) financing activities	14,795	(1,745)
Net increase (decrease) in cash and cash equivalents	(4,620)	4,596
Cash and cash equivalents at beginning of year	12,035	7,439
Cash and cash equivalents at end of year	$ 7,415	$ 12,035
Supplemental disclosures of cash flow information:		
Cash used to pay interest	$ 273	$ --
Cash used to pay income taxes	$ 419	$ 375
Transfer of premises and equipment to subsidiary for note receivable	$ --	$ 5,056

BERKSHIRE BANCORP INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements (continued)

NOTE Q - QUARTERLY FINANCIAL DATA (UNAUDITED)

The following represents summarized quarterly financial data of the Company which, in the opinion of management, reflects all adjustments, consisting only of normal recurring adjustments, necessary for a fair presentation of the Company's results of operations. (In thousands, except per share data).

	Three Months Ended		
	March 31	June 30	Septem

2004			
Interest income	$ 9,638	$ 9,626	$ 10,2
Interest expense	(3,720)	(3,796)	(4,1
Net interest income	5,918	5,830	6,1
Provision for loan losses	(45)	(45)	(
Gains on sales of securities	93	49	1
Non-interest income	325	202	2
Non-interest expenses	(2,962)	(3,172)	(3,1
Income before taxes	3,329	2,864	3,4
Provision for taxes	(1,378)	(1,383)	(1,4
Net income	$ 1,951	$ 1,481	$ 1,9
Per share data			
Net income per common share			
Basic	$ .29	$ .22	$.
Diluted	$ .28	$ .22	$.

	Three Months Ende		
	March 31	June 30	Septem
2003			
Interest income	$ 8,378	$ 8,480	$ 8,6
Interest expense	(3,388)	(3,395)	(3,3
Net interest income	4,990	5,085	5,2
Provision for loan losses	(105)	(45)	(
Gains on sales of securities	628	1,491	1
Non-interest income	364	305	2
Non-interest expenses	(2,712)	(2,727)	(3,0
Income before taxes	3,165	4,109	2,6
Provision for taxes	(1,423)	(1,801)	(1,2
Net income	$ 1,742	$ 2,308	$ 1,4
Per share data			
Net income per common share			
Basic	$ .26	$ .35	$.
Diluted	$ .26	$ .34	$.

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

Not Applicable.

ITEM 9A. Controls and Procedures

Evaluation of the Company's Disclosure Controls and Internal Control. As of the end of the period covered by this Annual Report on Form 10-K, the Company evaluated the effectiveness of the design and operation of its "disclosure controls and procedures" as defined in Rule 13a-15(e) of the Securities Exchange Act of 1934 ("Disclosure Controls"). This evaluation ("Controls Evaluation") was done under the supervision and with the participation of the Company's management, including the Chief Executive Officer ("CEO") who is also the Chief Financial Officer ("CFO").

Limitations on the Effectiveness of Controls. The Company's management, including the CEO/CFO, does not expect that its Disclosure Controls and/or its "internal control over financial reporting" as defined in Rule 13(a)-15(f) of the Securities Exchange Act of 1934 ("Internal Control") will prevent all error and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the control. The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions; over time, control may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

Conclusions. Based upon the Controls Evaluation, the CEO/CFO has concluded that, subject to the limitations noted above, the Disclosure Controls are effective in reaching a reasonable level of assurance that information required to be disclosed by the Company is recorded, processed, summarized and reported within the time period specified in the Securities and Exchange Commission's rules and forms. In accordance with SEC requirements, the CEO/CFO notes that during the fiscal quarter ended December 31, 2004, no changes in Internal Control have occurred that have materially affected or are reasonably likely to materially affect Internal Control.

ITEM 9B. Other Information

Not Applicable

PART III

ITEM 10. Directors and Executive Officers of the Registrant.

The following are the current directors and executive officers of the Company:

Name	Age	Position(s)
Steven Rosenberg	56	President, Director
William L. Cohen	63	Director
Thomas V. Guarino	51	Director
Moses Marx	69	Director
Randolph B. Stockwell	58	Director
Moses Krausz	64	President of The Berkshire Bank
David Lukens	55	Executive Vice President, Chief Financial Officer of The Berkshire Bank

Mr. Rosenberg has served as President and Chief Executive Officer of the Company since March 1999 and as Vice President and Chief Financial Officer of the Company from April 1990 to March 1999. He continues to serve as Chief Financial Officer. Mr. Rosenberg was elected a director in May 1995. From September 1987 through April 1990, he served as President and Director of Scomel Industries, Inc., a company engaged in international marketing and consulting. Mr. Rosenberg is a director of The Cooper Companies, Inc. (a developer and manufacturer of healthcare products).

Mr. Cohen was elected a director in July 1993. He has served as the Chief Executive Officer of Andover Properties, LLC, a real estate development company specializing in self storage facilities since November 2003, and has been a private investor for over six years. Mr. Cohen served as President, Chief Executive Officer and Chairman of the Board of The Andover Apparel Group, Inc., an apparel manufacturing company, from 1980 to 2000.

Mr. Guarino was elected a director in March 2001. He served as a director of Goshen Savings Bank from 1996, and chairman of the Board of Directors of GSB Financial Corporation from April 1998, until the respective mergers of those companies into The Berkshire Bank and the Company in March 2001. Mr. Guarino is the President and Senior Portfolio Manager of the Hudson Valley Investment Advisors, Inc., an investment management and advisory company, a position he has held since 1995. Prior to that, he had been, since 1988, a Vice President of Fleet Investment Advisors, Inc. and was Vice President in charge of investments of Norstar Bank of the Hudson Valley from 1981 to 1988.

Mr. Marx was elected a director in May 1995. Mr. Marx has been the General Partner in United Equities Company since 1954 and General Partner in United Equities Commodities Company since 1972. He is also President of Momar Corp. All of these are investment companies. Mr. Marx is a director of The Cooper Companies, Inc.

Mr. Stockwell was elected a director in July 1988. He has been a private investor for over ten years. Since April 1999, Mr. Stockwell has served as President of Yachting Systems of America, LLC, a small start-up company. In addition, he served in various capacities with the Community Bank, a commercial bank, from September 1972 to January 1987.

Mr. Krausz has held the position of President of The Berkshire Bank since March 1992 and Chief Executive Officer since November 1993. Prior to joining The Berkshire Bank, Mr. Krausz was Managing Director of SFS Management

Co., L.P., a mortgage banker, from 1987 to 1992 and was President of UMB Bank and Trust Company, a New York State chartered bank, from 1978 to 1987.

Mr. Lukens has held the position of Senior Vice President and Chief Financial Officer of The Berkshire Bank since December 1999, Executive Vice President since December 2003. Prior to joining the Bank, Mr. Lukens was Senior Vice President and Chief Financial officer of First Washington State Bank, a New Jersey commercial bank, from 1994 to 1999 and was Vice President and Controller at the Philadelphia, PA branch of Bank Leumi Le-Israel B.M., an international commercial bank, from 1978 to 1994.

There are no family relationships (whether by blood, marriage or adoption) among any of the Company's current directors or executive officers.

Audit Committee Members, Financial Expert and Independence

The Board of Directors of the Company has established an Audit Committee comprised of three independent directors, Messrs. William L. Cohen, Thomas V. Guarino and Randolph B. Stockwell. All of the members of the Audit Committee meet the independence requirements under current NASDAQ corporate governance standards for companies whose securities are quoted on NASDAQ. Based upon their education and relevant experience, the Board of Directors has determined that Messrs. Guarino and Stockwell each qualify as financial experts as defined by the Sarbanes-Oxley Act of 2002 and the rules of the Securities and Exchange Commission.

Corporate Code of Ethics

We have adopted a Corporate Code of Ethics that applies to the directors, officers and employees, including the senior management: the chief executive officer, chief financial officer, controller and persons performing similar functions, of Berkshire Bancorp Inc. and its subsidiaries. Copies of our Corporate Code of Ethics are available without charge upon written request to the Company at its principal executive office.

ITEM 11. Executive Compensation

The following table shows the compensation paid in or with respect to each of the last three fiscal years to the individual who served as the Company's Chief Executive Officer for the fiscal year ended December 31, 2004, and to each of the other executive officers who were paid more than $100,000 during the fiscal year ended December 31, 2004.

Summary Compensation Table

		Annual Compensation		
Name and Principal Position	Year	Salary	Bonus	All Other Compensation

	----	------	-----	------------
Steven Rosenberg	2004	$182,000	$ 10,000	$ --
President, Chief Executive	2003	$175,500	$ --	$ --
Officer and Chief Financial Officer	2002	$167,500	$ --	$ --
Moses Krausz	2004	$382,865	$200,000	$ 11,405(1)
President and Chief Executive	2003	$358,864	$175,000	$ 10,405(1)
Officer of The Berkshire Bank	2002	$347,288	$175,000	$ 10,050(1)
David Lukens	2004	$155,000	$ 25,000	$ 7,350(2)
Executive Vice President and	2003	$138,500	$ 25,000	$ 5,968(2)
Chief Financial Officer of The Berkshire Bank	2002	$125,000	$ 24,000	$ 5,367(2)

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(1) Consists of contributions by the Company to a 401(k) account of $8,000, $7,000 and $6,000, respectively, in 2004, 2003 and 2002, and income associated with life insurance coverage in excess of $50,000.

(2) Consists of contributions by the Company to a 401(k) account of $5,205, $4,905 and $4,470, respectively, in 2004, 2003 and 2002, and income associated with life insurance coverage in excess of $50,000. Does not include the annual retirement credits of 5% of gross wages under the Company's Retirement Income Plan.

Option Grants in Last Fiscal Year

There were no stock option grants during the fiscal year ended December 31, 2004.

Aggregated Option Exercises and Fiscal Year-End Option Values

The following table sets forth information concerning options exercised during the fiscal year ended December 31, 2004, and the number of options owned and the value of any in-the-money unexercised options as of December 31, 2004 by each of the individuals named in the Summary Compensation Table.

Name	Shares Acquired on Exercise (#)	Value Realized ($)	Number of Unexercised Options at Fiscal Year-End (#) Exercisable /Unexercisable	Value of Une In-the-Money O Fiscal Year- Exercisable/Une
Steven Rosenberg	-0-	-0-	30,000/0	315,00

Moses Krausz	-0-	-0-	150,000/0	1,334,70
David Lukens	-0-	-0-	30,000/0	306,30

Year-end values for unexercised in-the-money options represent the positive spread between the exercise price of such options and the fiscal year end market value of the common stock. An Option is "in-the-money" if the fiscal year end fair market value of the Common Stock exceeds the option exercise price.

Compensation of Directors

Each director who is not also an employee of the Company (a "Non-Employee Director") receives a stipend of $18,000 per annum and $1,500 for each day during which he participates in a meeting of the Board or a Committee of the Board. Each Non-Employee Director also receives a fee of $1,000 for telephonic meetings of the Board or a Board Committee. In addition, see "1999 Stock Incentive Plan" below.

1999 Stock Incentive Plan

The 1999 Stock Incentive Plan permits the granting of awards in the form of nonqualified stock options, incentive stock options, restricted stock, deferred stock, and other stock-based incentives. Up to 600,000 shares of common stock of the Company may be issued pursuant to the 1999 Stock Incentive Plan (subject to appropriate adjustment in the event of changes in the corporate structure of the Company). Officers, directors and other key employees of the Company or any subsidiary are eligible to receive awards under the 1999 Stock Incentive Plan. The option exercise price of all options which are granted under the 1999 Stock Incentive Plan must be at least equal to 100% of the fair market value of a share of common stock of the Company on the date of grant. At December 31, 2004, options to acquire 560,757 shares of common stock have been granted under this plan and 39,243 options are available for future grants.

Retirement Income Plan

The Company has a Retirement Income Plan (the "Retirement Plan"), a noncontributory plan covering substantially all full-time, non-union United States employees of the Company. Benefits were based upon a combination of employee compensation and years of service. The Company paid the entire cost of the plan for its employees and funded such costs as they accrued. The Company's funding policy was to make annual contributions within minimum and maximum levels required by applicable regulations. The Company's customary contributions were designed to fund normal cost on a current basis and fund over 30 years the estimated prior service cost of benefit improvements (15 years of annual gains and losses). The projected unit cost method was used to determine the annual cost. Plan assets consist principally of equity and fixed income mutual funds.

Benefit accruals were frozen as of September 15, 1988, resulting in a plan curtailment. As a result of such curtailment, the Company did not accrue benefits for future services; however, the Company did continue to contribute as necessary for any unfunded liabilities. In 2000, the Company reinstated the Retirement Plan to cover substantially all full-time, non-union United States employees of the Company.

A participant in the Plan accumulates a balance in his or her retirement account by receiving: (i) an annual retirement credit of 5% of gross wages paid during the year, but not in excess of the applicable annual maximum compensation permitted to be taken into account under Internal Revenue Service guidelines for each year of service; and (ii) an annual interest credit based upon the 30-year U. S. Treasury securities rate. The Company pays the entire cost of the Plan for its employees and funds such costs as they accrue.

The estimated annual benefits payable under the Plan upon retirement (at the normal retirement age of 65) for Messrs. Rosenberg and Lukens are approximately $160,000 and $16,000, respectively. In accordance with the laws currently governing the Plan, the estimated annual benefit payable to Mr. Rosenberg is not expected to increase. Mr. Krausz is not a participant in the Plan. (see Note K of Notes to Consolidated Financial Statements).

ITEM 12. Security Ownership of Certain Beneficial Owners and Management and Equity Compensation Plans.

The following table sets forth certain information as of March 24, 2005 with respect to the beneficial ownership of the Company's Common Stock by (i) each person who is known by the Company to own beneficially more than 5% of the Company's Common Stock, (ii) each of the Company's directors and executive officers, and (iii) all executive officers and directors as a group.

	Number of Shares	Percent of Class
William Cohen	7,500 (1)	*
Thomas V. Guarino	99,370 (2)	1.5%
Moses Krausz	238,000 (3)	3.4%
David Lukens	30,600 (4)	*
Moses Marx 160 Broadway New York, NY 10038	3,560,693 (5)	52.7%
Steven Rosenberg	62,580 (6)	*
Randolph B. Stockwell	24,000 (7)	*
All executive officers and directors as a group (7 persons)	4,022,743 (8)	57.3%

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* Less than 1%

(1) Includes 3,000 shares issuable upon the exercise of options which have been granted to Mr. Cohen under the Company's 1999 Stock Incentive Plan.

(2) Includes 43,650 shares issuable upon the exercise of options which have been granted to Mr. Guarino under the Company's 1999 Stock Incentive Plan. Includes 7,920 shares held in trust for minor children and 900 shares held by Mr. Guarino's wife

(3) Includes 150,000 shares issuable upon the exercise of options which have been granted to Mr. Krausz under the Company's 1999 Stock Incentive Plan and 2,100 shares owned by Mr. Krausz's spouse.

(4) Includes 30,000 shares issuable upon the exercise of options which have been granted to Mr. Lukens under the Company's 1999 Stock Incentive Plan.

ITEM 12. (continued)

(5) Includes 3,000 shares issuable upon the exercise of options which have been granted to Mr. Marx under the Company's 1999 Stock Incentive Plan, 285,000 shares owned by Momar Corporation and 391,163 shares owned by Terumah Foundation. Does not include 129,201 shares representing 80.5% of the shares owned by Eva and Esther, L.P., of which Mr. Marx has an 80.5% limited partnership interest. Mr. Marx's daughters and their husbands are the general partners of Eva and Esther, L.P.

(6) Includes 30,000 shares issuable upon the exercise of options which have been granted to Mr. Rosenberg under the Company's 1999 Stock Incentive Plan.

(7) Includes 3,000 shares issuable upon the exercise of options which have been granted to Mr. Stockwell under the Company's 1999 Stock Incentive Plan.

(8) Includes 262,650 shares of Common Stock which are issuable upon the exercise of outstanding options.

Equity Compensation Plans

The following table details information regarding the Company's existing equity compensation plans as of December 31, 2004.

Plan Category	(a) Number of securities to be issued upon exercise of outstanding options, warrants and rights	(b) Weighted-average exercise price of outstanding options, warrants and rights	Number of remaining future iss equity comp (excluding reflected
Equity compensation plans approved by security holders	365,084	$10.65	39
Equity compensation plans not approved by security holders	--	--	
Total	365,084	$10.65	39

ITEM 13. Certain Relationships and Related Transactions.

In January 2000, the Bank entered into a lease agreement with Bowling Green Associates, LP, the principal owner of which is Mr. Marx, for commercial space to open a bank branch. The Company obtained an appraisal of the market rental value of the space from an independent appraisal firm and management believes that the terms of the lease, including the annual rent paid, $298,000 and $270,000 in fiscal 2004 and 2003, is comparable to the terms and annual rent that would be paid to non-affiliated parties in a similar commercial transaction for similar commercial space.

See Item 1. Business - Transactions With Related Parties and Item 2.

Properties for additional information.

ITEM 14. Principal Accountant Fees and Services

The Company's principal accountant is Grant Thornton LLP ("Grant Thornton"). The total fees paid to Grant Thornton for the last two fiscal years are as follows:

	Fiscal Year Ended December 31, 2004	Fiscal Year Ended December 31, 2003
Audit Fees	$208,167	$146,153
Audit Related Fees: Professional services rendered for employee benefit plan audits, accounting assistance in connection with acquisitions and consultations related to financial accounting and reporting standards	16,250	6,815
Tax Fees: Tax consulting, preparation of returns	55,070	72,096
All Other Fees: Professional services rendered for corporate support	3,400	--

The Audit Committee has established its pre-approval policies and procedures, pursuant to which the Audit Committee approved the foregoing audit and permissible non-audit services provided by Grant Thornton LLP in 2004 and 2003. Consistent with the Audit Committee's responsibility for engaging our independent auditors, all audit and permitted non-audit services require pre-approval by the Audit Committee. The full Audit Committee approves proposed services and fee estimates for these services. The Audit Committee chairperson has been designated by the Audit Committee to approve any services arising during the year that were not pre-approved by the Audit Committee and services that were pre-approved. Service approved by the Audit Committee chairperson are communicated to the full Audit Committee at its next regular quarterly meeting and the Audit Committee reviews services and fees for the fiscal year at each such meeting. Pursuant to these procedures, the Audit Committee approved the foregoing audit and permissible non-audit services provided by Grant Thornton LLP.

PART IV

ITEM 15. Exhibits, Financial Statement Schedules.

(a) Documents filed as part of this Report:

(1) Financial Statements

Report of Independent Registered Public Accounting Firm

Consolidated Balance Sheets as of December 31, 2004 and 2003

Consolidated Statements of Income for the Years Ended December 31, 2004, 2003 and 2002

Consolidated Statements of Stockholders' Equity for the Years Ended December 31, 2004, 2003 and 2002

Consolidated Statements of Cash Flows for the Years Ended December 31, 2004, 2003 and 2002

Notes to Consolidated Financial Statements

ITEM 15. (continued)

Schedule Number	Description

None

All schedules for which provision is made in the applicable accounting regulations of the Securities and Exchange Commission are not required under the related instructions or are not applicable and, therefore, have been omitted.

(3) Exhibits

Exhibit Number	Description
2.1	Agreement and Plan of Reorganization, dated as of August 16, 2000, by and between Berkshire Bancorp Inc., Greater American Finance Group, Inc., The Berkshire Bank, GSB Financial Corporation and Goshen Savings Bank (incorporated by reference to the Companies Registration Statement on Form S-4 dated October 13, 2000.
3.1	Amended and Restated Certificate of Incorporation of the Company (incorporated by reference to Exhibit 3.1 to the Company's Current Report on Form 8-K dated March 30, 1999, and the Company's Quarterly Report on Form 10-Q for the Quarterly Period Ended June 30, 2004).
3.2	Amended and Restated By-laws of the Company (incorporated by reference to Exhibit 3.2 to the Company's Current Report on Form 8-K dated March 30, 1999).
10.1	1999 Stock Incentive Plan of the Company (incorporated by reference to Exhibit 10.8 to the Company's Current Report on Form 8-K dated March 30, 1999).+

10.2 Employment Agreement, dated May 1, 1999, between The Berkshire Bank and Moses Krausz (incorporated by reference to Exhibit 10.3 to the Company's Annual Report on Form 10-K for the Fiscal Year Ended December 31, 2000).+

10.3 Employment Agreement, dated January 1, 2001, between The Berkshire Bank and David Lukens (incorporated by reference to Exhibit 10.4 to the Company's Annual Report on Form 10-K for the Fiscal Year Ended December 31, 2000).+

10.4 Lease Agreement, dated October 26, 1999, between Braun Management, Inc. as agent for Bowling Green Associates, L.P., and The Berkshire Bank (incorporated by reference to Exhibit 10.5 to the Company's Quarterly Report on Form 10-Q for the Quarterly Period Ended March 31, 2001).

10.5 Amendment No. 1 to Employment Agreement, dated August 1, 2001, by and between The Berkshire Bank and Moses Krausz (incorporated by reference to Exhibit 10.6 to the Company's Quarterly Report on Form 10-Q for the Quarterly Period Ended September 30, 2001).+

10.6 Amendment No. 1 to Employment Agreement, dated June 3, 2002, by and between The Berkshire Bank and David Lukens (incorporated by reference to Exhibit 10.7 to the Company's Quarterly Report on Form 10-Q for the Quarterly Period Ended June 30, 2002).+

10.7 Amendment No. 2 to Employment Agreement, dated August 1, 2001, by and between The Berkshire Bank and Moses Krausz (incorporated by reference to Exhibit 10.8 to the Company's Quarterly Report on Form 10-Q for the Quarterly Period Ended June 30, 2002).+

21. Subsidiaries of the Company.

23. Consent of Independent Registered Public Accounting Firm 31. Certification of Principal Executive and Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32. Certification of Principal Executive and Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

+ Denotes a management compensation plan or arrangement.

SIGNATURES

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

BERKSHIRE BANCORP INC.

By: /s/ Steven Rosenberg

Steven Rosenberg
President, (Chief Executive Officer)

Date: March 24, 2005

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

Signature	Title	Date
/s/ Steven Rosenberg Steven Rosenberg	President, (Chief Executive Officer, Principal Financial Officer and Principal Accounting Officer); Director	March 24, 2005
/s/ William Cohen William Cohen	Director	March 24, 2005
/s/ Thomas V. Guarino Thomas V. Guarino	Director	March 24, 2005
/s/ Moses Marx Moses Marx	Director	March 24, 2005
/s/ Randolph B. Stockwell Randolph B. Stockwell	Director	March 24, 2005

STATEMENT OF DIFFERENCES

The greater-than-or-equal-to sign shall be expressed as.................. >=