INDEPENDENT BANK CORP
Form 10-K
March 03, 2006

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

Form 10-K

þ	**ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934** **For the fiscal year ended December 31, 2005**
	or
o	**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: 1-9047
Independent Bank Corp.
(Exact name of registrant as specified in its charter)

Massachusetts *(State or other jurisdiction of incorporation or organization)*	**04-2870273** *(I.R.S. Employer Identification No.)*
288 Union Street **Rockland, Massachusetts** *(Address of principal executive offices)*	**02370** *(Zip Code)*

Registrant s telephone number, including area code:
(781) 878-6100

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

Title of Each Class	Name of Each Exchange on Which Registered
None	None

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

Common Stock, $.0l par value per share
(Title of Class)

Preferred Stock Purchase Rights
(Title of Class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes o No þ

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes o No þ

Indicate by check mark whether the registrant (1) has filed all reports required 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 þ No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

Large Accelerated filer o Accelerated filer þ Non-accelerated filer o

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

The aggregate market value of the voting common stock held by non-affiliates of the registrant, computed by reference to the closing price of such stock on June 30, 2005, was approximately $412,672,609.

Indicate the number of shares outstanding of each of the registrant s classes of common stock, as of the latest practicable date. January 31, 2006: 15,395,347

DOCUMENTS INCORPORATED BY REFERENCE

List hereunder the following documents if incorporated by reference and the Part of the Form 10-K (e.g., Part I, Part II, etc.) into which the document is incorporated: (1) Any annual report to security holders; (2) Any proxy or information statement; and (3) Any prospectus filed pursuant to Rule 424(b) or (c) under the Securities Act of 1933. The listed documents should be clearly described for identification purposes (e.g., annual report to security holders for fiscal year ended December 24, 1980).

(1) Portions of the Registrant s Annual Report to Stockholders for the fiscal year ended December 31, 2005 are incorporated into Part II, Items 5-8 of this Form 10-K.

(2) Portions of the Registrant s definitive proxy statement for its 2006 Annual Meeting of Stockholders are incorporated into Part III, Items 10-13 of this Form 10-K.

INDEPENDENT BANK CORP.

2005 ANNUAL REPORT ON FORM 10-K

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CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

A number of the presentations and disclosures in this Form 10-K, including, without limitation, statements regarding the level of allowance for loan losses, the rate of delinquencies and amounts of charge-offs, and the rates of loan growth, and any statements preceded by, followed by, or which include the words may, could, should, will, would hope, might, believe, expect, anticipate, estimate, intend, plan, assume or similar expressions constit forward-looking statements within the meaning of the safe harbor provisions of the Private Securities Litigation Reform Act of 1995.

These forward-looking statements, implicitly and explicitly, include the assumptions underlying the statements and other information with respect to the Company s beliefs, plans, objectives, goals, expectations, anticipations, estimates, intentions, financial condition, results of operations, future performance and business, including the Company s expectations and estimates with respect to the Company s revenues, expenses, earnings, return on equity, return on assets, efficiency ratio, asset quality and other financial data and capital and performance ratios.

Although the Company believes that the expectations reflected in the Company s forward-looking statements are reasonable, these statements involve risks and uncertainties that are subject to change based on various important factors (some of which are beyond the Company s control). The following factors, among others, could cause the Company s financial performance to differ materially from the Company s goals, plans, objectives, intentions, expectations and other forward-looking statements:

A weakening in the strength of the United States economy in general and the strength of the regional and local economies within the New England region and Massachusetts which could result in a deterioration on credit quality, a change in the allowance for loan losses or a reduced demand for the Company s credit or fee-based products and services;

adverse changes in the local real estate market, as most of the Company s loans are concentrated in southeastern Massachusetts and Cape Cod and a substantial portion of these loans have real estate as collateral, could result in a deterioration of credit quality and an increase in the allowance for loan loss;

the effects of, and changes in, trade, monetary and fiscal policies and laws, including interest rate policies of the Board of Governors of the Federal Reserve System could affect the Company s business environment or affect the Company s operations;

the effects of, any changes in, and any failure by the Company to comply with tax laws generally and requirements of the federal New Markets Tax Credit program in particular could adversely affect the Company s tax provision and its financial results;

inflation, interest rate, market and monetary fluctuations could reduce net interest income and could increase credit losses;

adverse changes in asset quality could result in increasing credit risk-related losses and expenses;

competitive pressures could intensify and affect the Company s profitability, including as a result of continued industry consolidation, the increased financial services provided by non-banks and banking reform;

a deterioration in the conditions of the securities markets could adversely affect the value or credit quality of the Company s assets, the availability and terms of funding necessary to meet the Company s liquidity needs and the Company s ability to originate loans;

the potential to adapt to changes in information technology could adversely impact the Company s operations and require increased capital spending;

changes in consumer spending and savings habits could negatively impact the Company s financial results; and

future acquisitions may not produce results at levels or within time frames originally anticipated and may result in unforeseen integration issues.

If one or more of the factors affecting the Company s forward-looking information and statements proves incorrect, then the Company s actual results, performance or achievements could differ materially from those expressed in, or implied by, forward-looking information and statements contained in this Form 10-K. Therefore, the Company cautions you not to place undue reliance on the Company s forward-looking information and statements.

The Company does not intend to update the Company s forward-looking information and statements, whether written or oral, to reflect change. All forward-looking statements attributable to the Company are expressly qualified by these cautionary statements.

PART I.

Item 1. *Business*

General

Independent Bank Corp. (the   Company) is a state chartered, federally registered bank holding company headquartered in Rockland, Massachusetts that was incorporated under Massachusetts law in 1986. The Company is the sole stockholder of Rockland Trust Company (Rockland   or the   Bank), a Massachusetts trust company chartered in 1907. The Company is a community-oriented commercial bank. The community banking business, the Company s only reportable operating segment, consists of commercial banking, retail banking, investment management services, retail investments and insurance sales and is managed as a single strategic unit. The community banking business derives its revenues from a wide range of banking services, including lending activities, acceptance of demand, savings, and time deposits, trust investment management services, retail investments and insurance services, and mortgage banking income. Rockland offers a full range of community banking services through its network of 52 banking offices (including 50 full-service branches), nine commercial banking centers, three investment management group offices, and four residential lending centers, which are located in the Plymouth, Norfolk, Barnstable and Bristol counties of southeastern Massachusetts and Cape Cod. At December 31, 2005, the Company had total assets of $3.0 billion, total deposits of $2.2 billion, stockholders   equity of $228.2 million, and 722 full-time equivalent employees.

Market Area and Competition

The Bank contends with considerable competition both in generating loans and attracting deposits. The Bank s competition for loans is primarily from other commercial banks, savings banks, credit unions, mortgage banking companies, insurance companies, finance companies, and other institutional lenders. Competitive factors considered for loan generation include interest rates and terms offered, loan fees charged, loan products offered, service provided, and geographic locations.

In attracting deposits, the Bank s primary competitors are savings banks, commercial and co-operative banks, credit unions, as well as other non-bank institutions that offer financial alternatives such as brokerage firms and insurance companies. Competitive factors considered in attracting and retaining deposits include deposit and investment products and their respective rates of return, liquidity, and risk among other factors, such as, convenient branch locations and hours of operation, personalized customer service, online access to accounts, and automated teller machines.

The Bank s market area is attractive and entry into the market by financial institutions previously not competing in the market area may continue to occur. The entry into the market area by these institutions, and other non-bank institutions that offer financial alternatives could impact the Bank s growth or profitability.

Lending Activities

The Bank s gross loan portfolio (loans before allowance for loan losses) amounted to $2.0 billion on December 31, 2005 or 67.1% of total assets on that date. The Bank classifies loans as commercial, business banking, real estate, or consumer. Commercial loans consist primarily of loans to businesses with credit needs in excess of $250,000 and revenue in excess of $2.5 million for working capital and other business-related purposes and floor plan financing. Business banking loans consist primarily of loans to businesses with commercial credit needs of less than $250,000 and revenues of less than $2.5 million. Real estate loans are comprised of commercial mortgages that are secured by

non-residential properties, residential mortgages that are secured primarily by owner-occupied residences and mortgages for the construction of commercial and residential properties. Consumer loans consist primarily of automobile loans and home equity loans.

The Bank s borrowers consist of small-to-medium sized businesses and retail customers. The Bank s market area is generally comprised of the Plymouth, Norfolk, Barnstable and Bristol Counties located in southeastern Massachusetts and Cape Cod. Substantially all of the Bank s commercial, business banking and consumer loan portfolios consist of loans made to residents of and businesses located in southeastern Massachusetts and Cape Cod

with the primary exception being the origination of certain indirect auto loans in Rhode Island. The majority of the real estate loans in the Bank s loan portfolio are secured by properties located within this market area.

Interest rates charged on loans may be fixed or variable and vary with the degree of risk, loan term, underwriting and servicing costs, loan amount and the extent of other banking relationships maintained with customers. Rates are further subject to competitive pressures, the current interest rate environment, availability of funds and government regulations.

The Bank s principal earning assets are its loans. Although the Bank judges its borrowers to be creditworthy, the risk of deterioration in borrowers abilities to repay their loans in accordance with their existing loan agreements is inherent in any lending function. Participating as a lender in the credit markets requires a strict monitoring process to minimize credit risk. This process requires substantial analysis of the loan application, an evaluation of the customer s capacity to repay according to the loan s contractual terms, and an objective determination of the value of the collateral. The Bank also utilizes the services of an independent third-party consulting firm to provide loan review services, which consist of a variety of monitoring techniques performed after a loan becomes part of the Bank s portfolio.

The Bank s Controlled Asset Department is responsible for the management and resolution of nonperforming assets. In the course of resolving nonperforming loans, the Bank may choose to restructure certain contractual provisions. Nonperforming assets are comprised of nonperforming loans, nonperforming securities and Other Real Estate Owned (OREO). Nonperforming loans consist of loans that are more than 90 days past due but still accruing interest and nonaccrual loans. OREO includes properties held by the Bank as a result of foreclosure or by acceptance of a deed in lieu of foreclosure. In order to facilitate the disposition of OREO, the Bank may finance the purchase of such properties at market rates, if the borrower qualifies under the Bank s standard underwriting guidelines. The Bank had one property held as OREO for the period ending December 31, 2005 and did not hold any OREO for the period ending December 31, 2004.

Origination of Loans Commercial and industrial loan applications are obtained through existing customers, solicitation by Bank personnel, referrals from current or past customers, or walk-in customers. Commercial real estate loan applications are obtained primarily from previous borrowers, direct contact with the Bank, or referrals. Business banking loan applications are typically originated by the Bank s retail staff, through a dedicated team of business banking officers, by referrals from other areas of the Bank, referrals from current or past customers or through walk-in customers. Applications for residential real estate loans and all types of consumer loans are taken at all of the Bank s full-service branch offices. Beginning in November 2005, customers can now obtain residential applications and pre-approvals through Federal National Mortgage Association (F.N.M.A.) via a link from the Bank s website. Residential real estate loan applications primarily result from referrals by real estate brokers, homebuilders, and existing or walk-in customers. The Bank also maintains a staff of field originators who solicit and refer residential real estate loan applications to the Bank. These employees are compensated on a commission basis and provide convenient origination services during banking and non-banking hours. The Company uses a select group of third party originators to generate additional real estate loan volume. The loans are underwritten and closed in the name of the Bank. Volume generated by these third party originators was less than 6% of total origination in 2005. Consumer loan applications are directly obtained through existing or walk-in customers who have been made aware of the Bank s consumer loan services through advertising and other media, as well as indirectly through a network of automobile, recreational vehicle, and boat dealers.

Commercial and industrial loans, commercial real estate loans, and construction loans may be approved by commercial loan officers up to their individually assigned lending limits, which are established and modified periodically by management, with ratification by the Board of Directors, to reflect the officer s expertise and experience. Any of those types of loans which are in excess of a commercial loan officer s assigned lending authority must be approved by various levels of authority within the Commercial Lending Division, depending on the loan

amount, up to and including the Senior Loan Committee and, ultimately, the Executive Committee of the Board of Directors.

Business banking loans may be approved by business banking officers up to their individually assigned lending limits which are established and modified periodically by the Director of Consumer and Business Banking to reflect the officer s expertise and experience. The Director of Consumer and Business Banking s lending limit is

recommended by the Chief Financial Officer (CFO) and ratified by the Board of Directors. Any loan which is in excess of the business banking officer s assigned lending authority must be approved by the Director of Consumer and Business Banking.

Residential real estate and construction loans may be approved by residential underwriters and residential loan analysts up to their individually assigned lending limits, which are established and modified periodically by management, with ratification by the Board of Directors, to reflect the underwriter s and analyst s expertise and experience. Any loan which is in excess of the residential underwriter s and residential analyst s assigned residential lending authority must be approved by various levels of authority within the Residential Lending Division, depending on the loan amount, up to and including the Senior Loan Committee and, ultimately, the Executive Committee of the Board of Directors.

Consumer loans may be approved by consumer lenders up to their individually assigned lending limits which are established and modified periodically by the Consumer Loan Administrator and the Director of Consumer and Business Banking to reflect the officer s expertise and experience. The Director of Consumer and Business Banking s lending limit is recommended by the CFO and ratified by the Board of Directors. Any loan which is in excess of the consumer lender s assigned lending authority must be approved by the Consumer Loan Administrator or the Director of Consumer and Business Banking.

In accordance with governing banking statutes, Rockland is permitted, with certain exceptions, to make loans and commitments to any one borrower, including related entities, in the aggregate amount of not more than 20% of the Bank s stockholders equity, or $52.7 million at December 31, 2005. Notwithstanding the foregoing, the Bank has established a more restrictive limit of not more than 75% of the Bank s legal lending limit, or $39.5 million at December 31, 2005, which may only be exceeded with the approval of the Board of Directors. There were no borrowers whose total indebtedness in aggregate exceeded $39.5 million as of December 31, 2005.

Sale of Loans The Bank s residential real estate loans are generally originated in compliance with terms, conditions and documentation which permit the sale of such loans to the Federal Home Loan Mortgage Corporation (FHLMC), the Federal National Mortgage Association (FNMA), the Government National Mortgage Association (GNMA), and other investors in the secondary market. Loan sales in the secondary market provide funds for additional lending and other banking activities. The Bank may retain the servicing on the loans sold. As part of its asset/liability management strategy, the Bank may retain a portion of the adjustable and fixed rate residential real estate loan originations for its portfolio. During 2005, the Bank originated $287.8 million in residential real estate loans of which $101.9 million was retained in its portfolio, comprised primarily of adjustable rate loans.

Commercial and Industrial Loans The Bank offers secured and unsecured commercial loans for business purposes, including issuing letters of credit. At December 31, 2005, $155.1 million, or 7.6% of the Bank s gross loan portfolio consisted of commercial and industrial loans. Commercial and industrial loans generated 7.2%, 6.9%, and 7.2% of total interest income for the fiscal years ending 2005, 2004 and 2003, respectively.

Commercial loans may be structured as term loans or as revolving lines of credit. Commercial term loans generally have a repayment schedule of five years or less and, although the Bank occasionally originates some commercial term loans with interest rates which float in accordance with a designated index rate, the majority of commercial term loans have fixed rates of interest. The majority of commercial term loans are collateralized by equipment, machinery or other corporate assets. In addition, the Bank generally obtains personal guarantees from the principals of the borrower for virtually all of its commercial loans. At December 31, 2005, there were $56.0 million of term loans in the commercial loan portfolio.

Collateral for commercial revolving lines of credit may consist of accounts receivable, inventory or both, as well as other business assets. Commercial revolving lines of credit generally are reviewed on an annual basis and usually require substantial repayment of principal during the course of a year. The vast majority of these revolving lines of credit have variable rates of interest. At December 31, 2005, there were $97.0 million of revolving lines of credit in the commercial loan portfolio.

The Bank s standby letters of credit generally are secured, have terms of not more than one year, and are reviewed for renewal. At December 31, 2005, the Bank had $8.9 million of standby letters of credit.

The Bank also provides automobile and, to a lesser extent, boat and other vehicle floor plan financing. Floor plan loans are secured by the automobiles, boats, or other vehicles, which constitute the dealer s inventory. Upon the sale of a floor plan unit, the proceeds of the sale are applied to reduce the loan balance. In the event a unit financed under a floor plan line of credit remains in the dealer s inventory for an extended period, the Bank requires the dealer to pay-down the outstanding balance associated with such unit. Bank personnel make unannounced periodic inspections of each dealer to review the value and condition of the underlying collateral. At December 31, 2005, there were $14.2 million floor plan loans, all of which have variable rates of interest.

Business Banking Loans During the first quarter of 2005, the Company reclassified certain commercial and consumer loans to a new business banking loan category associated with the Company s business banking initiative. The business banking initiative was announced in 2004 and caters to all of the banking needs of businesses with commercial credit requirements and revenues typically less then $250,000 and $2.5 million respectively, with automated loan underwriting capabilities and new loan and deposit products. Business banking loans totaled $51.4 million, representing growth of 17.6% during the year ended December 31, 2005, compared to the same period last year. Business banking loans represented 2.5% of the Bank s gross loan portfolio. Business banking loans generated 2.4%, 1.3%, and 1.2% of total interest income for the fiscal years ending 2005, 2004 and 2003, respectively.

Business banking loans may be structured as term loans, lines of credit including overdraft protection, owner occupied commercial mortgages and standby letters of credit. Business banking generally obtains personal guarantees from the principals of the borrower for virtually all of its loan products. Business banking term loans generally have an amortization schedule of five years or less and, although business banking occasionally originates some term loans with interest rates that float in accordance with the prime rate, the majority of business banking term loans have fixed rates of interest. The majority of business banking term loans are collateralized by machinery, equipment and other corporate assets. At December 31, 2005, there were $16.0 million of term loans in the business banking loan portfolio.

Business banking lines of credit and overdraft protection may be offered on an unsecured basis to qualified applicants. Collateral for secured lines of credit and overdraft protection typically consists of accounts receivable and inventory as well as other business assets. Business banking lines of credit and overdraft protection are reviewed on a periodic basis based upon the total amount of exposure to the customer and are typically written on a demand basis. The vast majority of these lines of credit and overdraft protection have variable rates of interest. At December 31, 2005, there were $31.5 million of lines of credit and overdraft protection in the business banking loan portfolio.

Business banking owner occupied commercial mortgages typically have an amortization schedule of twenty years or less but are written with a five year maturity. The majority of business banking owner occupied commercial mortgages have fixed rates of interest that are adjusted typically every three to five years. The majority of business banking owner occupied commercial mortgages are collateralized by first or second mortgages on owner occupied commercial real estate. At December 31, 2005, there were $2.8 million of owner occupied commercial mortgages in the business banking loan portfolio.

Business banking s standby letters of credit generally are secured, have expirations of not more than one year, and are reviewed periodically for renewal. The business banking team makes use of the Bank s authority as a preferred lender with the U.S. Small Business Administration. At December 31, 2005, there were $992,000 of U.S. Small Business Administration loans in the business banking loan portfolio.

Real Estate Loans The Bank s real estate loans consist of loans secured by commercial properties, loans secured by one-to-four family residential properties, and construction loans. As of December 31, 2005, the Bank s loan portfolio included $683.2 million in commercial real estate loans, $433.4 million in residential real estate loans, $140.6 million in commercial construction loans and $8.3 million in residential construction loans, altogether totaling 62.0% of the Bank s gross loan portfolio. Real estate loans generated an aggregate of 47.5%, 46.2%, and 45.6% of total interest

income for the fiscal years ending December 31, 2005, 2004 and 2003, respectively.

A significant portion of the Bank s commercial real estate portfolio consists of loans secured by owner occupied commercial and industrial buildings and warehouses while a number of loans are secured by residential

development tracts. Commercial real estate loans also include multi-family residential loans that are primarily secured by apartment buildings and, to a lesser extent, condominiums. The Bank has a modest portfolio of loans secured by special purpose properties, such as hotels, motels, restaurants, and golf courses.

Although terms vary, commercial real estate loans generally have maturities of five years or less, amortization periods of 20 years, and interest rates that either float in accordance with a designated index or have fixed rates of interest. It is also the Bank s policy to obtain personal guarantees from the principals of the borrower on commercial real estate loans and to obtain financial statements at least annually from all commercial and multi-family borrowers.

Commercial real estate lending entails additional risks as compared to residential real estate lending. Commercial real estate loans typically involve larger loan balances to single borrowers or groups of related borrowers. Development of commercial real estate projects also may be subject to numerous land use and environmental issues. The payment experience on such loans is typically dependent on the successful operation of the real estate project, which can be significantly impacted by supply and demand conditions in the market for commercial and retail space.

Rockland originates both fixed-rate and adjustable-rate residential real estate loans. The Bank will lend up to 100% of the lesser of the appraised value of the residential property securing the loan or the purchase price, and generally requires borrowers to obtain private mortgage insurance when the amount of the loan exceeds 80% of the value of the property. The rates of these loans are typically competitive with market rates. The Bank s residential real estate loans are generally originated only under terms, conditions and documentation, which permit sale in the secondary market.

The Bank generally requires title insurance protecting the priority of its mortgage lien, as well as fire, extended coverage casualty and flood insurance when necessary in order to protect the properties securing its residential and other real estate loans. Independent appraisers appraise properties securing all of the Bank s first mortgage real estate loans.

Construction loans are intended to finance the construction of residential and commercial properties, including loans for the acquisition and development of land or rehabilitation of existing homes. Construction loans generally have terms of six months, but not more than two years. They usually do not provide for amortization of the loan balance during the term. The majority of the Bank s commercial construction loans have floating rates of interest based upon the Rockland base rate or the prime rate published daily in the Wall Street Journal.

A significant portion of the Bank s construction lending is related to one-to-four family residential development within the Bank s market area. The Bank typically has focused its construction lending on relatively small projects and has developed and maintains a relationship with a significant number of homebuilders in the Plymouth, Norfolk, Barnstable and Bristol Counties of southeastern Massachusetts and Cape Cod.

Construction loans are generally considered to present a higher degree of risk than permanent real estate loans. A borrower s ability to complete construction may be affected by a variety of factors such as adverse changes in interest rates and the borrower s ability to control costs and adhere to time schedules. The latter will depend upon the borrower s management capabilities, and may also be affected by strikes, adverse weather and other conditions beyond the borrower s control.

Consumer Loans The Bank makes loans for a wide variety of personal and consumer needs. Consumer loans primarily consist of installment loans, home equity loans, overdraft protection, and personal lines of credit. As of December 31, 2005, $568.8 million, or 27.9%, of the Bank s gross loan portfolio consisted of consumer loans. Consumer loans generated 20.8%, 20.1% and 20.6% of total interest income for the fiscal years ending December 31, 2005, 2004, and 2003, respectively.

The Bank s installment loans consist primarily of automobile loans, which totaled $263.2 million, at December 31, 2005, or 12.9% of loans, a decrease from 14.8% of loans at year-end 2004. A substantial portion of the Bank s automobile loans are originated indirectly by a network of approximately 230 new and used automobile dealers located within the Bank s market area. Although employees of the dealer take applications for such loans, the loans are made pursuant to Rockland s underwriting standards using Rockland s documentation, and

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a Rockland loan officer must approve all indirect loans. In addition to indirect automobile lending, the Bank also originates automobile loans directly.

The maximum term for the Bank s automobile loans is 84 months for a new car loan and 72 months with respect to a used car loan. Loans on new and used automobiles are generally made without recourse to the dealer. The Bank requires all borrowers to maintain automobile insurance, including full collision, fire and theft, with a maximum allowable deductible and with the Bank listed as loss payee. Some purchases from used car dealers are under a repurchase agreement. The dealer is required to pay off the loan (in return for the vehicle) as long as the Bank obtains the vehicle and returns it to the dealer within 180 days of the most recent delinquency payment. In addition, in order to mitigate the adverse effect on interest income caused by prepayments, all dealers are required to maintain a reserve, of up to 3% of the outstanding balance of the indirect loans originated by them under Reserve option A . Reserve option A allows the Bank to be rebated on a pro-rata basis in the event of prepayment prior to maturity. Reserve option B allows the dealer to share the reserve with the Bank, split 75/25, however for the Bank s receipt of 25%, no rebates are applied to the account after 90 days from date of first payment.

The Bank s consumer loans also include home equity, unsecured loans and loans secured by deposit accounts, loans to purchase motorcycles, recreational vehicles, motor homes, boats, or mobile homes. The Bank generally will lend up to 100% of the purchase price of vehicles other than automobiles with terms of up to three years for motorcycles and up to fifteen years for recreational vehicles.

Home equity loans may be made as a fixed rate term loan or under a variable rate revolving line of credit secured by a first or second mortgage on the borrower s residence or second home. At December 31, 2005, $41.4 million, or 16.4%, of the home equity portfolio were term loans and $210.5 million, or 83.6%, of the home equity portfolio were revolving lines of credit. The Bank will originate home equity loans in an amount up to 89.99% of the appraised value or on-line valuation, reduced for any loans outstanding secured by such collateral. Home equity loans are underwritten in accordance with the Bank s loan policy which includes a combination of credit score, loan to value ratio, employment history and debt to income ratio. Home equity lines of credit at December 31, 2005, had a weighted average FICO[2] score of 746 and a weighted average loan to value ratio of 59.0%. Home equity loans at December 31, 2005, had a weighted average FICO score of 730 and a weighted average loan to value ratio of 51.0%.

Cash reserve loans are made pursuant to previously approved unsecured cash reserve lines of credit. The rate on these loans is tied to the prime rate.

Investment Activities

The Bank s securities portfolio consists of U.S. Treasury and U.S. Government agency obligations, state, county and municipal securities, mortgage-backed securities, collateralized mortgage obligations, Federal Home Loan Bank (FHLB) stock, corporate debt securities and equity securities held for the purpose of funding supplemental executive retirement plan obligations through a Rabbi Trust. Most of these securities are investment grade debt obligations with average lives of five years or less. U.S. Treasury and U.S. Government agency securities entail a lesser degree of risk than loans made by the Bank by virtue of the guarantees that back them, require less capital under risk-based capital rules than non-insured or non-guaranteed mortgage loans, are more liquid than individual mortgage loans, and may be used to collateralize borrowings or other obligations of the Bank. The Bank views its securities portfolio as a source of income and liquidity. Interest and principal payments generated from securities provide a source of liquidity to fund loans and meet short-term cash needs. The Bank s securities portfolio is managed in accordance with the Rockland Trust Company Investment Policy adopted by the Board of Directors.

[1] Loan to Value is the ratio of the total potential exposure on a loan to the fair market value of the collateral. The higher the Loan to Value, the higher the loss risk in the event of default.
[2] FICO represents a credit score determined by the Fair Isaac Corporation, with data provided by the three major credit repositories (Trans Union, Experian, and Equifax). This score predicts the likelihood of loan default. The lower the score, the more likely an individual is to default. The relevant range of the score is 450 to 800.

The Chief Executive Officer or the Chief Financial Officer may make investments with the approval of one additional member of the Asset/Liability Management Committee, subject to limits on the type, size and quality of all investments, which are specified in the Investment Policy. The Bank s Asset/Liability Management Committee, or its appointee, is required to evaluate any proposed purchase from the standpoint of overall diversification of the portfolio. At December 31, 2005, securities totaled $716.6 million. Total securities generated interest and dividends on securities of 21.8%, 25.5%, and 25.4% of total interest income for the fiscal years ended 2005, 2004 and 2003, respectively.

Sources of Funds

Deposits Deposits obtained through Rockland s branch banking network have traditionally been the principal source of the Bank s funds for use in lending and for other general business purposes. The Bank has built a stable base of in-market core deposits from consumers, businesses, and municipalities located in southeastern Massachusetts and Cape Cod. Rockland offers a range of demand deposits, interest checking, money market accounts, savings accounts, and time certificates of deposit. Interest rates on deposits are based on factors that include loan demand, deposit maturities, alternative costs of funds, and interest rates offered by competing financial institutions in the Bank s market area. The Bank believes it has been able to attract and maintain satisfactory levels of deposits based on the level of service it provides to its customers, the convenience of its banking locations, and its interest rates that are generally competitive with those of competing financial institutions. Rockland has a municipal department that focuses on providing service to local municipalities. At December 31, 2005, there were municipal deposits from customers of $147.4 million which are included in total deposits. As of December 31, 2005, total deposits were $2.2 billion.

Rockland s branch locations are supplemented by the Bank s internet banking services as well as automated teller machine (ATM) cards and debit cards, which may be used to conduct various banking transactions at ATMs maintained at each of the Bank s full-service offices and three additional remote ATM locations. The ATM cards and debit cards also allow customers access to the NYCE regional ATM network, as well as the Cirrus nationwide ATM network. In addition, Rockland is a member of the SUM network, which allows access to 2,708 participating ATM machines free of surcharge. In Massachusetts there are 322 participating institutions and more than 1,770 ATMs. These networks provide the Bank s customers access to their accounts through ATMs located throughout Massachusetts, the United States, and the world. The debit card also can be used at any place that accepts MasterCard worldwide.

Borrowings Borrowings consist of short-term and intermediate-term obligations. Short-term borrowings can consist of FHLB advances, federal funds purchased, treasury tax and loan notes and assets sold under repurchase agreements. In a repurchase agreement transaction, the Bank will generally sell a security agreeing to repurchase either the same or a substantially identical security on a specified later date at a price slightly greater than the original sales price. The difference in the sale price and purchase price is the cost of the proceeds recorded as interest expense. The securities underlying the agreements are delivered to the dealer who arranges the transactions as security for the repurchase obligation. Payments on such borrowings are interest only until the scheduled repurchase date, which generally occurs within a period of 30 days or less. Repurchase agreements represent a non-deposit funding source for the Bank and the Bank is subject to the risk that the lender may default at maturity and not return the collateral. In order to minimize this potential risk, the Bank only deals with established investment brokerage firms when entering into these transactions. On December 31, 2005, the Bank had $25.0 million outstanding under these repurchase agreements with investment brokerage firms. In addition to agreements with brokers, the Bank has entered into similar agreements with its customers. At December 31, 2005, the Bank had $88.3 million of customer repurchase agreements outstanding.

In July 1994, Rockland became a member of the FHLB of Boston. Among the many advantages of this membership, this affiliation provides the Bank with access to short-to-medium term borrowing capacity. At December 31, 2005, the Bank had $417.5 million outstanding in FHLB borrowings with initial maturities ranging from 3 months to 20 years.

In addition, the Bank has $325.6 million of borrowing capacity remaining with the FHLB.

Also included in borrowings are junior subordinated debentures payable to the Company s unconsolidated special purpose entities (Independent Capital Trust III (Trust III) and Independent Capital Trust IV (Trust IV)) that issued trust preferred securities to the public. The Company pays interest of 8.625% and 8.375% on $25.8 million of junior subordinated debentures issued by each Trust III and Trust IV, respectively, on a quarterly basis in arrears. The debentures have a stated maturity date of December 31, 2031, and April 30, 2032, for amounts due to Trust III and Trust IV, respectively, and callable at the option of the Company on or after December 31, 2006 and April 30, 2007 for amounts due to Trust III and Trust IV, respectively.

Investment Management, Retail Investments and Insurance

Investment Management The Rockland Trust Investment Management Group provides investment and trust services to individuals, small businesses, and charitable institutions throughout southeastern Massachusetts and Cape Cod. In addition, the Bank serves as executor or administrator of estates.

Accounts maintained by the Rockland Trust Investment Management Group consist of managed and non-managed accounts. Managed accounts are those for which the Bank is responsible for administration and investment management and/or investment advice. Non-managed accounts are those for which the Bank acts solely as a custodian or directed trustee. The Bank receives fees dependent upon the level and type of service(s) provided. For the year ended December 31, 2005, the Investment Management Group generated gross fee revenues of $4.9 million. Total assets under administration as of December 31, 2005, were $680.1 million, an increase of $116.1 million, or 20.6%, from December 31, 2004.

The administration of trust and fiduciary accounts is monitored by the Trust Committee of the Bank s Board of Directors. The Trust Committee has delegated administrative responsibilities to three committees, one for investments, one for administration, and one for operations, all of which are comprised of Investment Management Group officers who meet not less than monthly.

Retail Investments and Insurance In 1999, the Bank entered into an agreement with Independent Financial Marketing Group, Inc. (IFMG) and their insurance subsidiary IFS Agencies, Inc. (IFS) for the sale of mutual fund shares, unit investment trust shares, general securities, fixed and variable annuities and life insurance. IFMG has placed their registered representatives onsite to market these products to the Bank s customer base. In 2005, the bank entered into an agreement with Savings Bank Life Insurance of Massachusetts (SBLI), to enable appropriately licensed Bank employees to offer SBLI s fixed annuities and life insurance to the Bank s customer base.

Regulation

The following discussion sets forth certain of the material elements of the regulatory framework applicable to bank holding companies and their subsidiaries and provides certain specific information relevant to the Company. To the extent that the following information describes statutory and regulatory provisions, it is qualified in its entirety by reference to the particular statutory and regulatory provisions. A change in applicable statutes, regulations or regulatory policy, may have a material effect on our business. The laws and regulations governing the Company and Rockland generally have been promulgated to protect depositors and not for the purpose of protecting stockholders.

General The Company is registered as a bank holding company under the Bank Holding Company Act of 1956 (BHCA), as amended, and as such is subject to regulation by the Board of Governors of the Federal Reserve System (Federal Reserve). Rockland is subject to regulation and examination by the Commissioner of Banks of the Commonwealth of Massachusetts (the Commissioner) and the Federal Deposit Insurance Corporation (FDIC). The majority of Rockland s deposit accounts are insured to the maximum extent permitted by law by the Bank Insurance Fund (BIF) which is administered by the FDIC. In 1994, the Bank purchased the deposits of three branches of a failed

savings and loan association from the Resolution Trust Corporation. These deposits are insured to the maximum extent permitted by law by the Savings Association Insurance Fund (SAIF).

The Bank Holding Company Act (BHCA) BHCA prohibits the Company from acquiring direct or indirect ownership or control of more than 5% of any class of voting shares of any bank, or increasing such ownership or control of any bank, without prior approval of the Federal Reserve. The BHCA also prohibits the Company from,

with certain exceptions, acquiring more than 5% of any class of voting shares of any company that is not a bank and from engaging in any business other than banking or managing or controlling banks.

Under the BHCA, the Federal Reserve is authorized to approve the ownership by the Company of shares in any company, the activities of which the Federal Reserve has determined to be so closely related to banking or to managing or controlling banks as to be a proper incident thereto. The Federal Reserve has, by regulation, determined that some activities are closely related to banking within the meaning of the BHCA. These activities include, but are not limited to, operating a mortgage company, finance company, credit card company, factoring company, trust company or savings association; performing data processing operations; providing some securities brokerage services; acting as an investment or financial adviser; acting as an insurance agent for types of credit-related insurance; engaging in insurance underwriting under limited circumstances; leasing personal property on a full-payout, non-operating basis; providing tax planning and preparation services; operating a collection agency and a credit bureau; providing consumer financial counseling and courier services. The Federal Reserve also has determined that other activities, including real estate brokerage and syndication, land development, property management and, except under limited circumstances, underwriting of life insurance not related to credit transactions, are not closely related to banking and are not a proper incident thereto.

Interstate Banking Pursuant to the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994 (the Interstate Banking Act), bank holding companies may acquire banks in states other than their home state without regard to the permissibility of such acquisitions under state law, but subject to any state requirement that the bank has been organized and operating for a minimum period of time, not to exceed five years, and the requirement that the bank holding company, after the proposed acquisition, controls no more than 10 percent of the total amount of deposits of insured depository institutions in the United States and no more than 30 percent or such lesser or greater amount set by state law of such deposits in that state.

Pursuant to Massachusetts law, no approval to acquire a banking institution, acquire additional shares in a banking institution, acquire substantially all the assets of a banking institution, or merge or consolidate with another bank holding company, may be given if the bank being acquired has been in existence for a period less than three years or, as a result, the bank holding company would control, in excess of 30%, of the total deposits of all state and federally chartered banks in Massachusetts, unless waived by the Commissioner. With the prior written approval of the Commissioner, Massachusetts also permits the establishment of de novo branches in Massachusetts to the full extent permitted by the Interstate Banking Act, provided the laws of the home state of such out-of-state bank expressly authorize, under conditions no more restrictive than those of Massachusetts, Massachusetts banks to establish and operate de novo branches in such state.

Capital Requirements The Federal Reserve has adopted capital adequacy guidelines pursuant to which it assesses the adequacy of capital in examining and supervising a bank holding company and in analyzing applications to it under the BHCA. The Federal Reserve s capital adequacy guidelines which generally require bank holding companies to maintain total capital equal to 8% of total risk-adjusted assets, with at least one-half of that amount consisting of Tier 1, or core capital and up to one-half of that amount consisting of Tier 2, or supplementary capital. Tier 1 capital for bank holding companies generally consists of the sum of common stockholders equity and perpetual preferred stock (subject in the case of the latter to limitations on the kind and amount of such stocks which may be included as Tier 1 capital), less net unrealized gains on available for sale securities and on cash flow hedges, and goodwill and other intangible assets required to be deducted from capital. Tier 2 capital generally consists of perpetual preferred stock which is not eligible to be included as Tier 1 capital; hybrid capital instruments such as perpetual debt and mandatory convertible debt securities, and term subordinated debt and intermediate-term preferred stock; and, subject to limitations, the allowance for loan losses. Assets are adjusted under the risk-based guidelines to take into account different risk characteristics, with the categories ranging from 0% (requiring no additional capital) for assets such as cash to 100% for the majority of assets which are typically held by a bank holding company, including commercial

real estate loans, commercial loans and consumer loans. Single family residential first mortgage loans which are not 90 days or more past due or nonperforming and which have been made in accordance with prudent underwriting standards are assigned a 50% level in the risk-weighting system, as are certain privately-issued mortgage-backed securities representing indirect ownership of such loans and certain multi-family housing loans. Off-balance sheet items also are adjusted to take into account certain risk characteristics.

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In addition to the risk-based capital requirements, the Federal Reserve requires bank holding companies to maintain a minimum leverage capital ratio of Tier 1 capital to total assets of 3.0%. Total assets for this purpose do not include goodwill and any other intangible assets or investments that the Federal Reserve determines should be deducted from Tier 1 capital. The Federal Reserve has announced that the 3.0% Tier 1 leverage capital ratio requirement is the minimum for the top-rated bank holding companies without any supervisory, financial or operational weaknesses or deficiencies or those which are not experiencing or anticipating significant growth. Other bank holding companies (including the Company) are expected to maintain Tier 1 leverage capital ratios of at least 4.0% to 5.0% or more, depending on their overall condition.

The Company currently is in compliance with the above-described regulatory capital requirements. At December 31, 2005, the Company had Tier 1 capital and total capital equal to 10.74% and 11.99% of total risk-adjusted assets, respectively, and Tier 1 leverage capital equal to 7.71% of total assets. As of such date, Rockland complied with the applicable federal regulatory capital requirements, with Tier 1 capital and total capital equal to 10.07% and 11.32% of total risk-adjusted assets, respectively, and Tier 1 leverage capital equal to 7.22% of total assets.

The FDIC has promulgated regulations and adopted a statement of policy regarding the capital adequacy of state-chartered banks, which, like Rockland, are not members of the Federal Reserve System. These requirements are substantially similar to those adopted by the Federal Reserve regarding bank holding companies, as described above. The FDIC s capital regulations establish a minimum 3.0% Tier 1 leverage capital to total assets requirement for the most highly-rated state-chartered, non-member banks, with an additional cushion of at least 100 to 200 basis points for all other state-chartered, non-member banks, which effectively will increase the minimum Tier 1 leverage capital ratio for such banks to 4.0% or 5.0% or more. Under the FDIC s regulations, the highest-rated banks are those that the FDIC determines are not anticipating or experiencing significant growth and have well diversified risk, including no undue interest rate risk exposure, excellent asset quality, high liquidity, good earnings and in general which are considered strong banking organizations, rated composite 1 under the Uniform Financial Institutions Rating System.

Each federal banking agency has broad powers to implement a system of prompt corrective action to resolve problems of institutions, which it regulates, which are not adequately capitalized. A bank shall be deemed to be (i) well capitalized if it has a total risk-based capital ratio of 10.0% or more, has a Tier 1 risk-based capital ratio of 6.0% or more, has a Tier 1 leverage capital ratio of 5.0% or more and is not subject to any written capital order or directive; (ii) adequately capitalized if it has a total risk-based capital ratio of 8.0% or more, a Tier 1 risk-based capital ratio of 4.0% or more, a Tier 1 leverage capital ratio of 4.0% or more (3.0% under certain circumstances) and does not meet the definition of well capitalized ; (iii) undercapitalized if it has a total risk-based capital ratio that is less than 8.0%, or a Tier 1 risk-based capital ratio that is less than 4.0% or a Tier 1 leverage capital ratio of less than 4.0% (3.0% under certain circumstances); (iv) significantly undercapitalized if it has a total risk-based capital ratio that is less than 6.0%, or a Tier 1 risk-based capital ratio that is less than 3.0%, or a Tier 1 leverage capital ratio that is less than 3.0%; and (v) critically undercapitalized if it has a ratio of tangible equity to total assets that is equal to or less than 2.0%. As of December 31, 2005, Rockland was deemed a well-capitalized institution for this purpose.

Commitments to Affiliated Institutions Under Federal Reserve policy, the Company is expected to act as a source of financial strength to Rockland and to commit resources to support Rockland. This support may be required at times when the Company may not be able to provide such support. Similarly, under the cross-guarantee provisions of the Federal Deposit Insurance Act, in the event of a loss suffered or anticipated by the FDIC either as a result of default of a banking or thrift subsidiary of a bank/financial holding company such as the Company or related to FDIC assistance provided to a subsidiary in danger of default the other banking subsidiaries of such bank/financial holding company may be assessed for the FDIC s loss, subject to certain exceptions.

Limitations on Acquisitions of Common Stock The federal Change in Bank Control Act (CBCA) prohibits a person or group of persons from acquiring control of a bank holding company or bank unless the appropriate federal bank

regulator has been given 60 days prior written notice of such proposed acquisition and within that time period such regulator has not issued a notice disapproving the proposed acquisition or extending for up to another 30 days the period during which such a disapproval may be issued. The acquisition of 25% or more of any class of

voting securities constitutes the acquisition of control under the CBCA. In addition, under a rebuttal presumption established under the CBCA regulations, the acquisition of 10% or more of a class of voting stock of a bank holding company or a FDIC insured bank, with a class of securities registered under or subject to the requirements of Section 12 of the Securities Exchange Act of 1934 would, under the circumstances set forth in the presumption, constitute the acquisition of control.

Any company would be required to obtain the approval of the Federal Reserve under the BHCA before acquiring 25% (5% in the case of an acquirer that is a bank holding company) or more of the outstanding common stock of, or such lesser number of shares as constitute control over, the Company. Such approval would be contingent upon, among other things, the acquirer registering as a bank holding company, divesting all impermissible holdings and ceasing any activities not permissible for a bank holding company. The Company owns no voting stock in any banking institution that would require approval of the Federal Reserve.

Deposit Insurance Premiums Rockland currently pays deposit insurance premiums to the FDIC based on a single, uniform assessment rate established by the FDIC for all BIF-member institutions. The assessment rates range from 0% to 0.27%. Under the FDIC s risk-based assessment system, institutions are assigned to one of three capital groups which assignment is based solely on the level of an institution s capital well capitalized, adequately capitalized, and undercapitalized which are defined in the same manner as the regulations establishing the prompt corrective action system under the Federal Deposit Insurance Act (FDIA). Rockland is presently well capitalized and as a result, Rockland is currently not subject to any FDIC premium obligation.

Community Reinvestment Act (CRA) Pursuant to the Community Reinvestment Act (CRA) and similar provisions of Massachusetts law, regulatory authorities review the performance of the Company and Rockland in meeting the credit needs of the communities served by Rockland. The applicable regulatory authorities consider compliance with this law in connection with applications for, among other things, approval of new branches, branch relocations, engaging in certain new financial activities under the Gramm-Leach-Bliley Act of 1999, as discussed below, and acquisitions of banks and bank holding companies. The FDIC and the Massachusetts Division of Banks has assigned the Bank a CRA rating of outstanding as of the latest examinations.

Bank Secrecy Act The Bank Secrecy Act requires financial institutions to keep records and file reports that are determined to have a high degree of usefulness in criminal, tax and regulatory matters, and to implement counter-money laundering programs and compliance procedures.

USA Patriot Act of 2001 In October 2001, the USA Patriot Act of 2001 was enacted in response to the terrorist attacks in New York, Pennsylvania and Washington D.C. which occurred on September 11, 2001. The Patriot Act is intended to strengthen U.S. law enforcement s and the intelligence communities abilities to work cohesively to combat terrorism on a variety of fronts. The potential impact of the Patriot Act on financial institutions of all kinds is significant and wide ranging. The Patriot Act contains sweeping anti-money laundering and financial transparency laws and imposes various regulations, including standards for verifying client identification at account opening, and rules to promote cooperation among financial institutions, regulators and law enforcement entities in identifying parties that may be involved in terrorism or money laundering.

Financial Services Modernization Legislation In November 1999, the Gramm-Leach-Bliley Act (GLB) of 1999, was enacted. The GLB repeals provisions of the Glass-Steagall Act which restricted the affiliation of Federal Reserve member banks with firms engaged principally in specified securities activities, and which restricted officer, director or employee interlocks between a member bank and any company or person primarily engaged in specified securities activities.

In addition, the GLB also contains provisions that expressly preempt any state law restricting the establishment of financial affiliations, primarily related to insurance. The general effect of the law is to establish a comprehensive framework to permit affiliations among commercial banks, insurance companies, securities firms and other financial service providers, by revising and expanding the Bank Holding Company Act framework to permit a holding company to engage in a full range of financial activities through a new entity known as a financial holding company. Financial activities is broadly defined to include not only banking, insurance and securities activities, but also merchant banking and additional activities that the Federal Reserve Board, in consultation with the Secretary of the Treasury, determines to be financial in nature, incidental to such financial activities or

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complementary activities that do not pose a substantial risk to the safety and soundness of depository institutions or the financial system generally.

The GLB also permits national banks to engage in expanded activities through the formation of financial subsidiaries. A national bank may have a subsidiary engaged in any activity authorized for national banks directly or any financial activity, except for insurance underwriting, insurance investments, real estate investment or development, or merchant banking, which may only be conducted through a subsidiary of a financial holding company. Financial activities include all activities permitted under new sections of the Bank Holding Company Act or permitted by regulation.

To the extent that the GLB permits banks, securities firms and insurance companies to affiliate, the financial services industry may experience further consolidation. The GLB is intended to grant to community banks certain powers as a matter of right that larger institutions have accumulated on an ad hoc basis and which unitary savings and loan holding companies already possess. Nevertheless, the GLB may have the result of increasing the amount of competition that the Company faces from larger institutions and other types of companies offering financial products, many of which may have substantially more financial resources than the Company.

Sarbanes-Oxley Act of 2002 On July 30, 2002, President Bush signed into law the Sarbanes-Oxley Act (SOA) of 2002. The stated goals of the SOA are to increase corporate responsibility, to provide for enhanced penalties for accounting and auditing improprieties at publicly traded companies, and to protect investors by improving the accuracy and reliability of corporate disclosures pursuant to the securities laws.

The SOA includes very specific additional disclosure requirements and new corporate governance rules, requires the Securities and Exchange Commission (SEC) and securities exchanges to adopt extensive additional disclosure, corporate governance and other related rules, and mandates further studies of certain issues by the SEC and the Comptroller General.

The SOA s principal legislation includes:

- auditor independence provisions which restrict non-audit services that accountants may provide to their audit clients;
- additional corporate governance and responsibility measures, including the requirement of certification of financial statements by the chief executive officer and the chief financial officer;
- the forfeiture of bonuses or other incentive-based compensation and profits from the sale of an issuer s securities by directors and senior officers in the twelve month period following initial publication of any financial statements that later require restatement;
- an increase in the oversight of, and enhancement of certain requirements relating to audit committees of public companies and how they interact with the Company s independent auditor;
- requirement that audit committee members must be independent and are absolutely barred from accepting consulting, advisory or other compensatory fees from the issuer;
- requirement that companies disclose whether at least one member of the audit committee is a financial expert (as such term will be defined by the SEC) and if not, why not;
- expanded disclosure requirements for corporate insiders, including a prohibition on insider trading during pension plan black out periods;

expedited filing requirements for Forms 4 s;

disclosure of off-balance sheet transactions;

a prohibition on personal loans to directors and officers, except certain loans made to insured financial institutions;

disclosure of a code of ethics and filing a Form 8-K for a change or waiver of such code;

real time filing of periodic reports;

- the formation of an independent public company accounting oversight board;
- mandatory disclosure by analysts of potential conflicts of interest; and
- various increased criminal penalties for violations of securities laws.

The SEC has been delegated the task of enacting rules to implement various provisions with respect to, among other matters, disclosure in periodic filings pursuant to the Exchange Act. The Company has incurred additional expenses in complying with the provisions of the SOA and the resulting regulations. As the SEC provides any new requirements under the SOA, we will review those rules, comply as required and may incur more expenses. However, management does not expect that such compliance will have a material impact on our results of operation or financial condition.

Regulation W Transactions between a bank and its affiliates are quantitatively and qualitatively restricted under the Federal Reserve Act. The Federal Deposit Insurance Act applies Sections 23A and 23B to insured nonmember banks in the same manner and to the same extent as if they were members of the Federal Reserve System. The Federal Reserve Board has also recently issued Regulation W, which codifies prior regulations under Sections 23A and 23B of the Federal Reserve Act and interpretative guidance with respect to affiliate transactions. Regulation W incorporates the exemption from the affiliate transaction rules, but expands the exemption to cover the purchase of any type of loan or extension of credit from an affiliate. Affiliates of a bank include, among other entities, the bank s holding company and companies that are under common control with the bank. The Company is considered to be an affiliate of the Bank. In general, subject to certain specified exemptions, a bank or its subsidiaries are limited in their ability to engage in covered transactions with affiliates:

- to an amount equal to 10% of the bank s capital and surplus, in the case of covered transactions with any one affiliate; and
- to an amount equal to 20% of the bank s capital and surplus, in the case of covered transactions with all affiliates.

In addition, a bank and its subsidiaries may engage in covered transactions and other specified transactions only on terms and under circumstances that are substantially the same, or at least as favorable to the bank or its subsidiary, as those prevailing at the time for comparable transactions with nonaffiliated companies. A covered transaction includes:

- a loan or extension of credit to an affiliate;
- a purchase of, or an investment in, securities issued by an affiliate;
- a purchase of assets from an affiliate, with some exceptions;
- the acceptance of securities issued by an affiliate as collateral for a loan or extension of credit to any party; and
- the issuance of a guarantee, acceptance or letter of credit on behalf of an affiliate.

In addition, under Regulation W:

- a bank and its subsidiaries may not purchase a low-quality asset from an affiliate;

covered transactions and other specified transactions between a bank or its subsidiaries and an affiliate must be on terms and conditions that are consistent with safe and sound banking practices; and

with some exceptions, each loan or extension of credit by a bank to an affiliate must be secured by collateral with a market value ranging from 100% to 130%, depending on the type of collateral, of the amount of the loan or extension of credit.

Regulation W generally excludes all non-bank and non-savings association subsidiaries of banks from treatment as affiliates, except to the extent that the Federal Reserve Board decides to treat these subsidiaries as affiliates.

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Employees As of December 31, 2005, the Bank had 722 full time equivalent employees. None of the Company s employees are represented by a labor union and management considers relations with its employees to be good.

Miscellaneous Rockland is subject to certain restrictions on loans to the Company, on investments in the stock or securities thereof, on the taking of such stock or securities as collateral for loans to any borrower, and on the issuance of a guarantee or letter of credit on behalf of the Company. Rockland also is subject to certain restrictions on most types of transactions with the Company, requiring that the terms of such transactions be substantially equivalent to terms of similar transactions with non-affiliated firms. In addition, under state law, there are certain conditions for and restrictions on the distribution of dividends to the Company by Rockland.

The regulatory information referenced briefly summarizes certain material statutes and regulations affecting the Company and the Bank and is qualified in its entirety by reference to the particular statutory and regulatory provisions.

Statistical Disclosure by Bank Holding Companies

The following information, included under Items 6, 7, and 8 of this report are incorporated by reference herein.

Note 8, Borrowings within *Notes to the Consolidated Financial Statements* which includes information regarding short-term borrowings and is included in Item 8 hereof.

For additional information regarding the Company s business and operations, see *Selected Financial Data* in Item 6 hereof, *Management s Discussion and Analysis of Financial Condition and Results of Operations* in Item 7 hereof and the *Consolidated Financial Statements* in Item 8 hereof.

Securities and Exchange Commission Availability of Filings on Company Web Site

Under the Securities Exchange Act of 1934 Sections 13 and 15(d), periodic and current reports must be filed with the SEC. The public may read and copy any materials filed with the SEC at the SEC s Public Reference Room at 450 Fifth Street, NW, Washington, DC 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0030. The Company electronically files the following reports with the SEC: Form 10-K (Annual Report), Form 10-Q (Quarterly Report), Form 11-K (Annual Report for Employees Stock Purchase and Savings Plans), Form 8-K (Report of Unscheduled Material Events), Forms S-4, S-3 and 8-A (Registration Statements), and Form DEF 14A (Proxy Statement). The Company may file additional forms. The SEC maintains an internet site that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC, at www.sec.gov, in which all forms filed electronically may be accessed. Additionally, our annual report on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K filed with the SEC and additional shareholder information are available free of charge on the Company s website: www.RocklandTrust.com. Information contained on our website and the SEC website is not incorporated by reference into this Form 10-K. We have included our web address and the SEC website address only as inactive textual references and do not intend them to be active links to our website or the SEC website. The Company s Code of Ethics and other Corporate Governance documents are also available on the Company s website in the Investor Relations section of the website.

Item 1A. ***Risk Factors***

Changes in interest rates could adversely impact the Company s financial condition and results of operations. The Company s ability to make a profit, like that of most financial institutions, substantially depends upon its net interest income, which is the difference between the interest income earned on interest earning assets, such as loans and

investment securities, and the interest expense paid on interest-bearing liabilities, such as deposits and borrowings. However, certain assets and liabilities, may react differently to changes in market interest rates. Further, interest rates on some types of assets and liabilities may fluctuate prior to changes in broader market interest rates, while rates on other types of assets may lag behind. Additionally, some assets such as adjustable-rate mortgages, have features, and rate caps, which restrict changes in their interest rates.

Factors such as inflation, recession, unemployment, money supply, global disorder such as that experienced as a result of the terrorist activity on September 11, 2001, instability in domestic and foreign financial markets, and other factors beyond the Company s control, may affect interest rates. Changes in market interest rates will also affect the level of voluntary prepayments on loans and the receipt of payments on mortgage-backed securities, resulting in the receipt of proceeds that may have to be reinvested at a lower rate than the loan or mortgage-backed security being prepaid. Although the Company pursues an asset-liability management strategy designed to control its risk from changes in market interest rates, changes in interest rates can still have a material adverse effect on the Company s profitability.

If the Company has higher loan losses than it has allowed for, its earnings could materially decrease. The Company s loan customers may not repay loans according to their terms, and the collateral securing the payment of loans may be insufficient to assure repayment. The Company may therefore experience significant credit losses which could have a material adverse effect on its operating results. The Company makes various assumptions and judgments about the collectibility of its loan portfolio, including the creditworthiness of borrowers and the value of the real estate and other assets serving as collateral for the repayment of loans. In determining the size of the allowance for loan losses, the Company relies on its experience and its evaluation of economic conditions. If its assumptions prove to be incorrect, its current allowance for loan losses may not be sufficient to cover losses inherent in its loan portfolio and adjustment may be necessary to allow for different economic conditions or adverse developments in its loan portfolio. Consequently, a problem with one or more loans could require the Company to significantly increase the level of its provision for loan losses. In addition, federal and state regulators periodically review the Company s allowance for loan losses and may require it to increase its provision for loan losses or recognize further loan charge-offs. Material additions to the allowance would materially decrease the Company s net income.

A significant amount of the Company s loans are concentrated in Massachusetts, and adverse conditions in this area could negatively impact its operations. Substantially all of the loans the Company originates are secured by properties located in or are made to businesses which operate in Massachusetts. Because of the current concentration of the Company s loan origination activities in Massachusetts, in the event of adverse economic conditions, potential downward pressure on housing prices, political or business developments or natural hazards that may affect Massachusetts and the ability of property owners and businesses in Massachusetts to make payments of principal and interest on the underlying loans, the Company would likely experience higher rates of loss and delinquency on its loans than if its loans were more geographically diversified, which could have an adverse effect on its results of operations or financial condition.

The Company operates in a highly regulated environment and may be adversely impacted by changes in law and regulations. The Company is subject to extensive regulation, supervision and examination. See Regulation in Item 1 hereof, *Business.* Any change in the laws or regulations and failure by the Company to comply with applicable law and regulation, or a change in regulators supervisory policies or examination procedures, whether by the Massachusetts Commissioner of Banks, the FDIC, the Federal Reserve Board, other state or federal regulators, the United States Congress, or the Massachusetts legislature could have a material adverse effect on the Company s business, financial condition, results of operations, and cash flows.

The Company has strong competition within its market area which may limit the Company s growth and profitability. The Company faces significant competition both in attracting deposits and in the origination of loans. See Market Area and Competition in Item 1 hereof, *Business.* Commercial banks, credit unions, savings banks, savings and loan associations operating in our primary market area have historically provided most of our competition for deposits. Competition for the origination of real estate and other loans come from other commercial banks, thrift institutions, insurance companies, finance companies, other institutional lenders and mortgage companies.

The success of the Company is dependent on hiring and retaining certain key personnel. The Company s performance is largely dependent on the talents and efforts of highly skilled individuals. The Company relies on key personnel to

manage and operate its business, including major revenue generating functions such as loan and deposit generation. The loss of key staff may adversely affect the Company s ability to maintain and manage these functions effectively, which could negatively effect the Company s revenues. In addition, loss of key personnel

could result in increased recruiting and hiring expenses, which could cause a decrease in the Company s net income. The Company s continued ability to compete effectively depends on its ability to attract new employees and to retain and motivate its existing employees.

Item 1B. ***Unresolved Staff Comments***

None

Item 2. ***Properties***

At December 31, 2005, the Bank conducted its business from its headquarters and main office located at 288 Union Street, Rockland, Massachusetts and an additional fifty-one banking offices located within Barnstable, Bristol, Norfolk and Plymouth Counties in southeastern Massachusetts and Cape Cod. In addition to its main office, the Bank owned twenty-one of its branches and leased the remaining thirty branches. All of the Bank s properties are considered to be in good condition and adequate for the purposes for which they are used. In addition to these branch locations, the Bank had three remote ATM locations all of which were leased.

County	Banking Offices	ATM	Deposits (Dollars in thousands)
Barnstable	15		$ 554,477
Bristol	3		83,738
Norfolk	5		192,303
Plymouth	29	3	1,374,976
Total	52	3	$ 2,205,494

The Bank conducted business in nine administrative locations. These locations housed executive, administrative, investment management, mortgage, consumer lending, commercial lending and back office support staff offices and warehouse space. The bank owned three of its administrative offices and leased the remaining six offices.

County	Administrative Offices
Barnstable	1
Bristol	1
Norfolk	2
Plymouth	5
Total	9

For additional information regarding our premises and equipment and lease obligations, see Notes 6 and 16, respectively, to the Consolidated Financial Statements included in Item 8 hereof.

Item 3. ***Legal Proceedings***

The Company expects that the federal judge presiding over the pending case known as Rockland Trust Company v. Computer Associates International, Inc., United States District Court for the District of Massachusetts Civil Action No. 95-11683-DPW, will issue a final trial court decision, in the form of Findings Of Fact and Conclusions Of Law, sometime soon. The case arises from a 1991 License Agreement (the Agreement) between the Bank and Computer Associates International, Inc. (CA) for an integrated system of banking software products.

In July 1995 the Bank filed a Complaint against CA in federal court in Boston which asserted claims for breach of the Agreement, breach of express warranty, breach of the implied covenant of good faith and fair dealing, fraud, and for unfair and deceptive practices in violation of section 11 of Chapter 93A of the Massachusetts General Laws (the 93A Claim). The Bank is seeking damages of at least $1.23 million from CA. If the Bank prevails on the 93A Claim, it shall be entitled to recover its attorney fees and costs and may also recover double or triple damages. CA asserted a Counterclaim against the Bank for breach of the Agreement. CA seeks to recover damages of at least $1.1 million from the Bank.

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The non-jury trial of the case was conducted in January 2001. The trial concluded with post-trial submissions to and argument before the Court in February 2001. In September 2002 the court, in response to a joint inquiry from counsel for the Bank and counsel for CA, indicated that the judge is actively working on the case and anticipated, at that time, rendering a decision sometime in the fall of 2002. The court, however, has not yet rendered a decision.

The Company has considered the potential impact of this case, and all cases pending in the normal course of business, when preparing its financial statements. While the trial court decision may affect the Company s operating results for the quarter in which the decision is rendered in either a favorable or unfavorable manner, the final outcome of this case will not likely have any material, long-term impact on the Company s financial condition.

In addition to the foregoing, the Company is involved in routine legal proceedings occurring in the ordinary course of business which in the aggregate are believed by us to be immaterial to our financial condition and results of operations.

Item 4. ***Submission of Matters to a Vote of Security Holders***

There were no matters submitted to a vote of our security holders in the fourth quarter of 2005.

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PART II

Item 5. ***Market for Independent Bank Corp. s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities***

Independent Bank Corp. s common stock trades on the NASDAQ National Market under the symbol INDB. The Company declared cash dividends of $0.60 per share in 2005 and $0.56 per share in 2004. The ratio of dividends paid to earnings in 2005 and 2004 was 27.8% and 27.2%, respectively.

Payment of dividends by the Company on its common stock is subject to various regulatory restrictions and guidelines. Since substantially all of the funds available for the payment of dividends are derived from the Bank, future dividends will depend on the earnings of the Bank, its financial condition, its need for funds, applicable governmental policies and regulations, and other such matters as the Board of Directors deem appropriate. Management believes that the Bank will continue to generate adequate earnings to continue to pay dividends on a quarterly basis.

The following schedule summarizes the price range of common stock and the cash dividends paid for the fiscal years ended 2005 and 2004.

Table 1 Price Range of Common Stock

	High	Low	Dividend
2005			
4th Quarter	$ 30.20	$ 26.98	$ 0.15
3rd Quarter	31.53	28.20	0.15
2nd Quarter	29.52	25.31	0.15
1st Quarter	33.20	28.34	0.15

	High	Low	Dividend
2004			
4th Quarter	$ 36.15	$ 30.96	$ 0.14
3rd Quarter	31.43	26.60	0.14
2nd Quarter	31.11	25.52	0.14
1st Quarter	32.27	27.50	0.14

As of December 31, 2005 there were 15,413,841 shares of common stock outstanding which were held by approximately 1,572 holders of record. The closing price of the Company s stock on December 31, 2005 was $28.53. Such number of record holders does not reflect the number of persons or entities holding stock in nominee name through banks, brokerage firms and other nominees.

During the three months ended December 31, 2005 the Company did not repurchase any of its common stock.

On January 19, 2006 the Company s Board of Directors approved a common stock repurchase program. Under the program, which is effective immediately, the Company is authorized to repurchase up to 800,000 shares, or approximately 5% of the Company s outstanding common stock. The Company placed no deadline on the repurchase program, but expects to make open market or privately negotiated purchases from time to time. The timing and amount of stock repurchases will depend upon market conditions, securities law limitations, and other corporate considerations. The repurchase program may be modified, suspended, or terminated by the Board of Directors at any time.

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Item 6. ***Selected Financial Data***

The selected consolidated financial and other data of the Company set forth below does not purport to be complete and should be read in conjunction with, and is qualified in its entirety by, the more detailed information, including the Consolidated Financial Statements and related notes, appearing elsewhere herein.

	As of or For the Years Ended December 31,				
	2005	2004	2003	2002	2001
	(Dollars in thousands, except per share data)				
Financial Condition Data:					
Securities available for sale	$ 581,516	$ 680,286	$ 527,507	$ 501,828	$ 569,288
Securities held to maturity	104,268	107,967	121,894	149,071	132,754
Loans	2,040,808	1,916,358	1,581,135	1,431,602	1,298,938
Allowance for loan losses	26,639	25,197	23,163	21,387	18,190
Total assets	3,041,685	2,943,926	2,436,755	2,285,372	2,199,188
Total deposits	2,205,494	2,060,235	1,783,338	1,688,732	1,581,618
Total borrowings	587,810	655,161	415,369	362,155	387,077
Corporation-obligated manditorily redeemable Trust Preferred Securities			47,857	47,774	75,329
Stockholders equity	228,152	210,743	171,847	161,242	133,261
Non-performing loans	3,339	2,702	3,514	3,077	3,015
Non-performing assets	3,339	2,702	3,514	3,077	3,015
Operating Data:					
Interest income	$ 155,661	$ 134,613	$ 128,306	$ 140,825	$ 145,069
Interest expense	49,818	36,797	32,533	40,794	54,478
Net interest income	105,843	97,816	95,773	100,031	90,591
Provision for loan losses	4,175	3,018	3,420	4,650	4,619
Non-interest income	27,150	28,355	27,794	22,644	20,760
Non-interest expenses	80,492	77,691	73,827	75,625	68,529
Minority interest expense		1,072	4,353	5,041	5,666
Net income	33,205	30,767	26,431	25,066	22,052
Net income available to common shareholders	33,205	30,767	26,431	23,561	22,052
Per Share Data:					
Net income Basic	$ 2.16	$ 2.06	$ 1.82	$ 1.63	$ 1.54
Net income Diluted	2.14	2.03	1.79	1.61	1.53
Cash dividends declared	0.60	0.56	0.52	0.48	0.44
Book value(1)	14.80	13.75	11.75	11.15	9.30
Tangible book value per share(2)	11.11	10.01	9.27	8.64	6.77
Operating Ratios:					
Return on average assets(3)	1.11%	1.13%	1.11%	1.12%	1.07%
Return on average equity(3)	15.10%	16.27%	15.89%	17.26%	17.42%
	3.88%	3.95%	4.40%	4.88%	4.84%

Net interest margin (on a fully tax equivalent basis)					
Equity to assets	7.50%	7.16%	7.05%	7.06%	6.06%
Dividend payout ratio	27.79%	27.23%	28.64%	27.67%	28.57%

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	As of or For the Years Ended December 31,				
	2005	2004	2003	2002	2001
	(Dollars in thousands, except per share data)				
Asset Quality Ratios:					
Nonperforming loans as a percent of gross loans	0.16%	0.14%	0.22%	0.21%	0.23%
Nonperforming assets as a percent of total assets	0.11%	0.09%	0.14%	0.13%	0.14%
Allowance for loan losses as a percent of total loans	1.31%	1.31%	1.46%	1.49%	1.40%
Allowance for loan losses as a percent of nonperforming loans	797.81%	932.53%	659.16%	695.06%	603.32%
Total allowance for loan losses as a percent of total loans(4)	1.31%	1.31%	1.46%	1.53%	1.46%
Total allowance for loan losses as a percent of nonperforming loans(4)	797.81%	932.53%	659.16%	711.89%	630.18%
Capital Ratios:					
Tier 1 leverage capital ratio	7.71%	7.06%	7.60%	7.10%	6.31%
Tier 1 risk-based capital ratio	10.74%	10.19%	11.00%	10.37%	9.24%
Total risk-based capital ratio	11.99%	11.44%	12.25%	11.68%	12.96%

(1) Calculated by dividing total stockholders equity by the net outstanding shares as of the end of each period.

(2) Calculated by dividing stockholders equity less goodwill and core deposit intangible by the net outstanding shares as of the end of each period.

(3) Calculated using net income which excludes the write-off of trust preferred issuance costs in 2002.

(4) Including credit quality discount for the years 2001 through 2002.

See Item 8. Financial Statements and Supplementary Data, *Consolidated Financial Statements*, Note 1 Summary of Significant Accounting Policies, Goodwill and Core Deposit Intangibles and Note 10 Goodwill and Core Deposit Intangibles , for information related to the Company s acquisitions and adoption of Statement of Financial Accounting Standards (SFAS) No. 147 Acquisitions of Certain Financial Institutions , and Financial Accounting Standards Board (FASB) Interpretation (FIN) No. 46 *Consolidation of Variable Interest Entities an Interpretation of Accounting Research Bulletin No. 51* for information related to the Company s adoption of Fin No. 46R which affects the comparability of the information reflected in the selected financial data.

Item 7. ***Management s Discussion and Analysis of Financial Condition and Results of Operations***

Independent Bank Corp. (the Company) is a state chartered, federally registered bank holding company headquartered in Rockland, Massachusetts that was incorporated under Massachusetts law in 1986. The Company is the sole stockholder of Rockland Trust Company (Rockland or the Bank), a Massachusetts trust company chartered in 1907. The Company also owns 100% of the common stock of Independent Capital Trust III (Trust III) and Independent Capital Trust IV (Trust IV), each of which are formed under Delaware law and have issued trust preferred securities to the public. As of March 31, 2004, Trust III and Trust IV are no longer included in the Company s consolidated

financial statements (see discussion in *Recent Accounting Pronouncements, Fin No. 46, within Item 7* hereof). The Bank s subsidiaries consist of: three Massachusetts securities corporations, RTC Securities Corp. I, RTC Securities Corp. X, and Taunton Avenue Securities Corp.; Taunton Avenue Inc.; and, Rockland Trust Community Development LLC (RTC CDE I) and Rockland Trust Community Development Corporation II (RTC CDE II). All of the Bank s subsidiaries are incorporated or formed under Massachusetts law. Taunton Avenue Inc. was formed in May 2003 to hold loans, industrial development bonds and other assets. RTC CDE I and RTC CDE II were formed in August 2003 and August 2005, respectively, to make loans and to provide financial assistance to qualified businesses and individuals in low-income communities in accordance with the U.S. Treasury s New Markets Tax Credit Program criteria. All material intercompany balances and transactions

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have been eliminated in consolidation. When necessary, certain amounts in prior year financial statements have been reclassified to conform to the current year s presentation. The following should be read in conjunction with the Consolidated Financial Statements and related notes thereto.

Critical Accounting Policies

Critical accounting policies are defined as those that are reflective of significant judgments and uncertainties, and could potentially result in materially different results under different assumptions and conditions. We believe that our most critical accounting policies upon which our financial condition depends, and which involve the most complex or subjective decisions or assessments are as follows:

Allowance for Loan Losses: The Company s allowance for loan losses provides for probable losses based upon evaluations of known and inherent risks in the loan portfolio. Arriving at an appropriate amount of allowance for loan losses involves a high degree of judgment.

The Company makes use of two types of allowances for loan losses: specific and general. A specific allowance may be assigned to a loan that is considered to be impaired. Loan impairment is determined based upon management s identification and evaluation of problem loans and is recognized when the Company deems that the timely collection of all principal and/or interest payments that are contractually due is no longer assured. Judgment is required as to the timing of designating a loan as impaired and the amount of the required specific allowance. Management s judgment is based upon its assessment of probability of default, loss given default and exposure at default. Changes in these estimates could be due to a number of circumstances which may have a direct impact on the provision for loan losses and may result in changes to the amount of allowance.

The general allowance is determined based upon management s judgment and its amount is dependent upon the prevailing business environment; as it is affected by changing economic conditions and various external factors, which may impact the portfolio in ways currently unforeseen, as well as historical and expected loss information, loan portfolio composition and other relevant indicators. The allowance is increased by provisions for loan losses and by recoveries of loans previously charged-off and is reduced by loans charged-off. For a full discussion of the Company s methodology of assessing the adequacy of the allowance for loan losses, see the *Allowance for Loan Loss and Provision for Loan Loss* sections within the Management s Discussion and Analysis of Financial Condition and Results of Operation to follow.

Income Taxes: The Company estimates income tax expense based on the amount it expects to owe various tax authorities. Taxes are discussed in more detail in Note 11, Income Taxes within *Notes to the Consolidated Financial Statements* included in Item 8 hereof. Accrued taxes represent the net estimated amount due to or to be received from taxing authorities in the current year. In estimating accrued taxes, management assesses the relative merits and risks of the appropriate tax treatment of transactions taking into account statutory, judicial and regulatory guidance in the context of our tax position. Deferred tax assets/liabilities represent differences between when a tax benefit or expense is recognized for book purposes and on the Company s tax return. Future tax assets are assessed for recoverability. The Company would record a valuation allowance if it believes based on available evidence, that it is more likely than not that the future tax assets recognized will not be realized before their expiration. The amount of the future income tax asset recognized and considered realizable could be reduced if projected income is not achieved due to various factors such as unfavorable business conditions. If projected income is not expected to be achieved, the Company would record a valuation allowance to reduce its future tax assets to the amount that it believes can be realized in its future tax returns. The Company has no recorded tax valuation allowance as of December 31, 2005. Additionally, deferred tax assets/liabilities are calculated based on tax rates expected to be in effect in future periods. Previously recorded tax assets and liabilities need to be adjusted when the expected date of the future event is revised based upon current information.

Valuation of Goodwill/Intangible Assets and Analysis for Impairment: Independent Bank Corp. in part has increased its market share through the acquisition of entire financial institutions accounted for under the purchase method of accounting, as well as from the acquisition of financial institution s branches (not the entire institution). For acquisitions accounted for under the purchase method and the acquisition of financial institution branches, the Company is required to record assets acquired and liabilities assumed at their fair value which is an estimate determined by the use of internal or other valuation techniques. These valuation estimates result in goodwill and other intangible assets. Goodwill is subject to ongoing periodic impairment tests and is evaluated using various fair value techniques including multiples of price/equity and price/earnings ratios. As a result of such impairment testing conducted in 2005 the Company determined goodwill was not impaired.

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Executive Level Overview

The Company s results of operations are largely dependent on net interest income, which is the difference between the interest earned on loans and securities and the interest paid on deposits and borrowings. The results of operations are also affected by the level of income/fees from loans, deposits, mortgage banking, and investment management activities, as well as operating expenses, the provision for loan losses, the impact of federal and state income taxes, and the relative levels of interest rates and economic activity.

The Company reported earnings of $33.2 million for the year ended December 31, 2005 representing growth of 7.9% from the same period last year. Earnings growth in 2005 was primarily due to targeted loan growth funded with strong growth in deposits. The Company also experienced growth in the core non-interest income categories of deposit service charges, mortgage banking revenue, and improved revenue from our wealth management business due to growth in managed assets. The Company s net interest margin remained stable in 2005 due to a number of management initiatives. Non-interest expense increased by 3.6% primarily due to normal increases in salaries and benefits as well as expenses associated with two new branch locations and the full year impact of the Falmouth Bancorp, Inc. acquisition.

Management has focused on earning asset growth in the high value segments of commercial lending and variable rate home equity lines of credit, while placing less emphasis on indirect auto, portfolio residential lending and the securities portfolio. While this strategy has slowed balance sheet growth, management believes it is prudent in the current interest rate environment. The securities portfolio has decreased on both a relative basis (as a percent of earning assets) as well as on an actual basis, reflecting good loan growth and the current flat yield curve environment (see definition below) which management believes not to be conducive to growing the securities portfolio.

The following graph depicts the historical U.S. Treasury yield curve as of December 31, for the years 2003 2005.

Historical U.S. Treasury Yield Curve

A yield curve is a graphic line chart that shows interest rates at a specific point for all securities having equal risk, but different maturity dates.[3] *A flat yield curve is one in which there is little difference between short-term and long-term rates for bonds of the same credit quality. When short- and long-term bonds are offering equivalent yields, there is usually little benefit in holding the longer-term instruments that is, the investor does not gain any excess compensation for the risks associated with holding longer-term securities. For example, a flat yield curve on U.S. Treasury Securities would be one in which the yield on a two-year bond is 5% and the yield on a 30-year bond is 5.1%.*[4]

[3] The Free Dictionary.com
[4] Investopedia.com

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The following pie charts present earning assets by type as a percent of total earning assets for the time period indicated below:

Earning Asset Profile

The following graph presents the decline in the securities portfolio throughout 2005:

Total Securities
(Dollars in Millions)

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Deposit growth of $145.3 million, or 7.1%, was strong in 2005 despite the intense competitive pricing in the Company s market area. The majority of deposit growth was experienced in time deposits which grew by $79.9 million, or 17.8%, and money market deposits which grew by $49.6 million, or 9.9%. The Company remains committed to deposit generation, with careful management of deposit pricing and selective deposit promotion, in an effort to control the Company s cost of funds.

Deposits
(Dollars in Millions)

While changes in the prevailing interest rate environment have and will continue to have an impact on the level of the Company s earnings, management strives to mitigate volatility in net interest income resulting from changes in benchmark interest rates through adjustable rate asset generation, effective liability management, and utilization of off-balance sheet interest rate derivatives. (For a discussion of interest rate derivatives and interest rate sensitivity see the Asset/Liability section and Market Risk section and Table 19 Interest Rate Sensitivity within the Market Risk section of the *Management Discussion and Analysis of Financial Condition and Results of Operations* hereof.)

In 2006, assuming a similar interest rate environment, the Company expects the net interest margin to gradually expand to the 4.00% level from the 3.88% experienced during 2005, with deposit pricing being a key determinant. Competition for deposit generation in the Company s footprint is expected to remain strong.

Asset quality continues to be a highlight for the Company and is not anticipated to change significantly in the near term. Non-performing assets at December 31, 2005 were $3.3 million, or 0.11%, of total assets, as compared to $2.7 million, or 0.09%, of total assets at December 31, 2004.

The following graph depicts the Company s non-performing assets and the ratio of non-performing assets to total assets at the periods indicated.

Asset Quality Highlights
(Dollars in Millions)

2005 was a year of many accomplishments. Management is confident that these accomplishments will serve to enhance the Company s performance in 2006 and beyond.

2005 Significant Accomplishments

Improved and expanded business development across all business units and channels.

Extended bank branch hours across our network, and added Sunday hours in busy retail markets. By increasing convenience and offering customers the products and services that they need, the Company was able to increase both core consumer checking households and core business checking customers.

Introduced a market-leading Remote Deposit Capture product, enabling business customers to scan and deposit checks into their Rockland Trust Company account directly from their place of business.

Implemented a new service model in the Bank s Investment Management Group that increased client satisfaction and the Company s productivity. Assets under management at the end of 2005 reached $680.1 million, an increase of $116.1 million, or 20.6%, from 2004.

Made capital contributions to Rockland Trust Community Development LLC, a community development subsidiary, during 2005 to the full extent of its award under the federal New Markets Tax Credit program. Making this contribution allowed the Company to recognize the full amount of the New Market Tax Credit for the year of $1.5 million, and will make the Company eligible to realize additional tax credits totaling $9.5 million between 2006 and 2011. By year-end that contribution had been used to make almost $20.0 million in commercial loans, on favorable terms and conditions, to qualified borrowers in severely economically distressed areas throughout southeastern Massachusetts.

Developed and opened the Rockland Trust eMortgageCenter (www.RocklandTrust.Com/Mortgage), enabling customers to get on-line residential loan pre-approval within minutes.

Implemented a new credit rating methodology that increases loan rating categories, thus allowing the Company to have an even better understanding of the performance of our commercial portfolio.

Management plans to continue to grow earnings through prudent balance sheet management. Asset growth will focus upon commercial and home equity lending, and the securities portfolio will be deemphasized. Deposit origination will focus upon core household checking account generation. Management also intends to continue the growth of primary non-interest income lines, and to maintain its persistent attentiveness to non-interest expense control.

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Financial Position

The Company s total assets increased by $97.8 million, or 3.3%, from $2.9 billion at December 31, 2004 to $3.0 billion at December 31, 2005. Total average assets were $3.0 billion and $2.7 billion in 2005 and 2004, respectively. These increases were primarily due to growth in loans. Total liabilities and stockholders equity increased by $97.8 million in 2005, primarily due to growth in money market and time certificates of deposits. During 2004, the Company completed the acquisition of Falmouth Bancorp, Inc., parent of Falmouth Co-Operative Bank (Falmouth) resulting in total assets acquired of $158.4 million, total liabilities assumed of $141.6 million, or $16.8 million of net assets.

Loan Portfolio Management is focusing on earning asset growth in the high value sections of commercial lending and variable rate home equity lines of credit, while placing less emphasis on indirect auto and portfolio residential lending and the securities portfolio. While this strategy has slowed balance sheet growth, management believes it is prudent in the current interest rate environment. At December 31, 2005, the Bank s loan portfolio amounted to $2.0 billion, an increase of $124.5 million, or 6.5%, from year-end 2004. This increase was primarily in commercial real estate and construction loans, which increased $84.0 million, or 11.3%, and consumer home equity lines which increased $57.2 million, or 29.4%. Consumer auto loans decreased $20.8 million, or 7.3%, and the consumer other category increased $1.7 million, or 3.2%. Business banking loans increased $7.7 million, or 17.6%. Residential real estate loans decreased $4.1 million, or 0.9% and commercial and industrial loans decreased $1.2 million, or 0.8%.

In accordance with governing banking statutes, Rockland is permitted, with certain exceptions, to make loans and commitments to any one borrower, including related entities, in the aggregate amount of not more than 20% of the Bank s stockholders equity, or $52.7 million at December 31, 2005. Notwithstanding the foregoing, the Bank has established a more restrictive limit of not more than 75% of the Bank s legal lending limit, or $39.5 million at December 31, 2005, which may only be exceeded with the approval of the Board of Directors. There were no borrowers whose total indebtedness in aggregate exceeded $39.5 million as of December 31, 2005.

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The following table sets forth information concerning the composition of the Bank s loan portfolio by loan type at the dates indicated.

Table 2 Loan Portfolio Composition

	At December 31,								
	2005		2004		2003		2002		2
	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent	Amoun
	(Dollars in thousands)								
Industrial	$ 155,081	7.6%	$ 156,260	8.2%	$ 161,675	10.2%	$ 143,074	10.0%	$ 141,5
l Estate	683,240	33.5%	613,300	32.0%	564,890	35.7%	511,102	35.7%	463,0
nstruction	140,643	6.9%	126,632	6.6%	75,380	4.8%	49,113	3.4%	39,7
g	51,373	2.5%	43,673	2.3%	27,807	1.8%	22,717	1.6%	22,0
Estate	428,343	21.0%	427,556	22.3%	324,052	20.5%	281,452	19.7%	229,1
struction	8,316	0.4%	7,316	0.4%	9,633	0.6%	10,258	0.7%	7,5
s Held for	5,021	0.2%	10,933	0.6%	1,471	0.1%		0.0%	
me Equity	251,852	12.4%	194,647	10.2%	132,629	8.4%	109,122	7.6%	93,4
o	263,179	12.9%	283,964	14.8%	240,504	15.2%	265,690	18.6%	268,6
er	53,760	2.6%	52,077	2.7%	43,094	2.7%	39,074	2.7%	33,8
	2,040,808	100.0%	1,916,358	100.0%	1,581,135	100.0%	1,431,602	100.0%	1,298,9
oan	26,639		25,197		23,163		21,387		18,1
	$ 2,014,169		$ 1,891,161		$ 1,557,972		$ 1,410,215		$ 1,280,7

(1) 2002 2001 Residential Loans Held for Sale are classified within Residential Real Estate.

At December 31, 2005, $155.1 million, or 7.6%, of the Bank s gross loan portfolio consisted of commercial and industrial loans, compared to $156.3 million, or 8.2%, at December 31, 2004. The Bank s commercial revolving lines of credit generally are for the purpose of providing working capital to borrowers and may be secured or unsecured. At December 31, 2005, the Bank had $81.9 million outstanding under commercial revolving lines of credit compared to $87.7 million at December 31, 2004, and $160.2 million of unused commitments under such lines at December 31, 2005 compared to $126.6 million in the prior year. As of December 31, 2005, the Bank had $8.9 million in outstanding commitments pursuant to standby letters of credit compared to $7.1 million at December 31, 2004. Floor plan loans, which are included in commercial and industrial loans, and are secured by the automobiles, boats, or other vehicles constituting the dealer s inventory, amounted to $14.2 million as of December 31, 2005 compared to $17.1 million at the prior year-end.

During the first quarter of 2005 the Company reclassified certain commercial and consumer loans associated with the Company s business banking initiative to a new business banking loan category. The business banking initiative was

announced in 2004 and caters to the banking needs of businesses with commercial credit needs of less than $250,000 and revenues of less than $2.5 million. Business banking loans totaled $51.4 million, representing 2.5% of the total loan portfolio during the year ended December 31, 2005, compared to $43.7 million, or 2.3% at December 31, 2004. The Bank had unused business lines of credit of $35.3 million at December 31, 2005 compared to $30.0 million at December 31, 2004.

Real estate loans totaling $1.3 billion comprised 62.0% of gross loans at December 31, 2005, as compared to $1.2 billion, or 61.9%, of gross loans at December 31, 2004. The Bank s real estate loan portfolio included

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$683.2 million in commercial real estate loans at December 31, 2005. This category reflected increases over last year of $69.9 million, or 11.4%. Commercial construction of $140.6 million increased by $14.0 million, or 11.1% compared to year-end 2004. Residential real estate loans, including residential construction and residential loans held for sale, which were $8.3 million and $5.0 million, respectively, at year-end 2005, decreased $4.1 million, or 0.9%, in 2005. During 2005, the Bank sold $191.4 million of the current production of residential mortgages as part of its overall asset/liability management.

Consumer loans primarily consist of automobile, home equity, and other consumer loans. As of December 31, 2005, $568.8 million, or 27.9%, of the Bank s gross loan portfolio, consisted of consumer loans compared to $530.7 million, or 27.6%, of the Bank s gross loans at December 31, 2004. Home equity loans may be made as a term loan or under a revolving line of credit secured by a first or second mortgage on the borrower s residence. Consumer home equity loans of $251.9 million, increased $57.2 million, or 29.4%, in 2005 and represented 44.3% of the total consumer loan portfolio. As of December 31, 2005, there were $199.3 million in unused commitments under revolving home equity lines of credit compared to $162.9 million at December 31, 2004. As of December 31, 2005 and 2004, automobile loans were $263.2 million, representing 46.3%, and $284.0 million, representing 53.5%, respectively, of the Bank s consumer loan portfolio. As of December 31, 2005, other consumer loans amounted to $53.8 million compared to $52.1 million as of December 31, 2004. These loans largely consisted of loans secured by recreational vehicles, motor homes, boats, mobile homes, and motorcycles and cash reserve loans. Cash reserve loans are designed to afford the Bank s customers overdraft protection. Cash reserve loans are made pursuant to previously approved unsecured cash reserve lines of credit and the rate on these loans is subject to change due to market conditions. As of December 31, 2005 and 2004, $19.5 million and $20.6 million, respectively, had been committed to but was unused under cash reserve lines of credit.

The following table sets forth the scheduled contractual amortization of the Bank s loan portfolio at December 31, 2005. Loans having no schedule of repayments or no stated maturity are reported as due in one year or less. Adjustable rate mortgages are included in the adjustable rate category. The following table also sets forth the rate structure of loans scheduled to mature after one year.

Table 3 Scheduled Contractual Loan Amortization At December 31, 2005

	Commercial	Commercial Real Estate	Commercial Construction	Business Banking	Residential Real Estate	Residential Construction	Residential Held for Sale	Consumer Home Equity	Consumer Auto	Consumer Other
					(Dollars in thousands)					
n:										
s	$ 103,562	$ 99,630	$ 66,720	$ 36,905	$ 15,708	$ 475	$ 5,021	$ 3,809	$ 76,114	$ 16,917
	46,318	443,862	54,991	13,525	69,212			13,770	182,317	18,388
	5,201	139,748	18,932	943	343,423	7,841		234,273	4,748	18,455
	$ 155,081	$ 683,240	$ 140,643	$ 51,373	$ 428,343	$ 8,316	$ 5,021	$ 251,852	$ 263,179	$ 53,760

	$ 31,995	$ 501,704	$ 22,362	$ 14,468	$ 142,817	$	$	$ 37,854	$ 187,065	$ 36,843
e	19,524	81,906	51,561		269,818	7,841		210,189		

As of December 31, 2005, $174,000 of loans scheduled to mature within one year were nonperforming.

Generally, the actual maturity of loans is substantially shorter than their contractual maturity due to prepayments and, in the case of real estate loans, due-on-sale clauses, which generally gives the Bank the right to declare a loan immediately due and payable in the event that, among other things, the borrower sells the property subject to the mortgage and the loan is not repaid. The average life of real estate loans tends to increase when current real estate loan rates are higher than rates on mortgages in the portfolio and, conversely, tends to decrease when rates on mortgages in the portfolio are higher than current real estate loan rates. Under the latter scenario, the weighted average yield on the portfolio tends to decrease as higher yielding loans are repaid or refinanced at lower rates. Due to the fact that the Bank may, consistent with industry practice, roll over a significant portion of commercial and commercial real estate loans at or immediately prior to their maturity by renewing the loans on substantially similar or revised terms, the principal repayments actually received by the Bank are anticipated to be significantly less than

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the amounts contractually due in any particular period. In addition, a loan, or a portion of a loan, may not be repaid due to the borrower s inability to satisfy the contractual obligations of the loan.

Residential mortgage loans originated for sale are classified as held for sale. These loans are specifically identified and carried at the lower of aggregate cost or estimated market value. Forward commitments to sell residential real estate mortgages are contracts that the Bank enters into for the purpose of reducing the market risk associated with originating loans for sale should interest rates change. Forward commitments to sell as well as commitments to originate rate-locked loans intended for sale are recorded at fair value.

During 2005 and 2004, the Bank originated residential loans with the intention of selling these loans in the secondary market. Loans are sold both with servicing rights released and servicing rights retained. Loans originated and sold with servicing rights released were $171.3 million and $110.4 million in 2005 and 2004, respectively. Loans originated and sold with servicing rights retained were $20.1 million and $34.6 million in 2005 and 2004, respectively.

The principal balance of loans serviced by the Bank on behalf of investors amounted to $336.5 million at December 31, 2005 and $392.0 million at December 31, 2004. The fair value of the servicing rights associated with these loans was $2.9 million and $3.3 million as of December 31, 2005 and 2004, respectively.

Asset Quality Rockland Trust Company actively manages all delinquent loans in accordance with formally drafted policies and established procedures. In addition, Rockland Trust Company s Board of Directors reviews delinquency statistics, by loan type, on a monthly basis.

Delinquency The Bank s philosophy toward managing its loan portfolios is predicated upon careful monitoring which stresses early detection and response to delinquent and default situations. The Bank seeks to make arrangements to resolve any delinquent or default situation over the shortest possible time frame. Generally, the Bank requires that a delinquency notice be mailed to a borrower upon expiration of a grace period (typically no longer than 15 days beyond the due date). Reminder notices and telephone calls may be issued prior to the expiration of the grace period. If the delinquent status is not resolved within a reasonable time frame following the mailing of a delinquency notice, the Bank s personnel charged with managing its loan portfolios, contacts the borrower to ascertain the reasons for delinquency and the prospects for payment. Any subsequent actions taken to resolve the delinquency will depend upon the nature of the loan and the length of time that the loan has been delinquent. The borrower s needs are considered as much as reasonably possible without jeopardizing the Bank s position. A late charge is usually assessed on loans upon expiration of the grace period.

On loans secured by one-to-four family, owner-occupied properties, the Bank attempts to work out an alternative payment schedule with the borrower in order to avoid foreclosure action. If such efforts do not result in a satisfactory arrangement, the loan is referred to legal counsel whereupon counsel initiates foreclosure proceedings. At any time prior to a sale of the property at foreclosure, the Bank may and will terminate foreclosure proceedings if the borrower is able to work out a satisfactory payment plan. On loans secured by commercial real estate or other business assets, the Bank similarly seeks to reach a satisfactory payment plan so as to avoid foreclosure or liquidation.

The following table sets forth a summary of certain delinquency information as of the dates indicated:

Table 4 Summary of Delinquency Information

	At December 31, 2005				At December 31, 2004			
	60-89 days		90 days or more		60-89 days		90 days or more	
	Number of Loans	Principal Balance	Number of Loans	Principal Balance	Number of Loans	Principal Balance	Number of Loans	Principal Balance
	(Dollars in thousands)							
Commercial and Industrial	2	$ 24	4	$ 209	1	$ 130	4	$ 207
Commercial Real Estate	3	2,892	2	288	1	188	2	227
Commercial Construction								
Business Banking	5	97	3	47	1	11	7	311
Residential Real Estate	4	1,337	2	373	3	764	4	173
Residential Construction								
Consumer Home Equity								
Consumer Auto(1)	65	597	61	572	N/A	N/A	N/A	N/A
Consumer Other	18	112	17	110	76	626	92	315
Total	97	$ 5,059	89	$ 1,599	82	$ 1,719	109	$ 1,233

(1) For periods prior to December 31, 2005, Consumer-Auto loans are included in Consumer-Other.

Delinquencies have increased year over year mainly due to two commercial real estate credits and one residential real estate loan, all of which the Company believes to be adequately collateralized. The increase in consumer delinquency is generally a result of the recent changes in bankruptcy laws.

Nonaccrual Loans As permitted by banking regulations, consumer loans and home equity loans past due 90 days or more continue to accrue interest. In addition, certain commercial and real estate loans that are more than 90 days past due may be kept on an accruing status if the loan is well secured and in the process of collection. As a general rule, a commercial or real estate loan more than 90 days past due with respect to principal or interest is classified as a nonaccrual loan. Income accruals are suspended on all nonaccrual loans and all previously accrued and uncollected interest is reversed against current income. A loan remains on nonaccrual status until it becomes current with respect to principal and interest (and in certain instances remains current for up to three months), when the loan is liquidated, or when the loan is determined to be uncollectible it is charged-off against the allowance for loan losses.

Nonperforming Assets Nonperforming assets are comprised of nonperforming loans, nonperforming securities and Other Real Estate Owned (OREO). Nonperforming loans consist of loans that are more than 90 days past due but still accruing interest and nonaccrual loans. OREO includes properties held by the Bank as a result of foreclosure or by acceptance of a deed in lieu of foreclosure. As of December 31, 2005, nonperforming assets totaled $3.3 million, an increase of $637,000 or 23.6%, from the prior year-end. Nonperforming assets represented 0.11% of total assets for the year ending December 31, 2005 and 0.09% for the year ending December 31, 2004. The Bank had one property

held as OREO for the period ending December 31, 2005 and did not hold any OREO for the period ending December 31, 2004.

Repossessed automobile loan balances continue to be classified as nonperforming loans, and not as other assets, because the borrower has the potential to satisfy the obligation within twenty days from the date of repossession (before the Bank can schedule disposal of the collateral). The borrower can redeem the property by payment in full at any time prior to the disposal of it by the Bank. Repossessed automobile loan balances amounted to $509,000 and $594,000 for the periods ending December 31, 2005, and December 31, 2004, respectively.

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The following table sets forth information regarding nonperforming assets held by the Bank at the dates indicated.

Table 5 Nonperforming Assets

	At December 31, 2005	2004	2003	2002	2001
	(Dollars in thousands)				
Loans past due 90 days or more but still accruing					
Consumer Home Equity	$	$	$	$	$ 292
Consumer Auto	165	72	128	220	167
Consumer Other	62	173	28	41	49
Total	$ 227	$ 245	$ 156	$ 261	$ 508
Loans accounted for on a nonaccrual basis(1)					
Commercial and Industrial	$ 245	$ 334	$ 971	$ 300	$ 505
Business Banking(2)	47	N/A	N/A	N/A	N/A
Commercial Real Estate	313	227	691	1,320	618
Residential Real Estate	1,876	1,193	926	533	848
Consumer Auto	509	594	714	656	487
Consumer Other	122	109	56	7	49
Total	$ 3,112	$ 2,457	$ 3,358	$ 2,816	$ 2,507
Total nonperforming loans	$ 3,339	$ 2,702	$ 3,514	$ 3,077	$ 3,015
Total nonperforming assets	$ 3,339	$ 2,702	$ 3,514	$ 3,077	$ 3,015
Restructured loans	$ 377	$ 416	$ 453	$ 497	$ 503
Nonperforming loans as a percent of gross loans	0.16%	0.14%	0.22%	0.21%	0.23%
Nonperforming assets as a percent of total assets	0.11%	0.09%	0.14%	0.13%	0.14%

(1) There were no restructured, nonaccruing loans at December 31, 2005, 2004, 2003 and 2002. In 2001 there were $0.1 million of restructured nonaccruing loans.

(2) For the periods prior to December 31, 2005, Business Banking loans are included in Commercial and Industrial and Consumer Other.

In the course of resolving nonperforming loans, the Bank may choose to restructure the contractual terms of certain commercial and real estate loans. Terms may be modified to fit the ability of the borrower to repay in line with its current financial status. It is the Bank s policy to maintain restructured loans on nonaccrual status for approximately six months before management considers its return to accrual status. At December 31, 2005 and 2004, the Bank had $377,000 and $416,000, respectively, of restructured loans.

Potential problem loans are any loans, which are not included in nonaccrual or non-performing loans and which are not considered troubled debt restructures, where known information about possible credit problems of the borrowers causes management to have concerns as to the ability of such borrowers to comply with present loan repayment terms. At December 31, 2005 and 2004, the Bank had nine and four potential problem loan relationships, respectively, which are not included in nonperforming loans with an outstanding balance of $30.3 million and $10.7 million, respectively. At December 31, 2005, problem loans continued to perform and the Company s management actively monitors these loans to minimize any possible adverse impact to the Bank.

Real estate acquired by the Bank through foreclosure proceedings or the acceptance of a deed in lieu of foreclosure is classified as OREO. When property is acquired, it is recorded at the lesser of the loan s remaining principal balance or the estimated fair value of the property acquired, less estimated costs to sell. Any loan balance

in excess of the estimated fair value less estimated cost to sell on the date of transfer is charged to the allowance for loan losses on that date. All costs incurred thereafter in maintaining the property, as well as subsequent declines in fair value are charged to non-interest expense.

Interest income that would have been recognized for the years ended December 31, 2005, 2004 and 2003, if nonperforming loans at the respective dates had been performing in accordance with their original terms approximated $282,000, $312,000, and $210,000, respectively. The actual amount of interest that was collected on these nonaccrual and restructured loans during each of those periods and included in interest income was approximately $103,000, $140,000, and $261,000, respectively.

A loan is considered impaired when, based on current information and events, it is probable that the Bank will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower s prior payment record, and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan by loan basis for commercial, commercial real estate, and construction loans by either the present value of expected future cash flows discounted at the loan s effective interest rate, the loan s obtainable market price, or the fair value of the collateral if the loan is collateral dependent.

Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. Accordingly, the Bank does not separately identify individual, consumer, or residential loans for impairment disclosures. At December 31, 2005, impaired loans include all commercial real estate loans and commercial and industrial loans on nonaccrual status and restructured loans and certain potential problem loans for which a collateral deficit exists and a specific allocation of allowance for loan loss has been assigned. Total impaired loans at December 31, 2005 and 2004 were $935,000 and $2.6 million, respectively.

Allowance for Loan Losses While management uses available information to recognize losses on loans, future additions to the allowance may be necessary based on increases in nonperforming loans, changes in economic conditions, or for other reasons. Various regulatory agencies, as an integral part of their examination process, periodically review the Bank s allowance for loan losses. Federal Reserve regulators examined the Company in the third quarter of 2004 and the Bank was most recently examined by the Federal Deposit Insurance Corporation, FDIC , in the first quarter of 2005. No additional provision for loan losses was required as a result of these examinations.

The allowance for loan losses is maintained at a level that management considers adequate to provide for probable loan losses based upon evaluation of known and inherent risks in the loan portfolio. The allowance is increased by provisions for loan losses and by recoveries of loans previously charged-off and reduced by loans charged-off. Additionally, in 2004 the Bank s allowance increased by $870,000 upon acquisition of Falmouth Bancorp, Inc. This increase represents management s estimate of potential inherent losses in the acquired portfolio.

The Bank s total allowances for loan losses as of December 31, 2005 was $26.6 million, or 1.31%, of total loans as compared to $25.2 million, or 1.31% of total loans at December 31, 2004.

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The following table summarizes changes in the allowance for loan losses and other selected statistics for the periods presented:

Table 6 Summary of Changes in the Allowance for Loan Losses

	Year Ending December 31,				
	2005	2004	2003	2002	2001
	(Dollars in thousands)				
Average total loans	$ 1,987,591	$ 1,743,844	$ 1,512,997	$ 1,345,720	$ 1,237,230
Allowance for loan losses, beginning of year	$ 25,197	$ 23,163	$ 21,387	$ 18,190	$ 15,493
Charged-off loans:					
Commercial and Industrial	120	181	195	134	144
Business Banking(1)	505	N/A	N/A	N/A	N/A
Commercial Real Estate					
Residential Real Estate					63
Commercial Construction					
Residential Construction					
Consumer Home Equity					
Consumer Auto	1,772	2,089	1,938	1,958	2,115
Consumer Other	1,077	329	196	373	404
Total charged-off loans	3,474	2,599	2,329	2,465	2,726
Recoveries on loans previously charged-off:					
Commercial and Industrial	85	214	283	628	194
Business Banking(1)	14	N/A	N/A	N/A	N/A
Commercial Real Estate	128	2	2	2	71
Residential Real Estate		30			
Commercial Construction					
Residential Construction					
Consumer Home Equity	20				
Consumer Auto	350	372	321	286	447
Consumer Other	144	127	79	96	92
Total recoveries	741	745	685	1,012	804
Net loans charged-off	2,733	1,854	1,644	1,453	1,922
Allowance related to business combinations		870			
Provision for loan losses	4,175	3,018	3,420	4,650	4,619
Allowance for loan losses, end of period	$ 26,639	$ 25,197	$ 23,163	$ 21,387	$ 18,190

Credit quality discount on acquired loans(2)								518		810
Total allowances for loan losses, end of year	$	26,639	$	25,197	$	23,163	$	21,905	$	19,000
Net loans charged-off as a percent of average total loans		0.14%		0.11%		0.11%		0.11%		0.16%
Allowance for loan losses as a percent of total loans		1.31%		1.31%		1.46%		1.49%		1.40%
Allowance for loan losses as a percent of nonperforming loans		797.81%		932.53%		659.16%		695.06%		603.32%
Total allowances for loan losses as a percent of total loans (including credit quality discount)		1.31%		1.31%		1.46%		1.53%		1.46%
Total allowance for loan losses as a percent of nonperforming loans (including credit quality discount)		797.81%		932.53%		659.16%		711.89%		630.18%
Net loans charged-off as a percent of allowance for loan losses		10.26%		7.36%		7.10%		6.79%		10.57%
Recoveries as a percent of charge-offs		21.33%		28.66%		29.41%		41.05%		29.49%

(1) For periods prior to December 31, 2005, Business Banking loans are included in Commercial and Industrial and Consumer-Other.

(2) The Bank established a separate credit quality discount in 2000 as a reduction of the loan balances acquired from FleetBoston Financial. The credit quality discount was fully utilized by 2003.

The allowance for loan losses is allocated to various loan categories as part of the Bank s process of evaluating the adequacy of the allowance for loan losses. Allocated allowances increased by approximately $1.7 million to $24.1 million at December 31, 2005. Increased amounts of allowance were allocated to five major loan categories: commercial real estate, business banking, real estate construction, consumer home equity, and consumer other. The increased amounts allocated to these loan categories represented substantially all of the increase in the allocated allowance amounts, as compared to December 31, 2004. Decreased allowances were posted in commercial & industrial, residential real estate, and consumer auto, due mainly to a lower level of outstanding loan balances from the end of 2004.

The decrease of 7.5% in allowance allocated to the commercial and industrial category is attributed to the risk rating changes of certain loan balances and to portfolio turnover. Additionally, those loan balances in certain commercial and industrial loan groupings that have been repaid were replaced by newly originated loan balances that have been placed into other loan groupings within this loan category that require different levels of allocated allowance based upon the ascertainable risk characteristics of those loans.

The decrease in the amount of allowance allocated to the consumer auto loan category of 7.4% reflects a 7.3% decrease in loan balances, from December 31, 2004 to December 31, 2005.

The increase in the amount of allowance allocated to the commercial real estate category is due to loan balance growth within this loan category attributed to new loan origination and risk rating changes of certain loan balances. Loan balances outstanding in this portfolio, at December 31, 2005, increased by 11.4%, while the amount of allowance allocated to this portfolio grew by 11.7%, as compared to December 31, 2004. The amount of allowance allocated reflects increases in loan balances distributed among certain loan types within commercial real estate that require different levels of allocated allowance based upon the ascertainable risk characteristics of those loans.

The increase in the amount of allowance allocated to the real estate construction portfolio is due to loan balance growth within this portfolio attributed to new loan origination and the risk rating changes of certain loan balances. Loan balances outstanding in this portfolio component, at December 31, 2005, increased by 11.2%, while the corresponding amount of allowance allocated increased by 19.6%, as compared to December 31, 2004. The amount of allowance allocated within the real estate construction portfolio reflects loan balance growth distributed among certain loan groupings within this portfolio that require different levels of allocated allowance based upon the ascertainable risk characteristics of those loans.

The increase in the amount of allowance allocated to the consumer-home equity portfolio is due to growth in this loan portfolio attributed to new loan origination. Outstanding balances at December 31, 2005 grew by 29.4% as compared to the amount shown at December 31, 2004, while the corresponding amount of allowance allocated increased by 29.5%, as compared to December 31, 2004.

The increase in the amount of allowance allocated to the consumer-other loan portfolio reflects 3.2% growth in loan balances as compared to December 31, 2004. Consumer-other is comprised of other consumer loan product types including non-auto installment loans, overdraft lines and other credit line facilities.

The increase in the amount of allowance allocated to the business banking portfolio component resulted from a 17.6% increase in loan balances as compared to December 31, 2004.

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The following table summarizes the allocation of the allowance for loan losses for the years indicated:

Table 7 Summary of Allocation of Allowance for Loan Losses

	At December 31,										
	2005		2004		2003		2002			20	
	Allowance Amount	Percent of Loans In Category To Total Loans	Allowance Amount	Percent of Loans In Category To Total Loans	Allowance Amount	Percent of Loans In Category To Total Loans	Allowance Amount	Credit Quality Discount	Percent of Loans In Category To Total Loans	Allowance Amount	Cr Qu Dis
	(Dollars in thousands)										
ce:											
	$ 3,134	7.6%	$ 3,387	8.2%	$ 4,653	10.8%	$ 3,435	$ 10	10.6%	$ 3,036	$
(1)	1,193	2.5%	1,022	2.3%	N/A	N/A	N/A	N/A	N/A	N/A	
Estate	11,554	33.5%	10,346	32.0%	9,604	35.7%	7,906	419	35.7%	6,751	
uction	3,474	7.3%	2,905	7.0%	1,389	5.4%	1,196		4.1%	1,152	
state	650	21.2%	659	22.9%	488	20.6%	422		19.7%	343	
e Equity	755	12.4%	583	10.1%	398	8.4%	304	63	7.6%	247	
	2,629	12.9%	2,839	14.8%	2,399	15.2%	2,623	22	18.6%	2,638	
	757	2.6%	667	2.7%	1,244	3.9%	1,073	4	3.7%	983	
ance	2,493	N/A	2,789	N/A	2,988	N/A	4,428		N/A	3,040	
or Loan	$ 26,639	100.0%	$ 25,197	100.0%	$ 23,163	100.0%	$ 21,387	$ 518	100.0%	$ 18,190	$

(1) For the periods prior to December 31, 2004, Business Banking loans are included in Commercial and Industrial and Consumer Other.

Allocated allowance for loan losses are determined using both a formula-based approach applied to groups of loans and an analysis of certain individual loans for impairment.

The formula-based approach evaluates groups of loans to determine the allocation appropriate within each portfolio section. Individual loans within the commercial and industrial, commercial real estate and real estate construction loan portfolio sections are assigned internal risk ratings to group them with other loans possessing similar risk characteristics. The level of allowance allocable to each group of risk-rated loans is then determined by management applying a loss factor that estimates the amount of probable loss inherent in each category. The assigned loss factor for each risk rating is a formula-based assessment of historical loss data, portfolio characteristics, economic trends, overall market conditions, past experience and management s analysis of considerations of probable loan loss based on these factors.

During the quarter-ended March 31, 2005, enhancements to the Bank s internal risk-rating framework were implemented. These enhancements refine the definitional detail of the risk attributes and characteristics that compose each risk grouping and add granularity to the assessment of credit risk across those defined risk groupings.

Allocations for business banking, residential real estate and other consumer loan categories are principally determined by applying loss factors that represent management s estimate of probable or expected losses inherent in those categories. In each section, inherent losses are estimated, based on a formula-based assessment of historical loss data, portfolio characteristics, economic trends, overall market conditions, past loan loss experience and management s considerations of probable loan loss based on these factors.

The other method used to allocate allowances for loan losses entails the assignment of allowance amounts to individual loans on the basis of loan impairment. Certain loans are evaluated individually and are judged to be impaired when management believes it is probable that the Bank will not collect all of the contractual interest and principal payments as scheduled in the loan agreement. Under this method, loans are selected for evaluation based

upon a change in internal risk rating, occurrence of delinquency, loan classification or non-accrual status. A specific allowance amount is allocated to an individual loan when such loan has been deemed impaired and when the amount of a probable loss is able to be estimated on the basis of: (a) the present value of anticipated future cash flows or on the loan s observable fair market value or (b) the fair value of collateral if the loan is collateral dependent. Loans with a specific allowance and the amount of such allowance totaled $558,000 and $1,000, respectively, at December 31, 2005 and $1.1 million and $400,000, respectively, at December 31, 2004.

A portion of the allowance for loan loss is not allocated to any specific section of the loan portfolio. This non-specific allowance is maintained for two primary reasons: (a.) there exists an inherent subjectivity and imprecision to the analytical processes employed and (b.) the prevailing business environment, as it is affected by changing economic conditions and various external factors, may impact the portfolio in ways currently unforeseen. Moreover, management has identified certain risk factors, which could impact the degree of loss sustained within the portfolio. These include: (a.) market risk factors, such as the effects of economic variability on the entire portfolio, and (b.) unique portfolio risk factors that are inherent characteristics of the Bank s loan portfolio. Market risk factors may consist of changes to general economic and business conditions that may impact the Bank s loan portfolio customer base in terms of ability to repay and that may result in changes in value of underlying collateral. Unique portfolio risk factors may include industry concentration or covariant industry concentrations, geographic concentrations or trends that may exacerbate losses resulting from economic events which the Bank may not be able to fully diversify out of its portfolio.

Due to the imprecise nature of the loan loss estimation process and ever changing conditions, these risk attributes may not be adequately captured in data related to the formula-based loan loss components used to determine allocations in the Bank s analysis of the adequacy of the allowance for loan losses. Management, therefore, has established and maintains an imprecision allowance for loan losses reflecting the uncertainty of future economic conditions within the Bank s market area. The amount of this measurement imprecision allocation was $2.5 million at December 31, 2005.

Inflationary concerns resulting from higher energy and commodity prices, potential downward pressure on housing prices, fluctuating interest rates, and changes in the level of employment are just some of the drivers that could impact local and regional economic growth and the banking environment in the near term. Unforeseen changes in the economy can impact the risk characteristics of the Bank s loan portfolio. As such, management maintains the imprecision allowance based on its analysis of regional and local economic conditions.

As of December 31, 2005, the allowance for loan losses totaled $26.6 million as compared to $25.2 million at December 31, 2004. Based on the processes described above, management believes that the level of the allowance for possible loan losses at December 31, 2005 is adequate.

Securities Portfolio The Company s securities portfolio consists of trading assets, securities available for sale, securities which management intends to hold until maturity, and Federal Home Loan Bank (FHLB) stock. Equity securities which are held for the purpose of funding Rabbi Trust obligations (*see Note 13 Employee Benefits of the Notes to Consolidated Financial Statements* in Item 8 hereof). are classified as trading assets. Trading assets are recorded at fair value with changes in fair value recorded in earnings. Trading assets were $1.6 million at December 31, 2005 and 2004.

Securities which management intends to hold until maturity consist of mortgage-backed securities, state, county and municipal securities and corporate debt securities. Securities held to maturity as of December 31, 2005 are carried at their amortized cost of $104.3 million and exclude gross unrealized gains of $2.7 million and gross unrealized losses of $230,000. A year earlier, securities held to maturity totaled $108.0 million excluding gross unrealized gains of $4.6 million and gross unrealized losses of $370,000.

Securities available for sale consist of certain, U.S. Treasury and U.S. Government agency obligations, mortgage-backed securities, collateralized mortgage obligations, and state, county and municipal securities. These securities are carried at fair value and unrealized gains and losses, net of applicable income taxes, are recognized as a separate component of stockholders equity. The fair value of securities available for sale at December 31, 2005 totaled $581.5 million including the associated pre-tax net unrealized loss totaled $14.4 million. A year earlier, securities available for sale were $680.3 million including a pre-tax net unrealized loss of $327,000. In 2005 and

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2004, the Company recognized $616,000 and $1.5 million, respectively of net gains on the sale of available for sale securities.

The following table sets forth the amortized cost and percentage distribution of securities held to maturity at the dates indicated.

Table 8 Amortized Cost of Securities Held to Maturity

	At December 31,					
	2005		2004		2003	
	Amount	Percent	Amount	Percent	Amount	Percent
	(Dollars in thousands)					
Mortgage-Backed Securities	$ 6,936	6.7%	$ 8,971	8.3%	$ 13,156	10.8%
State, County and Municipal Securities	41,628	39.9%	43,084	39.9%	47,266	38.8%
Corporate Debt Securities	55,704	53.4%	55,912	51.8%	61,472	50.4%
Total	$ 104,268	100.0%	$ 107,967	100.0%	$ 121,894	100.0%

The following table sets forth the fair value and percentage distribution of securities available for sale at the dates indicated.

Table 9 Fair Value of Securities Available for Sale

	At December 31,					
	2005		2004		2003	
	Amount	Percent	Amount	Percent	Amount	Percent
	(Dollars in thousands)					
U.S. Treasury and U.S. Government Agency Securities	$ 151,253	26.0%	$ 140,356	20.6%	$ 146,576	27.8%
Mortgage-Backed Securities	257,532	44.3%	349,716	51.4%	181,983	34.5%
Collateralized Mortgage Obligations	150,322	25.8%	170,661	25.1%	178,000	33.7%
State, County and Municipal Securities	22,409	3.9%	19,553	2.9%	20,948	4.0%
Total	$ 581,516	100.0%	$ 680,286	100.0%	$ 527,507	100.0%

The following two tables set forth contractual maturities of the Bank s securities portfolio at December 31, 2005. Actual maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

Table 10 Amortized Cost of Securities Held to Maturity

Amounts Maturing

% of Total	Weighted Average Yield	One Year to Five Years	% of Total	Weighted Average Yield	Five Years to Ten Years	% of Total	Weighted Average Yield	Over Ten Years	% of Total	Weighted Average Yield	Total	% o Tota
					(Dollars in thousands)							
0.0%		$	0.0%		$	0.0%		6,936	6.7%	5.5%	6,936	6
0.0%	5.0%	654	0.6%	4.1%	13,761	13.2%	4.3%	27,175	26.1%	5.0%	41,628	39
0.0%	0.0%		0.0%			0.0%		55,704	53.4%	7.9%	55,704	53
0.0%	5.0%	$ 654	0.6%	4.1%	$ 13,761	13.2%	4.3%	$ 89,815	86.2%	6.9%	$ 104,268	100

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Table 11 Fair Value of Securities Available for Sale

Amounts Maturing

% of otal	Weighted Average Yield	One Year to Five Years	% of Total	Weighted Average Yield	Five Years to Ten Years	% of Total	Weighted Average Yield	Over Ten Years	% of Total	Weighted Average Yield	Total
					(Dollars in thousands)						
0.0%	0.0%	$ 151,253	26.0%	3.7%	$	0.0%	0.0%	$	0.0%	0.0%	$ 151,253
0.0%	0.0%	240	0.0%	8.0%	78,847	13.6%	4.5%	178,445	30.7%	4.7%	257,532
0.0%	0.0%		0.0%	0.0%		0.0%	0.0%	150,322	25.9%	4.0%	150,322
0.6%	3.2%	15,749	2.7%	4.4%	3,260	0.5%	5.5%		0.0%	0.0%	22,409
0.6%	3.2%	$ 167,242	28.7%	3.7%	$ 82,107	14.1%	4.5%	$ 328,767	56.6%	4.4%	$ 581,516

At December 31, 2005 and 2004, the Bank had no investments in obligations of individual states, counties or municipalities which exceeded 10% of stockholders equity. In addition, there were no sales of state, county or municipal securities in 2005 or 2004.

Bank Owned Life Insurance In 1998, the Bank purchased $30.0 million of Bank Owned Life Insurance (BOLI). The Bank purchased these policies for the purpose of protecting itself against the cost/loss due to the death of key employees and to offset the Bank s future obligations to its employees under its retirement and benefit plans. During 2003, certain split dollar life policies with shared ownership between the Bank and certain executives were reassigned in total to the Bank in response to new legislation that considers any payments by a company to a split dollar life policy to be a prohibited loan (see Note 13 Employee Benefits *of the Notes to Consolidated Financial Statements* in Item 8 hereof). The original insurance policies totaling $1.4 million, are now included within the Bank s BOLI portfolio and will be used to fund future obligations to its employees under its retirement and benefits plan. The value of BOLI was $44.8 million and $42.7 million at December 31, 2005 and 2004, respectively. The Bank recorded income from BOLI of $1.8 million in 2005 and $1.9 million in both 2004, and 2003, respectively.

Deposits As of December 31, 2005, deposits of $2.2 billion were $145.3 million, or 7.1%, higher than the prior year-end. Core deposits increased by $65.4 million, or 4.1%. Core deposits consist of demand deposits, savings and

interest checking deposits and money market deposits. The time deposits category increased by $79.9 million, or 17.8%, to $529.1 million at December 31, 2005.

The following table sets forth the average balances of the Bank s deposits for the periods indicated.

Table 12 Average Balances of Deposits

	2005		2004		2003	
	Amount	Percent	Amount	Percent	Amount	Percent
			(Dollars in thousands)			
Demand Deposits	$ 514,611	24.0%	$ 478,073	24.1%	$ 428,396	24.7%
Savings and Interest Checking	599,797	28.0%	570,661	28.8%	494,498	28.5%
Money Market	519,461	24.2%	456,970	23.0%	350,118	20.2%
Time Certificates of Deposits	510,611	23.8%	478,037	24.1%	462,453	26.6%
Total	$ 2,144,480	100.0%	$ 1,983,741	100.0%	$ 1,735,465	100.0%

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The Bank s time certificates of deposit of $100,000 or more totaled $167.2 million at December 31, 2005. The maturity of these certificates is as follows:

Table 13 Maturities of Time Certificate of Deposits Over $100,000

	Balance (In thousands)	Percentage
1 to 3 months	$ 89,706	53.6%
4 to 6 months	31,223	18.7%
7 to 12 months	33,218	19.9%
Over 12 months	13,095	7.8%
Total	$ 167,242	100.0%

Borrowings The Bank s borrowings amounted to $587.8 million at December 31, 2005, a decrease of $67.4 million from year-end 2004. At December 31, 2005, the Bank s borrowings consisted primarily of FHLB borrowings totaling $417.5 million, a decrease of $120.4 million from the prior year-end. The decrease in FHLB borrowings is due to strong deposit growth and the Company s ability to obtain lower cost of funds through federal funds purchased and assets sold under repurchase agreements as well as a reduction in the Company s securities portfolio.

The remaining borrowings consisted of federal funds purchased; assets sold under repurchase agreements, junior subordinated debentures and treasury tax and loan notes. These borrowings totaled $170.3 million at December 31, 2005, an increase of $53.1 million from the prior year-end. See Note 8 Borrowings *of the Notes to Consolidated Financial Statements* included in Item 8 hereof for a schedule of borrowings outstanding and their interest rates and other information related to the Company s borrowings.

Junior Subordinated Debentures The Company formed Independent Capital Trust III (Trust III) and Independent Capital Trust IV (Trust IV) in 2001 and 2002, respectively, for the purposes of issuing Corporation-Obligated Mandatory Redeemable Trust Preferred Securities of Subsidiary Trust Holding Solely Junior Subordinated Debentures of the Corporation (trust preferred securities) and investing the proceeds in junior subordinated securities issued by the Company (the Junior Subordinated Debentures). Additionally, Trust III and Trust IV issued $0.8 million in common securities to the Company. These proceeds were then used to redeem previously issued trust preferred securities issued at higher rates. The Company initially raised this capital for the purposes of supporting asset growth. Under regulatory capital requirements, within certain limitations, the Junior Subordinated Debentures qualify as Tier I and Tier II capital.

Effective March 31, 2004, the Company no longer consolidates its investment in Capital Trust III and Capital Trust IV previously, recorded in the mezzanine section of the balance sheet between liabilities and equity as Corporation-Obligated Mandatory Redeemable Trust Preferred Securities of Subsidiary Trust Holding Solely Junior Subordinated Debentures of the Corporation, due to the adoption of FIN No. 46R (See *FIN No. 46 Consolidation of Variable Interest Entities within Recent Accounting Pronouncements* included in Item 7, hereof). Rather, the Company now classifies its obligation to the trusts within borrowings as *Junior Subordinated Debentures.* Additionally, the distributions payable on these securities and the amortization of the issuance costs are no longer reported as Minority Interest. The interest expense on the debentures, which includes the amortization of the issuance costs, is now captured as borrowings expense.

Junior Subordinated Debentures were $51.5 million at both December 31, 2005 and 2004. The unamortized issuance costs are included in other assets. Unamortized issuance costs were $2.0 million and $2.1 million in 2005 and 2004, respectively.

Minority Interest expense was $1.1 million, and $4.4 million, in 2004, and 2003, respectively. Interest expense on the junior subordinated debentures, reported in borrowings expense, which includes the amortization of the issuance cost, was $4.5 million in 2005 and $3.3 million in 2004.

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The Company unconditionally guarantees all Trust III and Trust IV obligations under the trust preferred securities.

In December, the Trustees of Trust III and Trust IV declared a cash dividend of $0.54 and $0.52 per share to stockholders of record of Trust III and Trust IV, respectively, as of the close of business on December 29, 2005. The dividend was paid on December 30, 2005. The Company has paid on all scheduled dividends.

Investment Management As of December 31, 2005, the Rockland Trust Investment Management Group had assets under management of $680.1 million which represents approximately 1,340 trust, fiduciary, and agency accounts. At December 31, 2004, assets under management were $563.9 million representing approximately 1,215 trust, fiduciary, and agency accounts. Income from the Investment Management Group amounted to $4.9 million, $4.2 million, and $3.8 million for 2005, 2004, and 2003, respectively, and is reported on an accrual basis.

Retail Investments and Insurance For the year ending December 31, 2005, 2004 and 2003 retail investments and insurance income was $404,000, $517,000, and $566,000, respectively. Retail investments and insurance, previously titled mutual fund sales, now includes revenue generated through Independent Financial Market Group (IFMG), a Sun Life Financial Company, IFMG s insurance subsidiary IFS Agencies, Inc. (IFS), and Savings Bank Life Insurance of Massachusetts (SBLI).

RESULTS OF OPERATIONS

Summary of Results of Operations Net income was $33.2 million for the year ended December 31, 2005, compared to $30.8 million for the year ended December 31, 2004. Diluted earnings per share were $2.14 and $2.03 for the years ended 2005 and 2004, respectively.

In 2005 the Company realized $616,000 of security gains as compared to $1.5 million of security gains in 2004. In 2004, the Company also realized a gain on the sale of a branch of $1.8 million, and merger and acquisition expense of $684,000.

Return on average assets and return on average equity was 1.11% and 15.10%, respectively, for the year ending December 31, 2005 as compared to 1.13% and 16.27%, respectively, for the year ending December 31, 2004. Equity to assets was 7.50% as of December 31, 2005 compared to 7.16% for the same period last year.

Net Interest Income The amount of net interest income is affected by changes in interest rates and by the volume, mix, and interest rate sensitivity of interest-earning assets and interest-bearing liabilities.

On a fully tax-equivalent basis, net interest income was $107.7 million in 2005, an 8.0% increase from 2004 net interest income of $99.6 million reported in 2004. This growth comes despite contraction in the net interest margin of 7 basis points from the 3.95% recorded in 2004 to 3.88% in 2005.

Growth in net interest income in 2005 compared with that of 2004 was primarily the result of a 14.0% increase in the average balance of the loan portfolio in 2005 as compared to 2004. The yield on earning assets was 5.68% in 2005, compared with 5.41% in 2004. The average balance of securities decreased by $6.0 million, or 0.8%, as compared with the prior year. The average balance of loans increased by $243.7 million, or 14.0%, and the yield on loans increased by 35 basis points to 6.12% in 2005, compared to 5.77% in 2004. This increase in the yield on earning assets was due to the higher interest rate environment in 2005 than during 2004 and growth in earning assets. During 2005, the average balance of interest-bearing liabilities increased by $215.2 million, or 10.7%, over 2004 average balances. The average cost of these liabilities increased to 2.23% compared to 1.82% in 2004.

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The following table presents the Company s average balances, net interest income, interest rate spread, and net interest margin for 2005, 2004, and 2003. Non-taxable income from loans and securities is presented on a fully tax-equivalent basis whereby tax-exempt income is adjusted upward by an amount equivalent to the prevailing federal income taxes that would have been paid if the income had been fully taxable.

Table 14 Average Balance, Interest Earned/Paid & Average Yields

	Years Ended December 31,								
	2005			2004			2003		
	Average Balance	Interest Earned/ Paid	Average Yield	Average Balance	Interest Earned/ Paid	Average Yield	Average Balance	Interest Earned/ Paid	Av Y
	(Dollars in thousands)								
Earning Assets:									
Funds Sold, Assets ed Under Resale ent and Short Term ents	$ 14,023	$ 515	3.67%	$ 750	$ 17	2.27%	$ 34	$	
es:									
Assets	1,548	36	2.33%	1,507	48	3.19%	1,116	36	
Investment es	708,043	31,188	4.40%	712,663	31,549	4.43%	639,361	29,724	
xable Investment es(1)	62,771	4,126	6.57%	64,215	4,261	6.64%	64,967	4,416	
curities	772,362	35,350	4.58%	778,385	35,858	4.61%	705,444	34,176	
)	1,987,591	121,605	6.12%	1,743,844	100,560	5.77%	1,512,997	95,994	
terest-Earning	$ 2,773,976	$ 157,470	5.68%	$ 2,522,979	$ 136,435	5.41%	$ 2,218,475	$ 130,170	
d Due from Banks	65,703			68,024			64,529		
ssets	144,747			120,550			100,618		
ssets	$ 2,984,426			$ 2,711,553			$ 2,383,622		
Bearing Liabilities:									
:									
and Interest g Accounts	$ 599,797	$ 3,037	0.51%	$ 570,661	$ 2,800	0.49%	$ 494,498	$ 2,302	
Market	519,461	9,549	1.84%	456,970	5,871	1.28%	350,118	4,278	
ertificates of	510,611	13,172	2.58%	478,037	10,254	2.15%	462,453	11,222	
terest Bearing	1,629,869	25,758	1.58%	1,505,668	18,925	1.26%	1,307,069	17,802	
ngs:									

Home Loan Bank ngs	468,821	18,162	3.87%	407,836	13,900	3.41%	356,152	14,236
Funds Purchased ets Sold Under ase Agreements	80,074	1,389	1.73%	61,199	589	0.96%	51,803	482
ubordinated res	51,546	4,469	8.67%	38,871	3,364	8.65%		
Tax and Loan	1,653	40	2.42%	3,154	19	0.60%	2,764	13
rrowings	602,094	24,060	4.00%	511,060	17,872	3.50%	410,719	14,731
terest-Bearing es	$ 2,231,963	$ 49,818	2.23%	$ 2,016,728	$ 36,797	1.82%	$ 1,717,788	$ 32,533
Deposits	514,611			478,073			428,396	
tion-Obligated rily Redeemable es of Subsidiary Solely Parent y Debentures				11,769			47,814	
abilities	17,897			15,849			23,256	
abilities	$ 2,764,471			$ 2,522,419			$ 2,217,254	
lders Equity	219,955			189,134			166,368	
abilities and lders Equity	$ 2,984,426			$ 2,711,553			$ 2,383,622	
rest Income(1)		$ 107,652			$ 99,638			$ 97,637
Rate Spread(2)			3.45%			3.59%		
rest Margin(3)			3.88%			3.95%		
nental Information:								
eposits, Including Deposits	$ 2,144,480	$ 25,758		$ 1,983,741	$ 18,925		$ 1,735,465	$ 17,802
Total Deposits			1.20%			0.95%		
nding Liabilities, g Demand Deposits	$ 2,746,574	$ 49,818		$ 2,494,801	$ 36,797		$ 2,146,184	$ 32,533
Total Funding es			1.81%			1.47%		

(1) The total amount of adjustment to present interest income and yield on a fully tax-equivalent basis is $1,809, $1,822 and $1,864 in 2005, 2004 and 2003, respectively.

(2) Interest rate spread represents the difference between the weighted average yield on interest-earning assets and the weighted average costs of interest-bearing liabilities.

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(3) Net interest margin represents net interest income as a percentage of average interest-earning assets.

The following table presents certain information on a fully-tax equivalent basis regarding changes in the Company s interest income and interest expense for the periods indicated. For each category of interest-earning assets and interest-bearing liabilities, information is provided with respect to changes attributable to (1) changes in rate (change in rate multiplied by prior year volume), (2) changes in volume (change in volume multiplied by prior year rate) and (3) changes in volume/rate (change in rate multiplied by change in volume).

Table 15 Volume Rate Analysis

	Year Ended December 31,										
	2005 Compared To 2004				2004 Compared To 2003				2003 Compare		
	Change Due to Rate	Change Due to Volume	Change Due to Volume/ Rate	Total Change	Change Due to Rate	Change Due to Volume	Change Due to Volume/ Rate	Total Change	Change Due to Rate	Change Due to Volume	C V
					(In thousands)						
ning											
ets e erm	$ 10	$ 301	$ 187	$ 498	$ 1	$ 0	$ 16	$ 17	$ (378)	$ (378)	$
	(13)	1		(12)		12		12	10		
	(157)	(205)	1	(361)	(1,420)	3,408	(163)	1,825	(8,588)	(1,126)	
(1)	(40)	(96)	1	(135)	(105)	(51)	1	(155)	(119)	671	
	(210)	(300)	2	(508)	(1,525)	3,369	(162)	1,682	(8,697)	(455)	
	6,132	14,056	857	21,045	(8,746)	14,646	(1,334)	4,566	(13,569)	12,300	
	$ 5,932	$ 14,057	$ 1,046	$ 21,035	$ (10,270)	$ 18,015	$ (1,480)	$ 6,265	$ (22,644)	$ 11,467	$
ties:											
	$ 89	$ 143	$ 5	$ 237	$ 124	$ 355	$ 19	$ 498	$ (1,011)	$ 481	$
	2,529	803	346	3,678	220	1,306	67	1,593	(1,653)	478	
	2,077	699	142	2,918	(1,302)	378	(44)	(968)	(4,161)	(1,207)	
	4,695	1,645	493	6,833	(958)	2,039	42	1,123	(6,825)	(248)	
nk											
	1,899	2,079	284	4,262	(2,099)	2,067	(305)	(337)	(3,180)	2,955	

ed											
s	472	182	146	800	17	87	3	107	(155)	(196)	
	6	1,097	2	1,105			3,364	3,364			
	57	(9)	(27)	21	4	1	1	6	(24)	(15)	
	2,434	3,349	405	6,188	(2,078)	2,155	3,063	3,140	(3,359)	2,744	
	$ 7,129	$ 4,994	$ 898	$ 13,021	$ (3,036)	$ 4,194	$ 3,105	$ 4,263	$ (10,184)	$ 2,496	$
	$ (1,197)	$ 9,063	$ 148	$ 8,014	$ (7,234)	$ 13,821	$ (4,585)	$ 2,002	$ (12,460)	$ 8,971	$

(1) The total amount of adjustment to present interest income and yield on a fully tax-equivalent basis is $1,809, $1,822 and $1,864 in 2005, 2004 and 2003, respectively.

(2) Loans include portfolio loans, loans held for sale and nonaccrual loans, however unpaid interest on nonperforming loans has not been included for purposes of determining interest income.

Net interest income on a fully tax-equivalent basis increased by $8.0 million in 2005 compared to 2004. Interest income on a fully tax-equivalent basis increased by $21.0 million, or 15.4%, to $157.5 million in 2005 as compared to the prior year-end primarily contributable to the growth in the average loan portfolio of $243.7 million to $2.0 billion during 2005. Based upon loan volume growth alone (not considering the impact of rate change and mix), interest income increased $14.1 million in 2005. Interest income from taxable securities decreased by $361,000, or 1.1%, to $31.2 million in 2005 as compared to the prior year. The overall yield on interest earning assets increased by 5.0% to 5.68% in 2005 as compared to 5.41% in 2004.

Interest expense for the year ended December 31, 2005 increased to $49.8 million from the $36.8 million recorded in 2004, an increase of $13.0 million, or 35.4%, of which $7.1 million is due to the increase in rates on deposits and borrowings. The total cost of funds increased 23.1% to 1.81% for 2005 as compared to 1.47% for 2004. Helping to offset some of the increase in the total cost of funds was a $36.5 million, or 7.6%, increase in non-interest bearing demand deposit balances. Average interest-bearing deposits increased $124.2 million, or 8.2% over prior year along with the cost of these deposits from 1.26%, to 1.58% attributable to both a higher rate environment and increases in higher yielding deposit categories.

Average borrowings increased by $91.0 million, or 17.8%, from the 2004 average balance. The majority of this increase is attributable to an increase in Federal Home Loan Bank borrowings of $61.0 million with an additional $12.7 million of the increase resulting from the inclusion of junior subordinated debentures in borrowings beginning in March of 2004 (see *Junior Subordinated Debentures* in Item 7 hereof.) The average cost of borrowings increased to 4.00% from 3.50%.

Provision For Loan Losses The provision for loan losses represents the charge to expense that is required to maintain an adequate level of allowance for loan losses. Management s periodic evaluation of the adequacy of the allowance considers past loan loss experience, known and inherent risks in the loan portfolio, adverse situations which may affect the borrowers ability to repay, the estimated value of the underlying collateral, if any, and current and prospective economic conditions. Substantial portions of the Bank s loans are secured by real estate in Massachusetts. Accordingly, the ultimate collectibility of a substantial portion of the Bank s loan portfolio is susceptible to changes in property values within the state.

The provision for loan losses increased in 2005 to $4.2 million, compared with $3.0 million in 2004. Provision for loan losses increased by $1.2 million as compared to last year maintaining a 1.31% reserve to loan ratio. For the year ended December 31, 2005, net loan charge-offs totaled $2.7 million, an increase of $879,000 from the prior year. The allowance for loan losses at December 31, 2005 was 797.81% of nonperforming loans, as compared to 932.53% at the prior year-end.

The provision for loan losses is based upon management s evaluation of the level of the allowance for loan losses in relation to the estimate of loss exposure in the loan portfolio. An analysis of individual loans and the overall risk characteristics and size of the different loan portfolios is conducted on an ongoing basis. This managerial evaluation is reviewed periodically by a third-party loan review consultant. As adjustments are identified, they are reported in the earnings of the period in which they become known.

Non-Interest Income The following table sets forth information regarding non-interest income for the periods shown.

Table 16 Non-Interest Income

Years Ended December 31,	2005	2004	2003
		(In thousands)	
Service charges on deposit accounts	$ 13,103	$ 12,345	$ 11,409
Investment management services	5,287	4,683	4,340
Mortgage banking income	3,155	2,763	4,451
Bank owned life insurance	1,831	1,902	1,862
Net gain on sales of securities	616	1,458	2,629
Gain on branch sale		1,756	
Other non-interest income	3,158	3,448	3,103
Total	$ 27,150	$ 28,355	$ 27,794

Non-interest income, which is generated by deposit account service charges, investment management services, mortgage banking activities, and miscellaneous other sources, amounted to $27.2 million in 2005, a $1.2 million, or 4.2%, decrease from the prior year. The majority of the decrease is attributable to the sale of a bank branch in North Eastham, MA during the fourth quarter of 2004 that resulted in a pre-tax gain of approximately $1.8 million as well as a decrease in net securities sales gains of $842,000. Service charges on deposit accounts, which represented 48.3% of total non-interest income in 2005, increased from $12.3 million in 2004 to $13.1 million in 2005, reflecting strong organic growth in core deposits, a full year of earnings related to the acquired deposits in 2005 and increased service charges on overdrafts and return check charges implemented in August 2005. Investment management services revenue increased by 12.9% to $5.3 million compared to $4.7 million in 2004, due to growth in managed assets. Assets under administration at December 31, 2005 were $680.1 million an increase of $116.1 million, or 20.6% as compared to December 31, 2004.

Mortgage banking income of $3.2 million in 2005, increased by 14.2% from the $2.8 million recorded in 2004. The increase is a result of selling a higher percentage of loan production and changes in market rates favorably impacting servicing asset amortization. The Bank s mortgage banking revenue consists primarily of servicing released premiums, net servicing income, and gains and losses on the sale of loans which includes application fees and origination fees on sold loans.

Gains and losses on sales of mortgage loans are recorded as mortgage banking income. The gains and losses resulting from the sales of loans with servicing retained are adjusted to recognize the present value of future servicing fee income over the estimated lives of the related loans. Residential real estate loans and the related servicing rights are sold on a flow basis.

Mortgage servicing rights are amortized on a method that approximates the estimated weighted average life of the underlying loans serviced for others. Amortization is recorded as a charge against mortgage service fee income, a component of mortgage banking income. Rockland s assumptions with respect to prepayments, which affect the estimated average life of the loans, are adjusted periodically to consider market consensus loan prepayment predictions at that date.

Mortgage servicing fees received from investors for servicing their loan portfolios are recorded as mortgage servicing fee income when received. Loan servicing costs are charged to non-interest expense when incurred.

At December 31, 2005 the mortgage servicing rights asset was $2.9 million, or 0.86% of the serviced loan portfolio. At December 31, 2004 the mortgage servicing rights asset was $3.3 million, or 0.84% of the serviced loan portfolio.

Net security gains were $616,000 for the twelve months ended December 31, 2005 as compared to $1.5 million for the same period in 2004, a decrease of $842,000, or 57.8%.

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Other non-interest income decreased by $290,000, or 8.4% for the twelve months ended December 31, 2005, mainly due to a decrease in commercial loan prepayment fees.

Non-Interest Expense The following table sets forth information regarding non-interest expense for the periods shown.

Table 17 Non-Interest Expense

Years Ended December 31,	2005		2004		2003	
			(Dollars in thousands)			
Salaries and employee benefits		$ 47,912		$ 44,899		$ 41,508
Occupancy and equipment expenses		10,070		8,894		8,692
Data processing and facilities management		4,091		4,474		4,517
Merger and acquisition				684		
Other						
Advertising	1,959		2,447		1,985	
Telephone	1,385		1,777		1,720	
Postage	1,006		942		1,034	
Debit card and ATM processing	940		624		546	
Software maintenance	873		308		628	
Consulting	794		1,701		1,637	
Examinations and audits	785		626		496	
Legal fees	641		478		534	
Business development	157		482		205	
Prepayment penalty on borrowings					1,941	
Other non-interest expense	9,879	18,419	9,355	18,740	8,384	19,110
Total		$ 80,492		$ 77,691		$ 73,827

Non-interest expense increased by $2.8 million, or 3.6%, during the year ended December 31, 2005 as compared to the same period last year. Salaries and employee benefits increased by $3.0 million, or 6.7%, for the year ended December 31, 2005, as compared to the prior year reflecting annual merit increases for employees, select additions to staff to support strategic initiatives, severance expense due to position eliminations of $333,000 recognized during the quarter ended December 31, 2005, an annual increase in performance based incentive compensation of $399,000 as well as increases in pension costs of $634,000 and medical insurance of $303,000.

Occupancy and equipment expenses increased $1.2 million, or 13.2%, for the twelve months ended December 31, 2005. The increase in this expense is primarily driven by facilities rent associated with the Falmouth Bancorp, Inc. acquisition which closed in mid 2004, closed branch lease buyout expense and the accelerated write-off of assets associated with these branch closings, two *de novo* branches, and increased depreciation expense related to a new phone system installed in 2004. Snow removal cost also increased by $165,000 on a year over year basis due to the inclement weather experienced in the early part of 2005.

Data processing and facilities management expense has decreased $383,000, or 8.6%, for the twelve months ended December 31, 2005, compared to the same period in 2004, as a result of a new data processing contract finalized in the

latter part of 2004.

Merger and acquisition expense of $684,000 related to the purchase of Falmouth Bancorp, Inc. was recognized in the twelve months ended December 31, 2004. No merger and acquisition expense was recognized in 2005.

Other non-interest expenses decreased by $321,000, or 1.7%, for the twelve months ended December 31, 2005, as compared to the same period in the prior year. The decrease in the twelve month period is due to lower consultant fees of $907,000, advertising expense of $488,000, telephone expense of $392,000, and business development fees

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of $325,000. These charges were offset by increases in software maintenance fees of $565,000, ATM and debit card services of $316,000 related primarily to system conversion charges, and internet banking expense of $215,000.

Minority Interest Effective March 31, 2004, the Company no longer reports the interest payable, net of the amortization of the issuance costs, on the Corporation-Obligated Mandatorily Redeemable Trust Preferred Securities of Subsidiary Trust Holding Solely Junior Subordinated Debentures of the Corporation as Minority Interest. Rather, the interest expense on the Junior Subordinated Debentures, offset by the amortization of the issuance costs, effective March 31, 2004, is captured in borrowings expense. See *Junior Subordinated Debentures* in Item 7 hereof.

Minority Interest expense was zero, $1.1 million, and $4.4 million in 2005, 2004, and 2003, respectively. Interest expense on the junior subordinated debentures, reported in the borrowings expense, was $4.5 million in 2005 and $3.3 million in 2004 and zero in 2003.

Income Taxes For the years ended December 31, 2005, 2004 and 2003 the Company recorded combined federal and state income tax provisions of $15.1 million, $13.6 million and $15.5 million, respectively. These provisions reflect effective income tax rates of 31.3%, 30.7% and 37.0%, in 2005, 2004, and 2003, respectively, which are less than the Bank s blended federal and state statutory tax rate of 41.8%. The lower effective income tax rates are attributable to certain non-taxable interest and dividends, certain tax efficiency strategies employed by the Company, and tax credits. The effective rate increased 60 basis points for 2005 as compared to 2004 mainly due to a decrease in securities held at the Company s security corporations year over year. Overall period to period comparisons are skewed due to the Company s recognition in 2003 of a $2.0 million charge, net of income tax benefits and applicable interest, directly to the provision for income taxes due to a settlement with the Massachusetts Department of Revenue (DOR) in connection to the retroactive change to Massachusetts tax law on the deductibility of Real Estate Investment Trust s (REIT) dividend distributions to its parent Company and due to the recognition of $750,000 and $1.5 million of New Markets Tax Credits in 2004 and 2005, respectively. The Company s effective rate for fiscal year 2003 excluding the $2.0 million settlement charge was 32.2%.

During the second quarter of 2004, the Company announced that one of its subsidiaries (a Community Development Entity, or CDE) had been awarded $30 million in tax credit allocation authority under the New Markets Tax Credit Program of the United States Department of Treasury. In both 2004 and 2005, the Bank invested $15.0 million in the CDE providing it with the capital necessary to begin assisting qualified businesses in low-income communities throughout its market area. Based upon the Bank s total $30.0 million investment, it will be eligible to receive tax credits over a eight year period totaling 39% of its investment, or $11.7 million. The Company has begun recognizing the benefit of these tax credits by reducing the provision of income taxes by $750,000 and $1.5 million during 2004 and 2005, respectively. The following table details the tax credit recognition by year based upon the $15 million invested in 2004 and 2005.

Table 18 New Markets Tax Credit Recognition Schedule

Investment		2004	2005	2006	2007	2008	2009	2010	2011	Total
					(Dollars in thousands)					
2004	**$ 15M**	$ 750	$ 750	$ 750	$ 900	$ 900	$ 900	$ 900	$	$ 5,850
2005	**$ 15M**		$ 750	$ 750	$ 750	$ 900	$ 900	$ 900	$ 900	$ 5,850
Total	**$ 30M**	$ 750	$ 1,500	$ 1,500	$ 1,650	$ 1,800	$ 1,800	$ 1,800	$ 900	$ 11,700

The tax effects of all income and expense transactions are recognized by the Company in each year s consolidated statements of income regardless of the year in which the transactions are reported for income tax purposes.

Comparison of 2004 vs. 2003 The Company s assets increased to $2.9 billion in 2004, an increase of $507.2 million, or 20.8%, from the $2.4 billion reported in 2003. Securities increased by $145.8 million, or 21.7%, to $818.2 million at December 31, 2004 from $672.5 million a year earlier. Loans increased by $335.2 million, or 21.2%, during the twelve months ended December 31, 2004. At December 31, 2004, deposits of $2.1 billion were $276.9 million, or 15.5%, higher than the prior year-end. Core deposits increased $279.2 million, or 21.0%, and time deposits decreased $2.3 million, or 0.5%. Borrowings were $655.2 million at December 31, 2004, an increase

of $239.8 million from December 31, 2003. During 2004, the Company completed the acquisition of Falmouth Bancorp, Inc., parent of Falmouth Co-Operative Bank (Falmouth) resulting in total assets acquired of $158.4 million, total liabilities assumed of $141.6 million, or $16.8 million of net assets. The acquisition contributed to many of the balance variances discussed below. For more insight into the acquisition see the 2004 Form 10-K.

Net income for 2004 was $30.8 million, or $2.03 per diluted share compared to $26.4 million, or $1.79 per diluted share, for 2003. Return on average assets and return on average equity were 1.13% and 16.27%, respectively, for 2004 and 1.11% and 15.89%, respectively, for 2003.

Net interest income on a fully tax-equivalent basis increased by $2.0 million in 2004 compared to 2003. Interest income on a fully tax-equivalent basis increased by $6.3 million, or 4.8%, to $136.4 million in 2004 as compared to the prior year-end mainly due to the growth in the average loan balance of $230.8 million to $1.7 billion at December 31, 2004. Based upon loan volume growth alone (not considering the impact of rate change and mix), interest income increased $14.6 million in 2004. Interest income from taxable securities increased by $1.8 million, or 6.1%, to $31.5 million in 2004 as compared to the prior year mainly attributable to higher balances on average in 2004. The overall yield on interest earning assets decreased by 7.8% to 5.41% in 2004 from the 5.87% reported the prior year during 2004 due to the higher yielding assets being replaced in a lower rate environment.

Interest expense for the year ended December 31, 2004 increased to $36.8 million from the $32.5 million recorded in 2003, an increase of $4.3 million, or 13.1%, due to an increase in the average balance on deposits and borrowings. The increase is partially offset by an overall decrease in the cost of funds from 1.89% in 2003 to 1.82% in 2004. Contributing to this decrease was a $49.7 million, or 8.6%, increase in non-interest bearing demand deposit balances favorably impacting the Bank s cost of funds. Average interest-bearing deposits increased $198.6 million, or 15.2%, over prior year, however, the cost of these deposits decreased from 1.36% to 1.26% attributable to both a lower rate environment and increases in lower yielding deposit categories.

Average borrowings increased by $100.3 million, or 24.4% from the 2003 average balance of which $38.9 million of the increase is due to the inclusion of junior subordinated debentures (see *Junior Subordinated Debentures of the Corporation* in Item 7 hereof) and the majority of the remaining increase is in Federal Home Loan Bank borrowings. The average cost of borrowings decreased to 3.50% from 3.59% despite the inclusion of the aforementioned junior subordinated debentures yielding 8.65%.

The provision for loan losses was $3.0 million in 2004 compared to $3.4 million in 2003. The allowance for loan losses at December 31, 2004 was 932.53% of nonperforming loans compared to 659.16% at December 31, 2003. Nonperforming loans represented 0.14% of gross loans at December 31, 2004 compared to 0.22% at December 31, 2003. Nonperforming assets were down $812,000 from December 31, 2003 to $2.7 million or 0.09% of total assets at December 31, 2004.

Non-interest income, which is generated by deposit account service charges, investment management services, mortgage banking activities, and miscellaneous other sources, amounted to $28.4 million in 2004, a $561,000, or 2.0%, increase over the prior year. The majority of the increase is attributable to the sale of a bank branch in North Eastham, MA during the fourth quarter of 2004 that resulted in a pre-tax gain of approximately $1.8 million. Service charges on deposit accounts, which represented 43.5% of total non-interest income in 2004, increased from $11.4 million in 2003 to $12.3 million in 2004, reflecting strong organic growth in core deposits. Investment management services revenue increased by 7.9% to $4.7 million compared to $4.3 million in 2003, due to growth in managed assets.

Mortgage banking income of $2.8 million in 2004, decreased by 37.9% from the $4.5 million recorded in 2003. The decrease experienced is a result of the decline in refinancing activity that was at its peak in 2003.

Net security gains were $1.5 million for the twelve months ended December 31, 2004 as compared to $2.6 million for the same period in 2003, a decrease of $1.2 million, or 44.5%. Net security gains of $2.0 million were recorded in the second quarter of 2003 on the sale of $20.0 million of investment securities as part of a strategy to improve the Company s overall interest rate risk position and increase the net interest margin. That strategy included prepaying $31.5 million of fixed high-rate borrowings resulting in the recognition of a $1.9 million prepayment penalty.

Other non-interest income increased by $345,000 for the twelve months ended December 31, 2004, compared to the same period in 2003 mainly due to increased commercial loan prepayment fees.

Non-interest expense increased by $3.9 million, or 5.2%, during the year ended December 31, 2004 as compared to the same period last year. Non-interest expense, excluding the merger and acquisition expense taken in the third quarter of 2004 and the prepayment penalty on borrowings taken in the second quarter of 2003, increased by $5.1 million, or 7.1%, for the year ended December 31, 2004, as compared to the prior year. Salaries and employee benefits increased by $3.4 million, or 8.2%, for the year ended December 31, 2004, as compared to the prior year reflecting additions to staff to support continued growth as well as increased pension expense.

Occupancy and equipment expenses increased $202,000, or 2.3%, for the twelve months ended December 31, 2004 due to infrastructure improvements made throughout the year.

A $1.9 million prepayment penalty was incurred during the quarter ended June 30, 2003 as part of the balance sheet repositioning strategy discussed above and is recorded in non-interest expense for the twelve months ended December 31, 2003.

During the twelve months ended December 31, 2004, the Company incurred expenses of approximately $684,000, related to the Falmouth acquisition.

Other non-interest expenses, not broken out in Table 17, *Non-Interest Expense*, increased $1.3 million, or 17.1%, for the twelve months ended December 31, 2004 compared to the same period in 2003. The increase in other non-interest expenses for the year is primarily attributable to increased expenditures for the Company s key business initiatives. During 2004, the Company incurred business initiative expenses to implement a small business banking model, to expand residential lending, to develop a new set of consumer deposit products, to improve the commercial loan process, to fund retail sales training, and to fund a core information system selection process. The Company estimates that the total cost associated with its business initiatives was approximately $2.1 million for the twelve months ended December 31, 2004, across all expense categories. In addition, advertising and business development increased by $739,000 for the twelve months ended December 31, 2004, as compared to the same period in the prior year, to support the aforementioned business initiatives and capitalize on market changes due to merger disruption.

Risk Management The Company s Board of Directors and executive management have identified seven significant Risk Categories consisting of credit, interest rate, liquidity, operations, compliance, reputation and strategic risk. The Board of Directors has approved a Risk Management Policy that addresses each category of risk. The chief executive officer, chief financial officer, chief technology and operations officer, the senior lending officer and other members of management provide regular reports to the Board of Directors that review the level of risk to limits established by the Risk Management Policy and other Policies approved by the Board of Directors that address risk and any key risk issues and plans to address these issues.

Asset/Liability Management The Bank s asset/liability management process monitors and manages, among other things, the interest rate sensitivity of the balance sheet, the composition of the securities portfolio, funding needs and sources, and the liquidity position. All of these factors, as well as projected asset growth, current and potential pricing actions, competitive influences, national monetary and fiscal policy, and the regional economic environment are considered in the asset/liability management process.

The Asset/Liability Management Committee (ALCO), whose members are comprised of the Bank s senior management, develops procedures consistent with policies established by the Board of Directors, which monitor and coordinate the Bank s interest rate sensitivity and the sources, uses, and pricing of funds. Interest rate sensitivity refers to the Bank s exposure to fluctuations in interest rates and its effect on earnings. If assets and liabilities do not re-price

simultaneously and in equal volume, the potential for interest rate exposure exists. It is management s objective to maintain stability in the growth of net interest income through the maintenance of an appropriate mix of interest-earning assets and interest-bearing liabilities and, when necessary, within prudent limits, through the use of off-balance sheet hedging instruments such as interest rate swaps, floors and caps. The Committee employs simulation analyses in an attempt to quantify, evaluate, and manage the impact of changes in interest rates on the Bank s net interest income. In addition, the Bank engages an independent consultant to render advice with respect to asset and liability management strategy.

The Bank is careful to increase deposits without adversely impacting the weighted average cost of those funds. Accordingly, management has implemented funding strategies that include FHLB advances and repurchase agreement lines. These non-deposit funds are also viewed as a contingent source of liquidity and, when profitable lending and investment opportunities exist, access to such funds provides a means to leverage the balance sheet.

From time to time, the Bank has utilized interest rate swap agreements and interest rates caps and floors as hedging instruments against interest rate risk. An interest rate swap is an agreement whereby one party agrees to pay a floating rate of interest on a notional principal amount in exchange for receiving a fixed rate of interest on the same notional amount for a predetermined period of time from a second party. Interest rate caps and floors are agreements whereby one party agrees to pay a floating rate of interest on a notional principal amount for a predetermined period of time to a second party if certain market interest rate thresholds are realized. The assets relating to the notional principal amount are not actually exchanged.

At December 31, 2005 the Company had interest rate swaps, designated as cash flow hedges, with total notional values of $110.0 million. The purpose of these swaps is to hedge the variability in the cash outflows of LIBOR based borrowings attributable to changes in interest rates. Under these swap agreements the Company pays a fixed rate of interest of 3.65% on $50.0 million notional value through November 21, 2006, 2.49% on $25.0 million notional value through January 21, 2007, and 4.06% on $35.0 million through January 10, 2010, and all receive 3 month LIBOR rate of interest. These swaps had a positive fair value of $2.0 million at December 31, 2005. The Company also has a $100 million, 4.0% 3-month LIBOR interest rate cap with an effective date of January 31, 2005 and a maturity date of January 31, 2008. The interest rate cap pays the Company when 3-month LIBOR exceeds 4.0% on a rate reset date during the effective period of the cap. At December 31, 2005 the interest rate cap had a fair value of $1.7 million.

Subsequently, during January 2006, the Company sold the interest rate swap that was hedging $25.0 million of 3 month LIBOR revolving FHLB borrowings with a maturity date of November 21, 2006 in connection with the Company s decision not to re-enter into these borrowings. A gain of approximately $237,000 will be recognized during the three months ending March 31, 2006 against the interest expense on FHLB borrowings.

During the third quarter ending September 30, 2005, the Company sold an interest rate swap that was hedging $25.0 million of 3-month LIBOR revolving FHLB borrowings in connection with the Company s decision not to re-enter into these borrowings. The gain of $215,000 on the sale of this swap was recognized in earnings against the interest expense on FHLB borrowings.

At December 31, 2004 the Company had interest rate swaps with a value of $75.0 million. Under these swap agreements the Company pays a fixed rate of interest of 3.65% on $50 million of the notional value through November 2006, and 2.49% on the remaining $25 million notional value through January 2007, and both receive a 3 month LIBOR rate of interest. These swaps had a positive fair value of $142,000 at December 31, 2004. All changes in the fair value of the interest rate swaps are recorded, net of tax, through equity as other comprehensive income.

To improve the Company s asset sensitivity, the Company sold interest rate swaps hedged against loans during the year ending December 31, 2002 resulting in total deferred gains of $7.1 million. The deferred gain is classified in other comprehensive income, net of tax, as a component of equity. The interest rate swaps sold had total notional amounts of $225.0 million. These swaps were accounted for as cash flow hedges, and therefore, the deferred gains will be amortized into interest income over the remaining life of the hedged item, which will run-off in April of 2007. At December 31, 2005, there are $980,000 gross, or $568,000 million, net of tax, of such deferred gains included in other comprehensive income.

Additionally, the Company enters into commitments to fund residential mortgage loans with the intention of selling them in the secondary markets. The Company also enters into forward sales agreements for certain funded loans and

loan commitments to protect against changes in interest rates. The Company records unfunded commitments and forward sales agreements at fair value with changes in fair value as a component of Mortgage Banking Income. At December 31, 2005 the Company had residential mortgage loan commitments with a fair value of $108,000 and forward sales agreements with a fair value of ($22,000). At December 31, 2004 the Company had residential mortgage loan commitments with a fair value of $148,000 and forward sales agreements with a fair value

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of ($47,000). Changes in these fair values of ($15,000) and $10,000 for the years ending December 31, 2005 and 2004, respectively, are recorded as a component of mortgage banking income.

Market Risk Market risk is the sensitivity of income to changes in interest rates, foreign exchange rates, commodity prices and other market-driven rates or prices. The Company has no trading operations and thus is only exposed to non-trading market risk.

Interest-rate risk is the most significant non-credit risk to which the Company is exposed. Interest-rate risk is the sensitivity of income to changes in interest rates. Changes in interest rates, as well as fluctuations in the level and duration of assets and liabilities, affect net interest income, the Company s primary source of revenue. Interest-rate risk arises directly from the Company s core banking activities. In addition to directly impacting net interest income, changes in the level of interest rates can also affect the amount of loans originated, the timing of cash flows on loans and securities and the fair value of securities and derivatives as well as other affects.

The primary goal of interest-rate risk management is to control this risk within limits approved by the Board. These limits reflect the Company s tolerance for interest-rate risk over both short-term and long-term horizons. The Company attempts to control interest-rate risk by identifying, quantifying and, where appropriate, hedging its exposure. The Company manages its interest-rate exposure using a combination of on and off-balance sheet instruments, primarily fixed rate portfolio securities, and interest rate swaps.

The Company quantifies its interest-rate exposures using net interest income simulation models, as well as simpler gap analysis, and Economic Value of Equity (EVE) analysis. Key assumptions in these simulation analyses relate to behavior of interest rates and behavior of the Company s deposit and loan customers. The most material assumptions relate to the prepayment of mortgage assets (including mortgage loans and mortgage-backed securities) and the life and sensitivity of nonmaturity deposits (e.g. DDA, NOW, savings and money market). The risk of prepayment tends to increase when interest rates fall. Since future prepayment behavior of loan customers is uncertain, the resultant interest rate sensitivity of loan assets cannot be determined exactly.

To mitigate these uncertainties, the Company gives careful attention to its assumptions. In the case of prepayment of mortgage assets, assumptions are derived from published dealer median prepayment estimates for comparable mortgage loans.

The Company manages the interest-rate risk inherent in its mortgage banking operations by entering into forward sales contracts. An increase in market interest rates between the time the Company commits to terms on a loan and the time the Company ultimately sells the loan in the secondary market will have the effect of reducing the gain (or increasing the loss) the Company records on the sale. The Company attempts to mitigate this risk by entering into forward sales commitments in amounts sufficient to cover all closed loans and a majority of rate-locked loan commitments.

The Company s policy on interest-rate risk simulation specifies that if interest rates were to shift gradually up or down 200 basis points, estimated net interest income for the subsequent 12 months should decline by less than 6.0%. Given the unusually low rate environments at December 31, 2004, the Company assumed a 100 basis point decline in interest rates in addition to the normal 200 basis point increase in rates. The Company was well within policy limits at December 31, 2005 and 2004.

The Company s earnings are not directly and materially impacted by movements in foreign currency rates or commodity prices. Movements in equity prices may have an indirect but modest impact on earnings by affecting the volume of activity or the amount of fees from investment-related business lines.

The following table sets forth the estimated effects on the Company s net interest income over a 12-month period following the indicated dates in the event of the indicated increases or decreases in market interest rates:

Table 19 Interest Rate Sensitivity

	200 Basis Point Rate Increase	200 Basis Point Rate Decrease	100 Basis Point Rate Decrease
December 31, 2005	(1.56%)	(0.87%)	N/A
December 31, 2004	(3.25%)	N/A	1.06%

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The results implied in the above table indicate estimated changes in simulated net interest income for the subsequent 12 months assuming a gradual shift up or down in market rates of 100 and 200 basis points across the entire yield curve. It should be emphasized, however, that the results are dependent on material assumptions such as those discussed above. For instance, asymmetrical rate behavior can have a material impact on the simulation results. If competition for deposits forced the Company to raise rates on those liabilities quicker than is assumed in the simulation analysis without a corresponding increase in asset yields net interest income may be negatively impacted. Alternatively, if the Company is able to lag increases in deposit rates as loans re-price upward net interest income would be positively impacted.

The most significant factors affecting market risk exposure of the Company s net interest income during 2005 were (i) changes in the composition and prepayment speeds of mortgage assets and loans (ii) the shape of the U.S. Government securities and interest rate swap yield curve (iii) the level of U.S. prime interest rates and (iv) the level of rates paid on deposit accounts.

The table below provides information about the Company s derivative financial instruments and other financial instruments that are sensitive to changes in interest rates, including interest rate swaps, interest rate caps and debt obligations. For debt obligations, the table presents principal cash flows and related weighted average interest rates by expected maturity dates. For interest rate swaps, the table presents notional amounts and weighted average interest rates by expected maturity dates. Notional amounts are used to calculate the contractual payments to be exchanged under the contract. Weighted average variable rates are based on implied forward rates at the reporting date. For interest rate caps, the table presents notional amounts by expected maturity dates, the strike rate, and the anticipated average interest rate cap will pay based upon the implied forward rates at the reporting date.

Table 20 Expected Maturities of Long Term Debt and Interest Rate Derivatives

	2006	2007	2008	2009	2010	Thereafter	Total	Fair Value
	(Dollars in thousands)							
LIABILITIES								