LAKELAND BANCORP INC
Form 10-K
March 15, 2013
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-K

(Mark One)

FOR THE FISCAL YEAR ENDED DECEMBER 31 2012

x **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE FISCAL YEAR ENDED DECEMBER 31, 2012.**

¨ **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: 000-17820

LAKELAND BANCORP, INC.

(Exact name of registrant as specified in its charter)

New Jersey	**22-2953275**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
250 Oak Ridge Road, Oak Ridge, New Jersey	**07438**
(Address of principal executive offices)	**(Zip code)**

Registrant s telephone number, including area code: (973) 697-2000

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

Title of each class	Name of each exchange on which registered
Common Stock, no par value	**NASDAQ**

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

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

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

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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of 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, a non-accelerated filer or a smaller reporting company. See definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act:

Large accelerated filer ¨	Accelerated filer x
Non-accelerated filer ¨	Smaller Reporting Company ¨

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

As of June 30, 2012, the aggregate market value of the registrant s common stock held by non-affiliates of the registrant was approximately $256,000,000, based on the closing sale price as reported on the NASDAQ Global Select Market.

The number of shares outstanding of the registrant s common stock, as of February 1, 2013, was 29,800,471.

DOCUMENTS INCORPORATED BY REFERENCE:

Lakeland Bancorp, Inc s. Proxy Statement for its 2013 Annual Meeting of Shareholders (Part III).

LAKELAND BANCORP, INC.

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PART I

ITEM 1 Business.

GENERAL

Lakeland Bancorp, Inc. (the Company or Lakeland Bancorp) is a bank holding company headquartered in Oak Ridge, New Jersey. The Company was organized in March of 1989 and commenced operations on May 19, 1989, upon the consummation of the acquisition of all of the outstanding stock of Lakeland Bank, formerly named Lakeland State Bank (Lakeland or the Bank or Lakeland Bank). Through Lakeland, the Company operates 46 banking offices, located in Morris, Passaic, Sussex, Warren, Essex and Bergen counties in New Jersey. Lakeland offers a full range of lending services, including commercial loans and leases, real estate and consumer loans to small and medium-sized businesses, professionals and individuals located in its markets.

The Company has shown substantial growth through a combination of organic growth and acquisitions. Since 1998, Lakeland has opened nineteen new branch offices and the Company has also acquired four community banks with an aggregate asset total of approximately $780 million. All of the acquired banks have been merged into Lakeland and their holding companies, if applicable, have been merged into the Company.

Lakeland Bancorp and Somerset Hills Bancorp, the parent company of Somerset Hills Bank, entered into an Agreement and Plan of Merger, dated as of January 28, 2013 (the Merger Agreement), pursuant to which Somerset Hills Bancorp will be merged with and into Lakeland Bancorp, with Lakeland Bancorp as the surviving bank holding company. Somerset Hills Bank operates six banking offices in New Jersey: its main office, located in Somerset County, four branch offices in Morris County and one branch office in Union County. At December 31, 2012, Somerset Hills Bancorp had consolidated total assets, total loans, total deposits and total stockholders equity of $368.9 million, $241.9 million, $320.2 million and $41.8 million, respectively.

The Merger Agreement provides that the shareholders of Somerset Hills Bancorp will receive, at their election, for each outstanding share of Somerset Hills Bancorp common stock that they own at the effective time of the merger, either 1.1962 shares of Lakeland Bancorp common stock or $12.00 in cash, subject to proration as described in the Merger Agreement, so that 90% of the aggregate merger consideration will be shares of Lakeland Bancorp common stock and 10% will be cash. The Merger Agreement provides that immediately after the merger of Somerset Hills Bancorp into Lakeland Bancorp, Somerset Hills Bank will merger with and into Lakeland Bank, with Lakeland Bank as the surviving bank. The mergers are subject to receipt of various regulatory approvals, the approval by the shareholders of Somerset Hills Bancorp of the Merger Agreement and the merger of Somerset Hills Bancorp into Lakeland Bancorp, and the approval by the shareholders of Lakeland Bancorp of the authorization of the issuance of the shares of Lakeland Bancorp common stock issuable in the merger with Somerset Hills Bancorp. The closing of the mergers is expected to occur in the second or third quarters of 2013.

At December 31, 2012, Lakeland Bancorp had total consolidated assets of $2.9 billion, total consolidated deposits of $2.4 billion, total consolidated loans, net of the allowance for loan and lease losses, of $2.1 billion and total consolidated stockholders equity of $280.9 million.

This Annual Report on Form 10-K contains certain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 (Forward-Looking Statements). Such statements are subject to risks and uncertainties that could cause actual results to differ materially from those projected in such Forward-Looking Statements. Certain factors which could materially affect such results and the future performance of the Company are described in Item 1A Risk Factors of this Annual Report on Form 10-K.

Unless otherwise indicated, all weighted average, actual shares and per share information contained in this Annual Report on Form 10-K have been adjusted retroactively for the effect of stock dividends, including the Company s 5% stock dividend which was distributed on April 16, 2012.

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Commercial Bank Services

Through Lakeland, the Company offers a broad range of lending, depository, and related financial services to individuals and small to medium sized businesses located primarily in northern New Jersey. In the lending area, these services include short and medium term loans, lines of credit, letters of credit, inventory and accounts receivable financing, real estate construction loans, mortgage loans and merchant credit card services. In addition to commercial real estate loans, Lakeland makes commercial and industrial loans, which are not always secured by real estate. These types of loans can diversify the Company s exposure in a depressed real estate market. Lakeland s equipment leasing division provides a solution to small and medium sized companies who prefer to lease equipment over other financial alternatives. Lakeland s asset based loan department provides commercial borrowers with another lending alternative.

Depository products include demand deposits, as well as savings, money market and time accounts. The Company also offers wire transfer, internet banking, mobile banking and night depository services to the business community and municipal relationships. In addition, Lakeland offers cash management services, such as remote capture of deposits and overnight sweep repurchase agreements.

Consumer Banking

Lakeland also offers a broad range of consumer banking services, including checking accounts, savings accounts, NOW accounts, money market accounts, certificates of deposit, internet banking, secured and unsecured loans, consumer installment loans, mortgage loans, and safe deposit services.

Other Services

Investment and advisory services for individuals and businesses are also available.

Competition

Lakeland faces considerable competition in its market areas for deposits and loans from other depository institutions. Many of Lakeland s depository institution competitors have substantially greater resources, broader geographic markets, and higher lending limits than Lakeland and are also able to provide more services and make greater use of media advertising. In recent years, intense market demands, economic pressures, increased customer awareness of products and services, and the availability of electronic services have forced banking institutions to diversify their services and become more cost-effective.

Lakeland also competes with credit unions, brokerage firms, insurance companies, money market mutual funds, consumer finance companies, mortgage companies and other financial companies, some of which are not subject to the same degree of regulation and restrictions as Lakeland in attracting deposits and making loans. Interest rates on deposit accounts, convenience of facilities, products and services, and marketing are all significant factors in the competition for deposits. Competition for loans comes from other commercial banks, savings institutions, insurance companies, consumer finance companies, credit unions, mortgage banking firms and other institutional lenders. Lakeland primarily competes for loan originations through its structuring of loan transactions and the overall quality of service it provides. Competition is affected by the availability of lendable funds, general and local economic conditions, interest rates, and other factors that are not readily predictable.

The Company expects that competition will continue in the future.

Concentration

The Company is not dependent for deposits or exposed by loan concentrations to a single customer or a small group of customers the loss of any one or more of which would have a material adverse effect upon the financial condition of the Company.

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Employees

At December 31, 2012, the Company had 522 full-time equivalent employees. None of these employees is covered by a collective bargaining agreement. The Company considers relations with its employees to be good.

SUPERVISION AND REGULATION

General

The Company is a registered bank holding company under the federal Bank Holding Company Act of 1956, as amended (the Holding Company Act), and is required to file with the Federal Reserve Board an annual report and such additional information as the Federal Reserve Board may require pursuant to the Holding Company Act. The Company is subject to examination by the Federal Reserve Board.

Lakeland is a state chartered banking association subject to supervision and examination by the Department of Banking and Insurance of the State of New Jersey (the Department) and the Federal Deposit Insurance Corporation (the FDIC). The regulations of the State of New Jersey and FDIC govern most aspects of Lakeland s business, including reserves against deposits, loans, investments, mergers and acquisitions, borrowings, dividends, and location of branch offices. Lakeland is subject to certain restrictions imposed by law on, among other things, (i) the maximum amount of obligations of any one person or entity which may be outstanding at any one time, (ii) investments in stock or other securities of the Company or any subsidiary of the Company, and (iii) the taking of such stock or securities as collateral for loans to any borrower.

The Holding Company Act

The Holding Company Act limits the activities which may be engaged in by the Company and its subsidiaries to those of banking, the ownership and acquisition of assets and securities of banking organizations, and the management of banking organizations, and to certain non-banking activities which the Federal Reserve Board finds, by order or regulation, to be so closely related to banking or managing or controlling a bank as to be a proper incident thereto. The Federal Reserve Board is empowered to differentiate between activities by a bank holding company or a subsidiary thereof and activities commenced by acquisition of a going concern.

With respect to non-banking activities, the Federal Reserve Board has by regulation determined that several non-banking activities are closely related to banking within the meaning of the Holding Company Act and thus may be performed by bank holding companies. Although the Company s management periodically reviews other avenues of business opportunities that are included in that regulation, the Company has no present plans to engage in any of these activities other than providing investment brokerage services.

If the proposed mergers with Somerset Hills Bancorp and Somerset Hills Bank are completed, the Company will acquire the mortgage banking subsidiary of Somerset Hills Bank and Somerset Hills Bank s 50% interest in a title insurance agency joint venture.

With respect to the acquisition of banking organizations, the Company is required to obtain the prior approval of the Federal Reserve Board before it may, by merger, purchase or otherwise, directly or indirectly acquire all or substantially all of the assets of any bank or bank holding company, if, after such acquisition, it will own or control more than 5% of the voting shares of such bank or bank holding company.

Regulation of Bank Subsidiaries

There are various legal limitations, including Sections 23A and 23B of the Federal Reserve Act, which govern the extent to which a bank subsidiary may finance or otherwise supply funds to its holding company or its holding company s non-bank subsidiaries. Under federal law, no bank subsidiary may, subject to certain limited

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exceptions, make loans or extensions of credit to, or investments in the securities of, its parent or the non-bank subsidiaries of its parent (other than direct subsidiaries of such bank which are not financial subsidiaries) or take their securities as collateral for loans to any borrower. Each bank subsidiary is also subject to collateral security requirements for any loans or extensions of credit permitted by such exceptions.

Commitments to Affiliated Institutions

The policy of the Federal Reserve Board provides that a bank holding company is expected to act as a source of financial strength to its subsidiary banks and to commit resources to support such subsidiary banks in circumstances in which it might not do so absent such policy.

Interstate Banking

The Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994 permits bank holding companies to acquire banks in states other than their home state, regardless of applicable state law. New Jersey enacted legislation to authorize interstate banking and branching and the entry into New Jersey of foreign country banks. New Jersey did not authorize de novo branching into the state. However, under federal law, federal savings banks, which meet certain conditions, may branch de novo into a state, regardless of state law. The Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act) removes the restrictions on interstate branching contained in the Riegle-Neal Act, and allows national banks and state banks to establish branches in any state if, under the laws of the state in which the branch is to be located, a state bank chartered by that state would be permitted to establish the branch.

Gramm-Leach-Bliley Act of 1999

The Gramm-Leach-Bliley Financial Services Modernization Act of 1999 (the Modernization Act) became effective in early 2000. The Modernization Act:

- allows bank holding companies meeting management, capital, and Community Reinvestment Act standards to engage in a substantially broader range of non-banking activities than previously was permissible, including insurance underwriting and making merchant banking investments in commercial and financial companies; if a bank holding company elects to become a financial holding company, it files a certification, effective in 30 days, and thereafter may engage in certain financial activities without further approvals;
- allows insurers and other financial services companies to acquire banks;
- removes various restrictions that previously applied to bank holding company ownership of securities firms and mutual fund advisory companies; and
- establishes the overall regulatory structure applicable to bank holding companies that also engage in insurance and securities operations.

The Modernization Act also modified other financial laws, including laws related to financial privacy and community reinvestment.

The USA PATRIOT Act

In response to the events of September 11, 2001, the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (the USA PATRIOT Act), was signed into law on October 26, 2001. The USA PATRIOT Act gives the federal government new powers to address terrorist threats through enhanced domestic security measures, expanded surveillance powers, increased information sharing, and broadened anti-money laundering requirements. By way of amendments to the Bank Secrecy Act, Title III of the USA PATRIOT Act encourages information sharing among bank regulatory

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agencies and law enforcement bodies. Further, certain provisions of Title III impose affirmative obligations on a broad range of financial institutions, including banks, thrifts, brokers, dealers, credit unions, money transfer agents and parties registered under the Commodity Exchange Act.

Among other requirements, Title III of the USA PATRIOT Act imposes the following requirements with respect to financial institutions:

All financial institutions must establish anti-money laundering programs that include, at a minimum: (i) internal policies, procedures, and controls; (ii) specific designation of an anti-money laundering compliance officer; (iii) ongoing employee training programs; and (iv) an independent audit function to test the anti-money laundering program.

The Secretary of the Department of the Treasury, in conjunction with other bank regulators, was authorized to issue regulations that provide for minimum standards with respect to customer identification at the time new accounts are opened.

Financial institutions that establish, maintain, administer, or manage private banking accounts or correspondent accounts in the United States for non-United States persons or their representatives (including foreign individuals visiting the United States) are required to establish appropriate, specific and, where necessary, enhanced due diligence policies, procedures, and controls designed to detect and report money laundering.

Financial institutions are prohibited from establishing, maintaining, administering or managing correspondent accounts for foreign shell banks (foreign banks that do not have a physical presence in any country), and will be subject to certain record keeping obligations with respect to correspondent accounts of foreign banks.

Bank regulators are directed to consider a holding company s effectiveness in combating money laundering when ruling on Federal Reserve Act and Bank Merger Act applications.

The United States Treasury Department has issued a number of implementing regulations which address various requirements of the USA PATRIOT Act and are applicable to financial institutions such as Lakeland. These regulations impose obligations on financial institutions to maintain appropriate policies, procedures and controls to detect, prevent and report money laundering and terrorist financing and to verify the identity of their customers.

Sarbanes-Oxley Act of 2002

On July 30, 2002, the Sarbanes-Oxley Act of 2002 (the SOA) was signed into law. 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 generally applies to all companies, both U.S. and non-U.S., that file or are required to file periodic reports with the Securities and Exchange Commission (the SEC) under the Securities Exchange Act of 1934 (the Exchange Act).

The SOA includes very specific additional disclosure requirements and new corporate governance rules, requires the 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 represents significant federal involvement in matters traditionally left to state regulatory systems, such as the regulation of the accounting profession, and to state corporate law, such as the relationship between a board of directors and management and between a board of directors and its committees.

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The SOA addresses, among other matters:

- audit committees for all reporting companies;
- 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;
- a prohibition on insider trading during pension plan black out periods;
- disclosure of off-balance sheet transactions;
- a prohibition on personal loans to directors and officers (other than loans made by an insured depository institution (as defined in the Federal Deposit Insurance Act), if the loan is subject to the insider lending restrictions of section 22(h) of the Federal Reserve Act);
- expedited filing requirements for Form 4 s;
- 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 a public accounting oversight board;
- auditor independence; and
- various increased criminal penalties for violations of the securities laws.

The SEC has enacted various rules to implement various provisions of the SOA with respect to, among other matters, disclosure in periodic filings pursuant to the Exchange Act.

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 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 Lakeland. 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 certain types of 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.

Community Reinvestment Act

Under the Community Reinvestment Act (CRA), as implemented by FDIC regulations, a state bank has a continuing and affirmative obligation consistent with its safe and sound operation to help meet the credit needs of its entire community, including low and moderate income neighborhoods. The CRA does not establish specific lending requirements or programs for financial institutions nor does it limit an institution s discretion to develop the types of products and services that it believes are best suited to its particular community. The CRA requires the FDIC, in connection with its examination of a state non-member bank, to assess the bank s record of meeting the credit needs of its community and to take that record into account in its evaluation of certain applications by the bank. Under the FDIC s CRA evaluation system, the FDIC focuses on three tests: (i) a lending test, to evaluate the institution s record of making loans in its service areas; (ii) an investment test, to evaluate the institution s record of investing in community development projects, affordable housing and programs benefiting low or moderate income individuals and businesses; and (iii) a service test, to evaluate the institution s delivery of services through its branches, ATMs and other offices.

Securities and Exchange Commission

The common stock of the Company is registered with the SEC under the Exchange Act. As a result, the Company and its officers, directors, and major stockholders are obligated to file certain reports with the SEC. The Company is subject to proxy and tender offer rules promulgated pursuant to the Exchange Act. You may read and copy any document the Company files with the SEC at the SEC s Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information about the Public Reference Room. The SEC maintains a website at http://www.sec.gov that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC, such as the Company.

The Company maintains a website at http://www.lakelandbank.com. The Company makes available on its website the proxy statements and reports on Forms 8-K, 10-K and 10-Q that it files with the SEC as soon as reasonably practicable after such material is electronically filed with or furnished to the SEC. Additionally, the Company has adopted and posted on its website a Code of Ethics that applies to its principal executive officer, principal financial officer and principal accounting officer. The Company intends to disclose any amendments to or waivers of the Code of Ethics on its website.

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Effect of Government Monetary Policies

The earnings of the Company are and will be affected by domestic economic conditions and the monetary and fiscal policies of the United States government and its agencies. The monetary policies of the Federal Reserve Board have had, and will likely continue to have, an important impact on the operating results of commercial banks through the Board s power to implement national monetary policy in order to, among other things, curb inflation or combat a recession. The Federal Reserve Board has a major effect upon the levels of bank loans, investments and deposits through its open market operations in United States government securities and through its regulation of, among other things, the discount rate of borrowings of banks and the reserve requirements against bank deposits. It is not possible to predict the nature and impact of future changes in monetary fiscal policies.

Dividend Restrictions

The Company is a legal entity separate and distinct from Lakeland. Virtually all of the revenue of the Company available for payment of dividends on its capital stock will result from amounts paid to the Company by Lakeland. All such dividends are subject to various limitations imposed by federal and state laws and by regulations and policies adopted by federal and state regulatory agencies. Under state law, a bank may not pay dividends unless, following the dividend payment, the capital stock of the bank would be unimpaired and either (a) the bank will have a surplus of not less than 50% of its capital stock, or, if not, (b) the payment of the dividend will not reduce the surplus of the bank.

If, in the opinion of the FDIC, a bank under its jurisdiction is engaged in or is about to engage in an unsafe or unsound practice (which could include the payment of dividends), the FDIC may require, after notice and hearing, that such bank cease and desist from such practice or, as a result of an unrelated practice, require the bank to limit dividends in the future. The Federal Reserve Board has similar authority with respect to bank holding companies. In addition, the Federal Reserve Board and the FDIC have issued policy statements which provide that insured banks and bank holding companies should generally only pay dividends out of current operating earnings. Regulatory pressures to reclassify and charge off loans and to establish additional loan loss reserves can have the effect of reducing current operating earnings and thus impacting an institution s ability to pay dividends. Further, as described herein, the regulatory authorities have established guidelines with respect to the maintenance of appropriate levels of capital by a bank or bank holding company under their jurisdiction. Compliance with the standards set forth in these policy statements and guidelines could limit the amount of dividends which the Company and Lakeland may pay. Under the Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA), banking institutions which are deemed to be undercapitalized will, in most instances, be prohibited from paying dividends. See FDICIA.

Capital Adequacy Guidelines

The Federal Reserve Board has adopted risk-based capital guidelines. These guidelines establish minimum levels of capital and require capital adequacy to be measured in part upon the degree of risk associated with certain assets. Under these guidelines all banks and bank holding companies must have a core or Tier 1 capital to risk-weighted assets ratio of at least 4% and a total capital to risk-weighted assets ratio of at least 8%. At December 31, 2012, the Company s Tier 1 capital to risk-weighted assets ratio and total capital to risk-weighted assets ratio were 11.52% and 12.77%, respectively.

In addition, the Federal Reserve Board and the FDIC have approved leverage ratio guidelines (Tier 1 capital to average quarterly assets, less goodwill) for bank holding companies such as the Company. These guidelines provide for a minimum leverage ratio of 3% for bank holding companies that meet certain specified criteria, including that they have the highest regulatory rating. All other holding companies are required to maintain a leverage ratio of 3% plus an additional cushion of at least 100 to 200 basis points. The Company s leverage ratio was 8.62% at December 31, 2012.

Under FDICIA, federal banking agencies have established certain additional minimum levels of capital. See FDICIA.

FDICIA

Enacted in December 1991, FDICIA substantially revised the bank regulatory provisions of the Federal Deposit Insurance Act and several other federal banking statutes. Among other things, FDICIA requires federal banking agencies to broaden the scope of regulatory corrective action taken with respect to banks that do not meet minimum capital requirements and to take such actions promptly in order to minimize losses to the FDIC. Under FDICIA, federal banking agencies were required to establish minimum levels of capital (including both a leverage limit and a risk-based capital requirement) and specify for each capital measure the levels at which depository institutions will be considered well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized or critically undercapitalized.

Under regulations adopted under these provisions, for an institution to be well capitalized it must have a total risk-based capital ratio of at least 10%, a Tier 1 risk-based capital ratio of at least 6% and a Tier 1 leverage ratio of at least 5% and not be subject to any specific capital order or directive. For an institution to be adequately capitalized it must have a total risk-based capital ratio of at least 8%, a Tier 1 risk-based capital ratio of at least 4% and a Tier 1 leverage ratio of at least 4% (or in some cases 3%). Under the regulations, an institution will be deemed to be undercapitalized if it has a total risk-based capital ratio that is less than 8%, a Tier 1 risk-based capital ratio that is less than 4%, or a Tier 1 leverage ratio of less than 4% (or in some cases 3%). An institution will be deemed to be significantly undercapitalized if it has a total risk-based capital ratio that is less than 6%, a Tier 1 risk-based capital ratio that is less than 3%, or a leverage ratio that is less than 3% and will be deemed to be critically undercapitalized if it has a ratio of tangible equity to total assets that is equal to or less than 2%. An institution may be deemed to be in a capitalization category that is lower than is indicated by its actual capital position if it receives an unsatisfactory examination rating or is deemed to be in an unsafe or unsound condition or to be engaging in unsafe or unsound practices. As of December 31, 2012, Lakeland met all regulatory requirements for classification as well capitalized under the regulatory framework.

Additional Regulation of Capital

The federal regulatory authorities risk-based capital guidelines are based upon the 1988 capital accord (Basel I) of the Basel Committee on Banking Supervision (the Basel Committee). The Basel Committee is a committee of central banks and bank supervisors/regulators from the major industrialized countries that develops broad policy guidelines for use by each country s supervisors in determining the supervisory policies and regulations to which they apply. Actions of the Committee have no direct effect on banks in participating countries. In 2004, the Basel Committee published a new capital accord (Basel II) to replace Basel I. Basel II provides two approaches for setting capital standards for credit risk an internal ratings-based approach tailored to individual institutions circumstances and a standardized approach that bases risk weightings on external credit assessments to a much greater extent than permitted in existing risk-based capital guidelines. Basel II also would set capital requirements for operational risk and refine the existing capital requirements for market risk exposures. The Company is not required to comply with the advanced approaches of Basel II.

In 2009, the United States Treasury Department issued a policy statement (the Treasury Policy Statement) entitled Principles for Reforming the U.S. and International Regulatory Capital Framework for Banking Firms, which contemplates changes to the existing regulatory capital regime involving substantial revisions to major parts of the Basel I and Basel II capital frameworks and affecting all regulated banking organizations. The Treasury Policy Statement calls for, among other things, higher and stronger capital requirements for all banking firms, with changes to the regulatory capital framework to be phased in over a period of several years.

On December 17, 2009, the Basel Committee issued a set of proposals (the 2009 Capital Proposals) that would significantly revise the definitions of Tier 1 capital and Tier 2 capital. Among other things, the 2009

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Capital Proposals would re-emphasize that common equity is the predominant component of Tier 1 capital. Concurrently with the release of the 2009 Capital Proposals, the Basel Committee also released a set of proposals related to liquidity risk exposure (the 2009 Liquidity Proposals). The 2009 Liquidity Proposals include the implementation of (i) a liquidity coverage ratio or LCR, designed to ensure that a bank maintains an adequate level of unencumbered, high-quality assets sufficient to meet the bank s liquidity needs over a 30-day time horizon under an acute liquidity stress scenario and (ii) a net stable funding ratio or NSFR, designed to promote more medium and long-term funding of the assets and activities of banks over a one-year time horizon.

The Dodd-Frank Act includes certain provisions, often referred to as the Collins Amendment, concerning the capital requirements of the United States banking regulators. These provisions are intended to subject bank holding companies to the same capital requirements as their bank subsidiaries and to eliminate or significantly reduce the use of hybrid capital instruments, especially trust preferred securities, as regulatory capital. Under the Collins Amendment, trust preferred securities issued by a company, such as Lakeland Bancorp, with total consolidated assets of less than $15 billion before May 19, 2010 and treated as regulatory capital are grandfathered, but any such securities issued later are not eligible as regulatory capital. The banking regulators must develop regulations setting minimum risk-based and leverage capital requirements for holding companies and banks on a consolidated basis that are no less stringent than the generally applicable requirements in effect for depository institutions under the prompt corrective action regulations. The banking regulators also must seek to make capital standards countercyclical so that the required levels of capital increase in times of economic expansion and decrease in times of economic contraction. See The Dodd-Frank Act.

In December 2010 and January 2011, the Basel Committee published the final texts of reforms on capital and liquidity generally referred to as Basel III. Although Basel III is intended to be implemented by participating countries for large, internationally active banks, its provisions are likely to be considered by United States banking regulators in developing new regulations applicable to other banks in the United States, including Lakeland. In June 2012, the U.S. banking regulators released notices of proposed rulemaking that would revise regulatory capital rules for U.S. banking organizations. In November 2012, U.S. banking regulators indicated that the implementation of the proposed rules would not become effective on January 1, 2013, as they are continuing to review various views expressed during the comment period. In January 2013, the Basel Committee revised the standard for the Liquidity Coverage Ratio (LCR), including increasing the range of eligible assets that can be held as part of a required liquidity buffer. It is not possible to predict when or in what form final regulations may be adopted.

For banks in the United States, among the most significant provisions of Basel III concerning capital (as proposed prior to the delay in implementation) are the following:

- A minimum ratio of common equity to risk-weighted assets reaching 4.5%, plus an additional 2.5% as a capital conservation buffer, by 2019 after a phase-in period.
- A minimum ratio of Tier 1 capital to risk-weighted assets reaching 6.0% by 2019 after a phase-in period.
- A minimum ratio of total capital to risk-weighted assets, plus the additional 2.5% capital conservation buffer, reaching 10.5% by 2019 after a phase-in period.
- An additional countercyclical capital buffer to be imposed by applicable national banking regulators periodically at their discretion, with advance notice.
- Restrictions on capital distributions and discretionary bonuses applicable when capital ratios fall within the buffer zone.
- Deduction from common equity of deferred tax assets that depend on future profitability to be realized.
- Increased capital requirements for counterparty credit risk relating to OTC derivatives, repos and securities financing activities.

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For capital instruments issued on or after January 13, 2013 (other than common equity), a loss-absorbency requirement such that the instrument must be written off or converted to common equity if a trigger event occurs, either pursuant to applicable law or at the direction of the banking regulator. A trigger event is an event under which the banking entity would become nonviable without the write-off or conversion, or without an injection of capital from the public sector. The issuer must maintain authorization to issue the requisite shares of common equity if conversion were required.

The Basel III provisions on liquidity include complex criteria establishing the LCR and NSFR. Although Basel III is described as a final text, it is subject to the resolution of certain issues and to further guidance and modification, as well as to adoption by United States banking regulators, including decisions as to whether and to what extent it will apply to United States banks that are not large, internationally active banks.

Federal Deposit Insurance and Premiums

Substantially all of the deposits of Lakeland are insured up to applicable limits by the Deposit Insurance Fund (DIF) of the FDIC and are subject to deposit insurance assessments to maintain the DIF. As a result of the Dodd-Frank Act, the basic federal deposit insurance limit was permanently increased from at least $100,000 to at least $250,000. As mandated by Section 343 of the Dodd-Frank Act, the FDIC had adopted rules providing for temporary unlimited deposit insurance for traditional noninterest-bearing transaction accounts and IOLTA accounts beginning December 31, 2010, but these temporary rules expired December 31, 2012. As a result, as of January 1, 2013, (i) noninterest-bearing transaction accounts are no longer insured separately from depositors other accounts at the same FDIC-insured depository institution, and such accounts will instead be added to any of a depositor s other accounts in the applicable ownership category, and the aggregate balance insured up to at least the standard maximum deposit insurance amount of $250,000 per depositor at each separately chartered FDIC-insured depository institution, and (ii) funds deposited in IOLTAs will no longer be insured under Section 343 of the Dodd-Frank Act, but because IOLTAs are fiduciary accounts, they generally qualify for pass-through coverage on a per-client basis.

On November 12, 2009, the FDIC adopted the final rule which required insured depository institutions to prepay their quarterly risk-based assessments for the fourth quarter of 2009 through the fourth quarter of 2012. On December 30, 2009, the Company remitted an FDIC prepayment in the amount of $18.0 million. An institution s prepaid assessment was based on the total base assessment rate that the institution paid for the third quarter of 2009, adjusted quarterly by an estimated annual growth rate of 5% through the end of 2012, plus, for 2011 and 2012, an increase in the total base assessment rate on September 30, 2009 by an annualized three basis points. Any prepaid assessment in excess of the amounts that are subsequently determined to be actually due to the FDIC by June 30, 2013, will be returned to the institution at that time.

In November 2010, the FDIC approved a rule to change the assessment base from adjusted domestic deposits to average consolidated total assets minus average tangible equity, as required by the Dodd-Frank Act. These new assessment rates began in the second quarter of 2011 and were paid at the end of September 2011. Since the new base is larger than the current base, the FDIC s rule lowered the total base assessment rates to between 2.5 and 9 basis points for banks in the lowest risk category, and 30 to 45 basis points for banks in the highest risk category. The Company paid $2.2 million in total FDIC assessments in 2012, compared to $2.8 million in 2011.

Pursuant to the Dodd-Frank Act, the FDIC has established 2.0% as the designated reserve ratio (DRR), that is, the ratio of the DIF to insured deposits. The FDIC has adopted a plan under which it will meet the statutory minimum DRR of 1.35% by September 30, 2020, the deadline imposed by the Dodd-Frank Act. The Dodd-Frank Act requires the FDIC to offset the effect on institutions with assets less than $10 billion of the increase in the statutory minimum DRR to 1.35% from the former statutory minimum of 1.15%. The FDIC has not yet announced how it will implement this offset.

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In addition to deposit insurance assessments, the FDIC is required to continue to collect from institutions payments for the servicing of obligations of the Financing Corporation (FICO) that were issued in connection with the resolution of savings and loan associations, so long as such obligations remain outstanding. Lakeland paid a FICO premium of approximately $170,000 in 2012 and expects to pay a similar premium in 2013.

The Dodd-Frank Act

The Dodd-Frank Act, which was signed into law on July 21, 2010, will continue to have a broad impact on the financial services industry as a result of significant regulatory and compliance changes, including, among other things, (i) enhanced resolution authority over troubled and failing banks and their holding companies; (ii) increased capital and liquidity requirements; (iii) increased regulatory examination fees; (iv) changes to assessments to be paid to the FDIC for federal deposit insurance; and (v) numerous other provisions designed to improve supervision and oversight of, and strengthening safety and soundness for, the financial services sector. Many of the requirements called for in the Dodd-Frank Act will be implemented over time and most will be subject to implementing regulations over the course of several years.

The following is a summary of certain provisions of the Dodd-Frank Act:

Minimum Capital Requirements. The Dodd-Frank Act requires new capital rules and the application of the same leverage and risk-based capital requirements that apply to insured depository institutions to most bank holding companies. In addition to making bank holding companies subject to the same capital requirements as their bank subsidiaries, these provisions (often referred to as the Collins Amendment to the Dodd-Frank Act) were also intended to eliminate or significantly reduce the use of hybrid capital instruments, especially trust preferred securities, as regulatory capital. Under the Collins Amendment, trust preferred securities issued by a bank holding company such as Lakeland Bancorp (with total consolidated assets between $500 million and $15 billion) before May 19, 2010 and treated as regulatory capital are grandfathered, but any such securities issued later are not eligible as regulatory capital. On June 14, 2011, the federal banking agencies published a final rule regarding minimum leverage and risk-based capital requirements for banks and bank holding companies consistent with the requirements of the Dodd-Frank Act. The Dodd-Frank Act also requires banking regulators to seek to make capital standards countercyclical, so that the required levels of capital increase in times of economic expansion and decrease in times of economic contraction.

Deposit Insurance. The Dodd-Frank Act makes permanent the $250,000 deposit insurance limit for insured deposits. Amendments to the Federal Deposit Insurance Act also revise the assessment base against which an insured depository institution s deposit insurance premiums paid to the Deposit Insurance Fund (DIF) will be calculated. Under the amendments, the assessment base will no longer be the institution s deposit base, but rather its average consolidated total assets less its average tangible equity during the assessment period. Additionally, the Dodd-Frank Act makes changes to the minimum designated reserve ratio of the DIF, increasing the minimum from 1.15 percent to 1.35 percent of the estimated amount of total insured deposits and eliminating the requirement that the FDIC pay dividends to depository institutions when the reserve ratio exceeds certain thresholds. In December 2010, the FDIC increased the designated reserve ratio to 2.0 percent.

Shareholder Votes. The Dodd-Frank Act requires publicly traded companies like Lakeland Bancorp to give shareholders a non-binding vote on executive compensation and so-called golden parachute payments in certain circumstances. The Dodd-Frank Act also authorizes the SEC to promulgate rules that would allow shareholders to nominate their own candidates using a company s proxy materials.

Transactions with Affiliates. The Dodd-Frank Act enhances the requirements for certain transactions with affiliates under Section 23A and 23B of the Federal Reserve Act, including an expansion of the definition of covered transactions and increasing the amount of time for which collateral requirements regarding covered transactions must be maintained. These requirements became effective during 2011.

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Transactions with Insiders. Insider transaction limitations are expanded through the strengthening of loan restrictions to insiders and the expansion of the types of transactions subject to the various limits, including derivative transactions, repurchase agreements, reverse repurchase agreements and securities lending or borrowing transactions. Restrictions are also placed on certain asset sales to and from an insider to an institution, including requirements that such sales be on market terms and, in certain circumstances, approved by the institution s board of directors. These requirements became effective during 2011.

Enhanced Lending Limits. The Dodd-Frank Act strengthened the previous limits on a depository institution s credit exposure to one borrower which limited a depository institution s ability to extend credit to one person (or group of related persons) in an amount exceeding certain thresholds. The Dodd-Frank Act expanded the scope of these restrictions to include credit exposure arising from derivative transactions, repurchase agreements, and securities lending and borrowing transactions.

Compensation Practices. The Dodd-Frank Act provides that the appropriate federal regulators must establish standards prohibiting as an unsafe and unsound practice any compensation plan of a bank holding company or other covered financial institution that provides an insider or other employee with excessive compensation or compensation that gives rise to excessive risk or could lead to a material financial loss to such firm. In June 2010, prior to the Dodd-Frank Act, the bank regulatory agencies promulgated the *Interagency Guidance on Sound Incentive Compensation Policies*, which sets forth three key principles concerning incentive compensation arrangements:

such arrangements should provide employees incentives that balance risk and financial results in a manner that does not encourage employees to expose the financial institution to imprudent risks;

such arrangements should be compatible with effective controls and risk management; and

such arrangements should be supported by strong corporate governance with effective and active oversight by the financial institution s board of directors.

Together, the Dodd-Frank Act and the recent guidance from the bank regulatory agencies on compensation may impact the Company s compensation practices.

The Consumer Financial Protection Bureau (Bureau). The Dodd-Frank Act created the Bureau within the Federal Reserve. The Bureau is tasked with establishing and implementing rules and regulations under certain federal consumer protection laws with respect to the conduct of providers of certain consumer financial products and services. The Bureau has rulemaking authority over many of the statutes governing products and services offered to bank consumers. In addition, the Dodd-Frank Act permits states to adopt consumer protection laws and regulations that are more stringent than those regulations promulgated by the Bureau and state attorneys general are permitted to enforce consumer protection rules adopted by the Bureau against state-chartered institutions. The Consumer Financial Protection Bureau has examination and enforcement authority over all banks and savings institutions with more than $10 billion in assets. Institutions with $10 billion or less in assets, such as the Bank, will continue to be examined for compliance with the consumer laws by their primary bank regulators.

De Novo Banking. The Dodd-Frank Act allows de novo interstate branching by banks.

Many aspects of the Dodd-Frank Act still remain subject to rulemaking by various regulatory agencies and will take effect over several years, making it difficult to anticipate the overall financial impact on the Company, its customers or the financial industry more generally. The elimination of the prohibition on the payment of interest on demand deposits could materially increase our interest expense, depending on our competitors responses. Provisions in the legislation that require revisions to the capital requirements of the Company and the Bank could require the Company and the Bank to seek additional sources of capital in the future.

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Proposed Legislation

From time to time proposals are made in the United States Congress, the New Jersey Legislature, and before various bank regulatory authorities, which would alter the powers of, and place restrictions on, different types of banking organizations. It is impossible to predict the impact, if any, of potential legislative trends on the business of the Company and its subsidiaries.

In accordance with federal law providing for deregulation of interest on all deposits, banks and thrift organizations are now unrestricted by law or regulation from paying interest at any rate on most time deposits. It is not clear whether deregulation and other pending changes in certain aspects of the banking industry will result in further increases in the cost of funds in relation to prevailing lending rates.

ITEM 1A Risk Factors.

Our business, financial condition, operating results and cash flows can be affected by a number of factors, including, but not limited to, those set forth below, any one of which could cause our actual results to vary materially from recent results or from our anticipated future results.

Recently enacted legislation, particularly the Dodd-Frank Act, could materially and adversely affect us by increasing compliance costs, heightening our risk of noncompliance with applicable regulations, and changing the competitive landscape in the banking industry.

From time to time, the U.S. Congress and state legislatures consider changing laws and enact new laws to further regulate the financial services industry. On July 21, 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, or the Dodd-Frank Act, was signed into law. The Dodd-Frank Act has resulted in sweeping changes in the regulation of financial institutions. As discussed in the section herein entitled Business-Supervision and Regulation, the Dodd-Frank Act contains numerous provisions that affect all banks and bank holding companies. Many of the provisions in the Dodd-Frank Act remain subject to regulatory rule-making and implementation, the effects of which are not yet known. Although we cannot predict the specific impact and long-term effects that the Dodd-Frank Act and the regulations promulgated thereunder will have on us and our prospects, our target markets and the financial industry more generally, we believe that the Dodd-Frank Act and the regulations promulgated thereunder are likely to impose additional administrative and regulatory burdens that will obligate us to incur additional expenses and will adversely affect our margins and profitability. For example, the elimination of the prohibition on the payment of interest on demand deposits could materially increase our interest expense, depending on our competitors responses. Provisions in the legislation that require revisions to the capital requirements of the Company and the Bank could require the Company and the Bank to seek additional sources of capital in the future. More stringent consumer protection regulations could materially and adversely affect our profitability. We will also have a heightened risk of noncompliance with all of the additional regulations. Finally, the impact of some of these new regulations is not known and may affect our ability to compete long-term with larger competitors.

The Federal Reserve s repeal of the prohibition against payment of interest on demand deposits may increase competition for such deposits and ultimately increase interest expense.

A major portion of our net income comes from our interest rate spread, which is the difference between the interest rates paid by us on amounts used to fund assets and the interest rates and fees we receive on our interest-earning assets. Our interest-earning assets include outstanding loans extended to our customers and securities held in our investment portfolio. We fund assets using deposits and other borrowings.

In July 2011, Regulation Q, which had prohibited the payment of interest on demand deposits by institutions that are member banks of the Federal Reserve System, was repealed. As a result, member banks and thrifts are

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now permitted to offer interest-bearing demand deposit accounts to commercial customers, which could result in increased competition for Lakeland for deposits. If we decide to pay interest on demand accounts in the face of such competition, we would expect our interest expense to increase.

The Company and the Bank may be subject to more stringent capital and liquidity requirements.

The Dodd-Frank Act also imposes more stringent capital requirements on bank holding companies such as Lakeland Bancorp by, among other things, imposing leverage ratios on bank holding companies and prohibiting new trust preferred issuances from counting as Tier I capital. These restrictions will limit our future capital strategies. Under the Dodd-Frank Act, our currently outstanding trust preferred securities will continue to count as Tier I capital, but we will be unable to issue replacement or additional trust preferred securities which would count as Tier I capital.

While U.S. banking regulators have postponed the implementation of the Basel III rules, which would generally be applicable to institutions with greater than $50 billion in assets, we expect that these rules will eventually be implemented in the U.S. In addition, banking regulators could implement additional changes to the capital adequacy standards applicable to financial institutions with $50 billion or less in assets, such as the Company and Lakeland, in light of Basel III.

Future increases in minimum capital requirements could adversely affect our net income. Furthermore, our failure to comply with the minimum capital requirements could result in our regulators taking formal or informal actions against us which could restrict our future growth or operations.

Recent negative developments in the financial services industry and U.S. and global credit markets may adversely impact our operations and results.

The general economic downturn during the past few years, including a decline in the value of the collateral supporting loans, has resulted in the deterioration of loan portfolio performances at many institutions. The competition for our deposits has increased significantly due to liquidity concerns at many of these same institutions. Stock prices of bank holding companies, like ours, have been negatively affected by the current condition of the financial markets, as has our ability, if needed, to raise capital or borrow in the debt markets compared to prior years. While economic growth may have resumed recently, the rate of this growth has been very slow and unemployment remains at a high level. As a result, recent legislation, such as the Dodd-Frank Act, will require new regulations regarding lending and funding practices and liquidity standards, and financial institution regulatory agencies are expected to be very aggressive in responding to concerns and trends identified in examinations, including the expected issuance of many formal enforcement actions. Negative developments in the financial services industry and the impact of new legislation, including The Dodd-Frank Act, in response to those developments could negatively impact our operations by restricting our business operations, including our ability to originate or sell loans, and adversely impact our financial performance.

The downgrade of the U.S. credit rating and Europe s debt crisis could have a material adverse effect on our business, financial condition and liquidity.

Standard & Poor s lowered its long term sovereign credit rating on the United States of America from AAA to AA+ on August 5, 2011. A further downgrade or a downgrade by other rating agencies could have a material adverse impact on financial markets and economic conditions in the United States and worldwide. Any such adverse impact could have a material adverse effect on our liquidity, financial condition and results of operations. Many of our investment securities are issued by and some of our loans are made to U.S. government agencies and U.S. government sponsored entities.

In addition, the possibility that certain European Union (EU) member states will default on their debt obligations have negatively impacted economic conditions and global markets. The continued uncertainty over

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the outcome of international and the EU s financial support programs and the possibility that other EU member states may experience similar financial troubles could further disrupt global markets. The negative impact on economic conditions and global markets could also have a material adverse effect on our liquidity, financial condition and results of operations.

A decrease in our ability to borrow funds could adversely affect our liquidity.

Our ability to obtain funding from the Federal Home Loan Bank or through our overnight federal funds lines with other banks could be negatively affected if we experienced a substantial deterioration in our financial condition or if such funding became restricted due to a further deterioration in the financial markets. While we have a contingency funds management plan to address such a situation if it were to occur (such plan includes deposit promotions, the sale of securities and the curtailment of loan growth, if necessary), a significant decrease in our ability to borrow funds could adversely affect our liquidity.

We are subject to interest rate risk and variations in interest rates may negatively affect our financial performance.

We are unable to predict actual fluctuations of market interest rates. Rate fluctuations are influenced by many factors, including:

- inflation or deflation
- excess growth or recession;
- a rise or fall in unemployment;
- tightening or expansion of the money supply;
- domestic and international disorder; and
- instability in domestic and foreign financial markets.

Both increases and decreases in the interest rate environment may reduce our profits. We expect that we will continue to realize income from the difference or spread between the interest we earn on loans, securities and other interest-earning assets, and the interest we pay on deposits, borrowings and other interest-bearing liabilities. Our net interest spreads are affected by the differences between the maturities and repricing characteristics of our interest-earning assets and interest-bearing liabilities. Our interest-earning assets may not reprice as slowly or rapidly as our interest-bearing liabilities. Changes in market interest rates could materially and adversely affect our net interest spread, asset quality, levels of prepayments, cash flows, the market value of our securities portfolio, loan and deposit growth, costs and yields on loans and deposits and our overall profitability.

The Company may incur impairment to goodwill.

We review our goodwill at least annually. Significant negative industry or economic trends, including the lack of recovery in the market price of our common stock price, reduced estimates of future cash flows or disruptions to our businesses, could indicate that goodwill might be impaired. Our valuation methodology for assessing impairment requires management to make judgments and assumptions based on historical experience and to rely on projections of future operating performance. We operate in a competitive environment and projections of future operating results and cash flows may vary significantly from actual results. Additionally, if our analysis results in an impairment to our goodwill, we would be required to record a non-cash charge to earnings in our financial statements during the period in which such impairment is determined to exist. Any such charge could have a material adverse effect on our results of operations and our stock price.

The extensive regulation and supervision to which we are subject impose substantial restrictions on our business.

The Company, Lakeland and certain non-bank subsidiaries are subject to extensive regulation and supervision. Banking regulations are primarily intended to protect depositors funds, federal deposit insurance funds and the banking system as a whole. Such laws are not designed to protect our shareholders. These regulations affect our lending practices, capital structure, investment practices, dividend policy and growth, among other things. Lakeland is also subject to a number of laws which, among other things, govern its lending practices and require the Bank to establish and maintain comprehensive programs relating to anti-money laundering and customer identification. The United States Congress and federal regulatory agencies continually review banking laws, regulations and policies for possible changes. Changes to statutes, regulations or regulatory policies, including changes in interpretation or implementation of statutes, regulations or policies, could affect us in substantial and unpredictable ways. Such changes could subject us to additional costs, limit the types of financial services and products we may offer and/or increase the ability of non-banks to offer competing financial services and products, among other things. Failure to comply with laws, regulations or policies could result in sanctions by regulatory agencies, civil money penalties and/or reputational damage, which could have a material adverse effect on our business, financial condition and results of operations.

Current levels of volatility in the capital markets are unprecedented and may adversely impact our operations and results.

The capital markets have been experiencing unprecedented volatility for the past several years. Such negative developments and disruptions have resulted in uncertainty in the financial markets and a general economic downturn. Bank and bank holding company stock prices have been negatively affected, as has the ability of banks and bank holding companies to raise capital or borrow in the debt markets compared to prior years. If current levels of market disruption and volatility continue or worsen, there can be no assurance that we will not experience an adverse effect, which may be material, on our business, financial condition and results of operations or our ability to access capital.

Lakeland s ability to pay dividends is subject to regulatory limitations which, to the extent that our holding company requires such dividends in the future, may affect our holding company s ability to pay its obligations and pay dividends to shareholders.

As a bank holding company, the Company is a separate legal entity from Lakeland and its subsidiaries, and we do not have significant operations of our own. We currently depend on Lakeland s cash and liquidity to pay our operating expenses and dividends to shareholders. The availability of dividends from Lakeland is limited by various statutes and regulations. The inability of the Company to receive dividends from Lakeland could adversely affect our financial condition, results of operations, cash flows and prospects and the Company s ability to pay dividends.

Our allowance for loan and lease losses may not be adequate to cover actual losses.

Like all commercial banks, Lakeland maintains an allowance for loan and lease losses to provide for loan and lease defaults and non-performance. If our allowance for loan and lease losses is not adequate to cover actual loan and lease losses, we may be required to significantly increase future provisions for loan and lease losses, which could materially and adversely affect our operating results. Our allowance for loan and lease losses is determined by analyzing historical loan and lease losses, current trends in delinquencies and charge-offs, plans for problem loan and lease resolution, the opinions of our regulators, changes in the size and composition of the loan and lease portfolio and industry information. We also consider the possible effects of economic events, which are difficult to predict. The amount of future losses is affected by changes in economic, operating and other conditions, including changes in interest rates, many of which are beyond our control. These losses may exceed our current estimates. Federal regulatory agencies, as an integral part of their examination process, review our loans and the allowance for loan and lease losses. While we believe that our allowance for loan and lease losses in relation to our current loan portfolio is adequate to cover current losses, we cannot assure you that we will not need to increase our allowance for loan and lease losses or that regulators will not require us to increase this allowance. Future increases in our allowance for loan and lease losses could materially and adversely affect our earnings and profitability.

We are subject to various lending and other economic risks that could adversely affect our results of operations and financial condition.

Economic, political and market conditions, trends in industry and finance, legislative and regulatory changes, changes in governmental monetary and fiscal policies and inflation affect our business. These factors are beyond our control. A further deterioration in economic conditions, particularly in New Jersey, could have the following consequences, any of which could materially adversely affect our business:

- loan and lease delinquencies may increase;
- problem assets and foreclosures may increase;
- demand for our products and services may decrease; and
- collateral for loans made by us may decline in value, in turn reducing the borrowing ability of our customers.

Further deterioration in the real estate market, particularly in New Jersey, could adversely affect our business. As real estate values in New Jersey decline, our ability to recover on defaulted loans by selling the underlying real estate is reduced, which increases the possibility that we may suffer losses on defaulted loans.

We may suffer losses in our loan portfolio despite our underwriting practices.

We seek to mitigate the risks inherent in our loan portfolio by adhering to specific underwriting practices. Although we believe that our underwriting criteria are appropriate for the various kinds of loans that we make, we may incur losses on loans that meet our underwriting criteria, and these losses may exceed the amounts set aside as reserves in our allowance for loan and lease losses.

We face strong competition from other financial institutions, financial service companies and other organizations offering services similar to the services that we provide.

Many competitors offer the types of loans and banking services that we offer. These competitors include other state and national banks, savings associations, regional banks and other community banks. We also face competition from many other types of financial institutions, including finance companies, brokerage firms, insurance companies, credit unions, mortgage banks and other financial intermediaries. Many of our competitors have greater financial resources than we do, which may enable them to offer a broader range of services and products, and to advertise more extensively, than we do. Our inability to compete effectively would adversely affect our business.

Declines in value may adversely impact our investment portfolio.

As of December 31, 2012, the Company had approximately $393.7 million and $96.9 million in available for sale and held to maturity investment securities, respectively. We may be required to record impairment charges on our investment securities if they suffer a decline in value that is considered other-than-temporary. Numerous factors, including lack of liquidity for sales of certain investment securities, absence of reliable pricing information for investment securities, adverse changes in business climate, adverse actions by regulators, or unanticipated changes in the competitive environment could have a negative effect on our investment portfolio in future periods. If an impairment charge is significant enough it could affect the ability of Lakeland to upstream dividends to us, which could have a material adverse effect on our liquidity and our ability to pay dividends to shareholders and could also negatively impact our regulatory capital ratios.

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Concern of customers over deposit insurance may cause a decrease in deposits.

With recent increased concerns about bank failures, customers increasingly are concerned about the extent to which their deposits are insured by the FDIC. Customers may withdraw deposits in an effort to ensure that the amount they have on deposit with their bank is fully insured. Decreases in deposits may adversely affect our funding costs and net income.

Increases in FDIC premiums could have a material adverse effect on our future earnings.

The FDIC insures deposits at FDIC insured financial institutions, including Lakeland Bank. The FDIC charges the insured financial institutions premiums to maintain the Deposit Insurance Fund at a certain level. The Dodd-Frank Act amended the Federal Deposit Insurance Act by changing the base against which an insured depository institution s deposit insurance assessment is calculated. These amendments require the appropriate assessment base to be calculated as the institution s average consolidated total assets minus average tangible equity, rather than the institution s deposits. These developments may cause an increase in Lakeland s future assessments. In addition, the FDIC may be required to increase assessment rates and levy special assessments on Lakeland and other financial institutions in the future, which could have a material adverse effect on Lakeland s future earnings.

A breach of information security could negatively affect our operations, earnings and reputation.

Increasingly, we depend upon data processing, communication and information exchange on a variety of computing platforms and networks, and over the internet. We cannot be certain all our systems are entirely free from vulnerability to attack, despite safeguards we have instituted including independent third party testing. In addition, we rely on the services of a variety of vendors to meet our data processing and communication needs. Disruptions to our vendors systems may arise from events that are wholly or partially beyond our vendors control (including, for example, computer viruses or electrical or telecommunications outages). The occurrence of system failures or security breaches, despite the controls we have instituted, could result in damage to our reputation, increased regulatory scrutiny and financial loss or costs to us.

Any unforeseen transition issues that arise in connection with upgrades to our computer hardware and software systems could adversely affect our business.

In the normal course of business, we upgrade certain hardware and software systems critical to our core banking operations and financial reporting. While we expect these changes to go smoothly, no assurances can be given that unforeseen issues will not arise. Depending on the nature of those issues, if any, and the time and resources necessary to correct or resolve them, our business could be adversely affected.

If we do not successfully integrate any banks that we may acquire in the future, the combined company may be adversely affected.

If our proposed acquisition of Somerset Hills Bancorp and Somerset Hills Bank is completed, and/or we make additional acquisitions in the future, we will need to integrate the acquired entities into our existing business and systems. We may experience difficulties in accomplishing this integration or in effectively managing the combined company after any future acquisition. Any actual cost savings or revenue enhancements that we may anticipate from a future acquisition will depend on future expense levels and operating results, the timing of certain events and general industry, regulatory and business conditions. Many of these events will be beyond our control, and we cannot assure you that if we make any acquisitions in the future, we will be successful in integrating those businesses into our own.

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ITEM 1B Unresolved Staff Comments.

Not Applicable.

ITEM 2 Properties.

The Company s principal office is located at 250 Oak Ridge Road, Oak Ridge, New Jersey 07438. The Company completed construction of a new training and operations center in Milton, New Jersey in mid-2012. The Bank purchased an assignment of an existing lease for this facility which expires on February 28, 2016, and contains five (5) five-year options to renew, at the Bank s discretion, at fixed base rent amounts. To the extent that the Bank exercises all of the options, the lease will expire on February 28, 2041.

The Company operates 46 banking locations in Passaic, Morris, Sussex, Bergen, Essex and Warren Counties, New Jersey. The following chart provides information about the Company s leased banking locations:

Location	Lease Expiration Date
Bristol Glen	October 31, 2013
Caldwell	September 30, 2024
Carlstadt	July 15, 2016
Cedar Crest	August 19, 2016
Hackensack	March 31, 2018
Hampton	September 30, 2019
Little Falls	November 30, 2015
Madison Avenue	April 30, 2017
North Haledon	June 30, 2017
Park Ridge	December 31, 2014
Pompton Plains	April 30, 2015
Ringwood	February 28, 2018
Rochelle Park	January 12, 2019
Sparta	August 31, 2032
Sussex/Wantage	June 19, 2017
Vernon	September 30, 2027
Wantage	October 31, 2016
Wayne	May 31, 2028
Wharton	July 31, 2015
Woodland Commons	August 31, 2016
West Caldwell	March 31, 2029

The Company has also entered into leases for two additional locations for administrative purposes, one in Wyckoff, New Jersey (this lease expires on February 28, 2014) and the other in Oak Ridge, New Jersey (this lease expires on January 31, 2014).

All other offices of the Company and Lakeland are owned and are unencumbered.

ITEM 3 Legal Proceedings.

On February 15, 2013, the Company was served with a Civil Action Summons and Class Action Complaint that was filed in the Superior Court of New Jersey, Chancery Division, Somerset County. The complaint states that the plaintiff is bringing the class action on behalf of the public stockholders of Somerset Hills Bancorp against the Board of Directors of Somerset Hills for their alleged breach of fiduciary duties arising out of the Agreement and Plan of Merger, dated as of January 28, 2013, by and between the Company and Somerset Hills Bancorp. The complaint alleges that the Company has aided and abetted the individual defendants in their alleged breaches of fiduciary duties. The Company intends to vigorously defend against these claims.

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Other than as described above, there are no pending legal proceedings involving the Company or Lakeland other than those arising in the normal course of business. Management does not anticipate that the potential liability, if any, arising out of such legal proceedings will have a material effect on the financial condition or results of operations of the Company and Lakeland on a consolidated basis.

ITEM 3A Executive Officers of the Registrant.

The following table sets forth the name and age of each executive officer of the Company. Each officer is appointed by the Company s Board of Directors. Unless otherwise indicated, the persons named below have held the position indicated for more than the past five years.

Name and Age	Officer of the Company Since	Position with the Company, its Subsidiary Banks, and Business Experience
Thomas J. Shara Age 55	2008	President and CEO, Lakeland Bancorp, Inc. (April 2, 2008 Present); President (April 2, 2008 January 29, 2013) and CEO (April 2, 2008 Present), Lakeland Bank; President and Chief Credit Officer (May 2007 April 1, 2008) and Executive Vice President and Senior Commercial Banking Officer (February 2006 May 2007), TD Banknorth, N.A. s Mid-Atlantic Division; Executive Vice President and Senior Loan Officer, Hudson United Bancorp and Hudson United Bank (prior years to February 2006)
Robert A. Vandenbergh Age 61	1999	Senior Executive Vice President and Chief Operating Officer of the Company (October 2008 Present) and of Lakeland Bank (October 2008 January 29, 2013); President of Lakeland Bank (January 29, 2013 Present); Senior Executive Vice President and Chief Lending Officer of the Company (December 2006 October 2008); Executive Vice President and Chief Lending Officer of the Company (October 1999 December 2006)
Joseph F. Hurley Age 62	1999	Executive Vice President and Chief Financial Officer of the Company (November 1999 Present)
Jeffrey J. Buonforte Age 61	1999	Executive Vice President and Senior Government Banking/Business Services Officer of the Company (June 2009 Present); Executive Vice President and Chief Retail Officer of the Company (November 1999 June 2009)
Louis E. Luddecke Age 66	1999	Executive Vice President and Chief Operations Officer of the Company (October 1999 Present)
David S. Yanagisawa Age 61	2008	Executive Vice President and Chief Lending Officer of the Company (November 2008 Present); Senior Vice President, TD Banknorth, N.A. (February 2006 November 2008); Hudson United Bank, Senior Vice President (1997 February 2006)
James R. Noonan Age 61	2003	Executive Vice President and Chief Credit Officer of the Company (December 2003 Present)
Ronald E. Schwarz Age 57	2009	Executive Vice President and Chief Retail Officer of the Company (June 2009 Present); Executive Vice President and Market Executive of Sovereign Bank (June 2006 June 2009); Senior Vice President and Director of Retail Banking of Independence Community Bank (June 1999 June 2006)

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Name and Age	Officer of the Company Since	Position with the Company, its Subsidiary Banks, and Business Experience
Timothy J. Matteson, Esq. Age 43	2008	Executive Vice President and General Counsel of the Company (March 2012 to Present); Senior Vice President and General Counsel of the Company (September 2008 March 2012); Assistant General Counsel, Israel Discount Bank (November 2007 September 2008); Senior Attorney and Senior Vice President, TD Banknorth, N.A. (February 2006 May 2007); General Counsel and Senior Vice President, Hudson United Bancorp and Hudson United Bank (January 2005 February 2006)

ITEM 4 MINE SAFETY DISCLOSURES.

Not applicable.

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PART II

ITEM 5 MARKET FOR THE REGISTRANT S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES.

Shares of the common stock of Lakeland Bancorp, Inc. have been traded under the symbol LBAI on the NASDAQ Global Select Market (or the NASDAQ National Market) since February 22, 2000 and in the over the counter market prior to that date. As of December 31, 2012, there were 3,227 shareholders of record of the common stock. The following table sets forth the range of the high and low daily closing prices of the common stock as provided by NASDAQ and dividends declared for the periods presented. All information is adjusted for the Company s 5% stock dividends distributed on April 16, 2012 and February 16, 2011.

	High	Low	Dividends Declared
Year ended December 31, 2012			
First Quarter	$ 10.21	$ 8.33	$ 0.057
Second Quarter	10.52	8.75	0.060
Third Quarter	10.97	9.09	0.060
Fourth Quarter	10.77	8.45	0.070

	High	Low	Dividends Declared
Year ended December 31, 2011			
First Quarter	$ 10.48	$ 8.92	$ 0.054
Second Quarter	10.95	8.71	0.057
Third Quarter	10.44	6.90	0.057
Fourth Quarter	9.30	6.90	0.057

Dividends on the Company s common stock are within the discretion of the Board of Directors of the Company and are dependent upon various factors, including the future earnings and financial condition of the Company and Lakeland and bank regulatory policies.

The Bank Holding Company Act of 1956 restricts the amount of dividends the Company can pay. Accordingly, dividends should generally only be paid out of current earnings, as defined.

The New Jersey Banking Act of 1948 restricts the amount of dividends paid on the capital stock of New Jersey chartered banks. Accordingly, no dividends shall be paid by such banks on their capital stock unless, following the payment of such dividends, the capital stock of the bank will be unimpaired and the bank will have a surplus of not less than 50% of its capital stock, or, if not, the payment of such dividend will not reduce the surplus of the bank. Under this limitation, approximately $219.0 million was available for the payment of dividends from Lakeland to the Company as of December 31, 2012.

Capital guidelines and other regulatory requirements may further limit the Company s and Lakeland s ability to pay dividends. See Item 1 Business Supervision and Regulation Dividend Restrictions.

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Performance Graph

The following chart compares the Company s cumulative total shareholder return (on a dividend reinvested basis) over the past five years with the NASDAQ Market Index and the Peer Group Index. The Peer Group Index is the Zacks (formerly Morningstar) Regional Northeast Banks Index, which consists of 158 Regional Northeast Banks.

Company/Market/Peer Group	12/31/2007	12/31/2008	12/31/2009	12/31/2010	12/31/2011	12/31/2012
Lakeland Bancorp, Inc.	100.00	100.33	59.19	103.99	87.86	111.75
NASDAQ Market Index	100.00	60.02	87.25	103.08	102.27	120.42
Zacks Regional Northeast Banks	100.00	70.02	66.58	78.30	73.30	96.70

ITEM 6 Selected Financial Data

SELECTED CONSOLIDATED FINANCIAL DATA

The following should be read in conjunction with Management s Discussion and Analysis and Results of Operations and the Company s consolidated financial statements included in item 7 and 8 of this report. The selective financial data set forth below has been derived from the Company s audited consolidated financial statements.

	2012	2011	2010	2009	2008
		(in thousands except per share data)			
Years Ended December 31					
Interest income	**$ 110,959**	$ 117,524	$ 125,649	$ 133,822	$ 143,937
Interest expense	**15,446**	20,111	25,895	40,443	55,358
Net interest income	**95,513**	97,413	99,754	93,379	88,579
Provision for loan and lease losses	**14,907**	18,816	19,281	51,615	23,730
Noninterest income excluding gains on investment securities	**17,856**	16,888	17,654	15,952	17,558
Gains on sales of investment securities	**1,049**	1,229	1,742	3,845	53
Other than temporary impairment losses on equity securities			(128)	(940)	
Noninterest expenses	**67,673**	68,151	70,405	73,794	60,071
Income (loss) before income taxes (benefit)	**31,838**	28,563	29,336	(13,173)	22,389
Income tax provision (benefit)	**10,096**	8,712	10,125	(7,777)	7,224
Net income (loss)	**21,742**	19,851	19,211	(5,396)	15,165
Dividends on preferred stock and accretion	**620**	2,167	3,987	3,194	
Net income (loss) available to common shareholders	**$ 21,122**	$ 17,684	$ 15,224	$ (8,590)	$ 15,165
Per-Share Data(1)					
Weighted average shares outstanding:					
Basic	**27,619**	26,572	26,352	26,099	25,870
Diluted	**27,692**	26,681	26,384	26,099	25,963
Earnings (loss) per share:					
Basic	**$ 0.76**	$ 0.66	$ 0.57	($ 0.33)	$ 0.58
Diluted	**$ 0.76**	$ 0.66	$ 0.57	($ 0.33)	$ 0.58
Cash dividend per common share	**$ 0.25**	$ 0.23	$ 0.19	$ 0.27	$ 0.36
Book value per common share	**$ 9.45**	$ 8.99	$ 8.40	$ 8.05	$ 8.46
Tangible book value per common share(2)	**$ 6.52**	$ 5.75	$ 5.10	$ 4.68	$ 5.02
At December 31					
Investment securities available for sale and other	**$ 399,092**	$ 471,944	$ 487,107	$ 375,530	$ 282,174
Investment securities held to maturity	**96,925**	71,700	66,573	81,821	110,114
Loans and leases, net of deferred costs	**2,146,843**	2,041,575	2,014,617	2,017,035	2,034,831
Goodwill and other identifiable intangible assets	**87,111**	87,111	87,689	88,751	89,812
Total assets	**2,918,703**	2,825,950	2,792,674	2,723,968	2,642,625
Total deposits	**2,370,997**	2,249,653	2,195,889	2,157,187	2,056,133
Total core deposits	**2,067,205**	1,890,101	1,783,040	1,691,447	1,445,101
Term borrowings	**136,548**	232,322	272,322	223,222	288,222
Total stockholders equity	**280,867**	259,783	260,709	267,986	220,941
Performance ratios					
Return on Average Assets(3)	**0.77%**	0.71%	0.69%	NM	0.59%
Return on Average Common Equity(3)	**8.48%**	8.53%	8.70%	NM	6.99%
Return on Average Equity(3)	**8.42%**	7.79%	7.13%	NM	6.99%
Efficiency ratio(4)	**58.33%**	56.87%	56.40%	62.06%	54.72%
Net Interest Margin (tax equivalent basis)	**3.70%**	3.85%	3.95%	3.74%	3.79%
Loans to Deposits	**90.55%**	90.75%	91.74%	93.50%	98.96%
Capital ratios					

Common Equity to Asset ratio	**9.62%**	8.54%	7.99%	7.78%	8.36%
Tangible common equity to tangible assets(2)	**6.84%**	5.63%	5.01%	4.68%	5.14%
Equity to Asset ratio	**9.62%**	9.19%	9.34%	9.84%	8.36%
Tier 1 leverage ratio	**8.62%**	8.33%	9.21%	9.44%	8.08%
Tier 1 risk-based capital ratio	**11.52%**	11.23%	12.43%	12.65%	10.24%
Total risk-based capital ratio	**12.77%**	13.39%	13.68%	13.90%	11.52%

(1) Restated for 5% stock dividends in 2012 and 2011.

(2) A non-GAAP financial measure. See Non-GAAP Financial Measures for a reconciliation of such measures to data calculated in accordance with generally accepted accounting principles.

(3) Ratios for 2009 are not meaningful (NM) and therefore not presented.

(4) Ratio represents non-interest expense, excluding other real estate expense, other repossessed asset expense, long-term debt prepayment fee, provision for unfunded lending commitments and core deposit amortization, as a percentage of total revenue (calculated on a tax equivalent basis), excluding gains (losses) on securities. Total revenue represents net interest income (calculated on a tax equivalent basis) plus non-interest income.

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ITEM 7 Management s Discussion and Analysis of Financial Condition and Results of Operations

This section presents a review of Lakeland Bancorp, Inc. s consolidated results of operations and financial condition. You should read this section in conjunction with the selected consolidated financial data that is presented on the preceding page as well as the accompanying consolidated financial statements and notes to financial statements. As used in the following discussion, the term Company refers to Lakeland Bancorp, Inc. and Lakeland refers to the Company s wholly owned banking subsidiary Lakeland Bank.

Statements Regarding Forward-Looking Information

The information disclosed in this document includes various forward-looking statements that are made in reliance upon the safe harbor provisions of the Private Securities Litigation Reform Act of 1995 with respect to credit quality (including delinquency trends and the allowance for loan and lease losses), corporate objectives, and other financial and business matters. The words anticipates, projects, intends, estimates, expects, believes, plans, may, will, should, could, and other similar expressions are intended to identify such forward-looking statemen Company cautions that these forward-looking statements are necessarily speculative and speak only as of the date made, and are subject to numerous assumptions, risks and uncertainties, all of which may change over time. Actual results could differ materially from such forward-looking statements.

In addition to the risk factors disclosed elsewhere in this document, the following factors, among others, could cause the Company s actual results to differ materially and adversely from such forward-looking statements: changes in the financial services industry and the U.S. and global capital markets, changes in economic conditions nationally, regionally and in the Company s markets, the nature and timing of actions of the Federal Reserve Board and other regulators, the nature and timing of legislation affecting the financial services industry including but not limited to the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, government intervention in the U.S. financial system, changes in levels of market interest rates, pricing pressures on loan and deposit products, credit risks of the Company s lending and leasing activities, customers acceptance of the Company s products and services and competition.

The above-listed risk factors are not necessarily exhaustive, particularly as to possible future events, and new risk factors may emerge from time to time. Certain events may occur that could cause the Company s actual results to be materially different than those described in the Company s periodic filings with the Securities and Exchange Commission. Any statements made by the Company that are not historical facts should be considered to be forward-looking statements. The Company is not obligated to update and does not undertake to update any of its forward-looking statements made herein.

Critical Accounting Policies, Judgments and Estimates

The accounting and reporting policies of the Company and Lakeland conform with accounting principles generally accepted in the United States of America (U.S. GAAP) and predominant practices within the banking industry. The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements. These estimates and assumptions also affect reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates. Significant estimates implicit in these financial statements are as follows. For additional accounting policies and detail, refer to Note 1 to the consolidated financial statements included in item 8 of this report.

Allowance for loan and lease losses. The allowance for loan and lease losses is established through a provision for loan and lease losses charged to expense. Loan principal considered to be uncollectible by management is charged against the allowance for loan and lease losses. The allowance is an amount that management believes will be adequate to absorb losses on existing loans and leases that may become

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uncollectible based upon an evaluation of known and inherent risks in the loan and lease portfolio. The evaluation takes into consideration such factors as changes in the nature and size of the loan and lease portfolio, overall portfolio quality, specific problem loans and leases, and current economic conditions which may affect the borrowers ability to pay. The evaluation also analyzes historical losses by loan and lease category, and considers the resulting loss rates when determining the reserves on current loan and lease total amounts. Loss estimates for specified problem loans and leases are also detailed. All of the factors considered in the analysis of the adequacy of the allowance for loan and lease losses may be subject to change. To the extent actual outcomes differ from management estimates, additional provisions for loan and lease losses may be required that would adversely impact earnings in future periods.

Loans and leases are considered impaired when, based on current information and events, it is probable that Lakeland will be unable to collect all amounts due in accordance with the original contractual terms of the loan agreement, including scheduled principal and interest payments. Impairment is measured based on the present value of expected cash flows discounted at the loan s effective interest rate, except that as a practical expedient, a creditor may measure impairment based on a loan s observable market price, or the fair value of the collateral if the loan is collateral-dependent. Regardless of the measurement method, a creditor must measure impairment based on the fair value of the collateral when the creditor determines that foreclosure is probable. Most of Lakeland s impaired loans are collateral-dependent. Lakeland groups impaired commercial loans under $250,000 into a homogeneous pool and collectively evaluates them. Interest received on impaired loans and leases may be recorded as interest income. However, if management is not reasonably certain that an impaired loan and lease will be repaid in full, or if a specific time frame to resolve full collection cannot yet be reasonably determined, all payments received are recorded as reductions of principal.

Fair value measurements and fair value of financial instruments. Fair values of financial instruments are volatile and may be influenced by a number of factors, including market interest rates, prepayment speeds, discount rates, credit ratings and yield curves. Fair values for investment securities are based on quoted market prices, where available. If quoted market prices are not available, fair values are based on the quoted prices of similar instruments or an estimate of fair value by using a range of fair value estimates in the market place as a result of the illiquid market specific to the type of security.

When the fair value of a security is below its amortized cost, and depending on the length of time the condition exists and the extent the fair value is below amortized cost, additional analysis is performed to determine whether an other-than-temporary impairment condition exists. Available-for-sale and held-to-maturity securities are analyzed quarterly for possible other-than-temporary impairment. The analysis considers (i) the length of time and the extent to which the fair value has been less than cost, (ii) the financial condition and near-term prospects of the issuer, and (iii) the intent and ability of the Company to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value. Often, the information available to conduct these assessments is limited and rapidly changing, making estimates of fair value subject to judgment. If actual information or conditions are different than estimated, the extent of the impairment of the security may be different than previously estimated, which could have a material effect on the Company s results of operations and financial condition.

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

The Company evaluates tax positions that may be uncertain using a recognition threshold of more-likely-than-not, and a measurement attribute for all tax positions taken or expected to be taken on a tax return, in order for those tax positions to be recognized in the financial statements. Additional information regarding the Company s uncertain tax positions is set forth in Note 9 to the Notes to the audited Consolidated Financial Statements contained herein.

Goodwill and other identifiable intangible assets. The Company reviews goodwill for impairment annually as of November 30 or when circumstances indicate a potential for impairment at the reporting unit level. U.S. GAAP requires at least an annual review of the fair value of a reporting unit that has goodwill in order to determine if it is more likely than not (that is, a likelihood of more than 50%) that the fair value of a reporting unit is less than its carrying amount, including goodwill. If this qualitative test determines it is unlikely (less than 50% probability) the carrying value of the Reporting Unit is less than its fair value, then the company does not have to perform a Step One impairment test. If the probability is greater than 50%, a Step One goodwill impairment test is required. The Step One test compares the fair value of each reporting unit to the carrying value of its net assets, including goodwill. The Company has determined that it has one reporting unit, Community Banking.

The Company performed a qualitative analysis to determine whether the weight of evidence, the significance of all identified events and circumstances indicated a greater than 50% likelihood existed that the carrying value of the Reporting Unit exceeded its fair value and if a Step One Test would be required. The Company identified nine qualitative assessments that are relative to the banking industry and to the Company. These factors included macroeconomic factors, banking industry conditions, banking merger and acquisition trends, Lakeland s historical performance, the Company s stock price, the expected performance of Lakeland, the change of control premium of the Company versus its peers and other miscellaneous factors. After reviewing and weighting these factors, the Company, as well as a third party adviser, determined as of November 30, 2012 that there was a less than 50% probability that the fair value of the Company was less than its carrying amount. Therefore, no Step One test was required.

Financial Overview

The year ended December 31, 2012 represented a year of continued growth for the Company. As discussed in this management s discussion and analysis:

Net income available to common shareholders increased $3.4 million or 19% to $21.1 million in 2012.

Total loans increased $105.9 million, or 5%, from 2011 to 2012.

Core deposits increased $177.1 million, or 9%, to $2.07 billion at year end 2012 and represented 87% of total deposits at December 31, 2012 compared to 84% at December 31, 2011.

Total noninterest-bearing deposits of $498.1 million increased $48.5 million, or 11%, from 2011.

The Company redeemed its remaining 19,000 shares of its Fixed Rate Cumulative Preferred Stock, Series A originally issued to the U.S. Department of the Treasury under the Troubled Asset Relief Program Capital Purchase Program (CPP). As a result of CPP repayments, dividends on preferred stock and accretion of the preferred stock discount declined from $2.2 million in 2011 to $620,000 in 2012. In 2012, the Company also repurchased the outstanding common stock warrant previously issued to the Treasury for a price of $2.8 million, completing the Company s participation in the Treasury s CPP.

In September 2012, the Company received $25.0 million in net proceeds from common stock offerings which allowed the Company to increase its tangible equity. On October 7, 2012 the Company redeemed $25.8 million in subordinated debentures that had a coupon rate of 7.535%.

Non-performing assets declined $21.7 million, or 43%, to $28.5 million at December 31, 2012 compared to December 31, 2011. The Allowance for Loan and Lease Losses at December 31, 2012 was 103% of non-performing loans compared to 58% at December 31, 2011.

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Net income for 2012 was $21.7 million compared to net income of $19.9 million in 2011. Net income available to common shareholders in 2012 was $21.1 million or $0.76 per diluted share compared to $17.7 million or $0.66 per diluted share in 2011.

Net interest income

Net interest income is the difference between interest income on earning assets and the cost of funds supporting those assets. The Company s net interest income is determined by: *(i)* the volume of interest-earning assets that it holds and the yields that it earns on those assets, and *(ii)* the volume of interest-bearing liabilities that it has assumed and the rates that it pays on those liabilities. Net interest income increases when the Company can use noninterest- bearing deposits to fund or support interest-earning assets. The Company s net interest margin has been influenced by the current low interest rate environment. For more information about how interest rate change can influence the Company s net interest income and how the Company manages its net interest income, see Interest Rate Risk below. The Company s net interest margin can also be influenced by its level of non-performing loans. If non-performing loans decline, this could positively influence the Company s net interest margin.

Net interest income for 2012 on a tax-equivalent basis was $96.5 million, representing a decrease of $2.0 million, or 2%, from the $98.5 million earned in 2011. The decrease in net interest income primarily resulted from a 34 basis point decrease in the yield on interest-earning assets, which was partially offset by a 22 basis point decline in the cost of interest-bearing liabilities. The net interest spread as a result declined 12 basis points to 3.55%. Although the net interest spread declined, the decline was mitigated by an increase in income earned on free funds (interest-earning assets funded by non-interest bearing liabilities) resulting from an increase in average non-interest bearing deposits of $52.0 million. The components of net interest income will be discussed in greater detail below.

Interest income and expense volume/rate analysis. The following table shows the impact that changes in average balances of the Company s assets and liabilities and changes in average interest rates have had on the Company s net interest income over the past three years. This information is presented on a tax equivalent basis assuming a 35% tax rate. If a change in interest income or expense is attributable to a change in volume and a change in rate, the amount of the change is allocated proportionately.

INTEREST INCOME AND EXPENSE VOLUME/RATE ANALYSIS

(tax equivalent basis, in thousands)

	2012 vs. 2011 Increase (Decrease) Due to Change in:			2011 vs. 2010 Increase (Decrease) Due to Change in:		
	Volume	**Rate**	**Total Change**	**Volume**	**Rate**	**Total Change**
Interest Income						
Loans and leases	**$ 4,284**	**$ (8,356)**	**$ (4,072)**	$ 140	$ (7,139)	$ (6,999)
Taxable investment securities and other	**(560)**	**(1,748)**	**(2,308)**	639	(1,691)	(1,052)
Tax-exempt investment securities	**(5)**	**(279)**	**(284)**	340	(346)	(6)
Federal funds sold				(40)	(30)	(70)
Total interest income	**3,719**	**(10,383)**	**(6,664)**	1,079	(9,206)	(8,127)
Interest Expense						
Savings deposits	**25**	**(113)**	**(88)**	26	(180)	(154)
Interest-bearing transaction accounts	**488**	**(1,449)**	**(961)**	49	(2,276)	(2,227)
Time deposits	**(753)**	**(732)**	**(1,485)**	(750)	(1,186)	(1,936)
Borrowings	**(1,110)**	**(1,021)**	**(2,131)**	(226)	(1,241)	(1,467)
Total interest expense	**(1,350)**	**(3,315)**	**(4,665)**	(901)	(4,883)	(5,784)
NET INTEREST INCOME (TAX EQUIVALENT BASIS)	**$ 5,069**	**$ (7,068)**	**$ (1,999)**	$ 1,980	$ (4,323)	$ (2,343)

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The following table reflects the components of the Company s net interest income, setting forth for the years presented, (1) average assets, liabilities and stockholders equity, (2) interest income earned on interest-earning assets and interest expense paid on interest-bearing liabilities, (3) average yields earned on interest-earning assets and average rates paid on interest-bearing liabilities, (4) the Company s net interest spread (i.e., the average yield on interest-earning assets less the average cost of interest-bearing liabilities) and (5) the Company s net interest margin. Rates are computed on a tax equivalent basis assuming a 35% tax rate.

CONSOLIDATED STATISTICS ON A TAX EQUIVALENT BASIS

	2012			2011			2010		
	Average Balance	Interest Income/ Expense	Average rates earned/ paid	Average Balance	Interest Income/ Expense	Average rates earned/ paid	Average Balance	Interest Income/ Expense	Average rates earned/ paid
				(dollars in thousands)					
Assets									
Interest-earning assets:									
Loans and leases(A)	**$ 2,073,562**	**$ 100,513**	**4.85%**	$ 1,997,652	$ 104,585	5.24%	$ 1,995,158	$ 111,584	5.59%
Taxable investment securities and other	**435,733**	**8,574**	**1.97%**	460,413	10,882	2.36%	438,653	11,934	2.72%
Tax-exempt securities	**70,309**	**2,802**	**3.98%**	70,437	3,086	4.38%	63,093	3,092	4.90%
Federal funds sold(B)	**30,373**	**51**	**0.17%**	31,939	51	0.16%	53,178	121	0.23%
Total interest-earning assets	**2,609,977**	**111,940**	**4.29%**	2,560,441	118,604	4.63%	2,550,082	126,731	4.97%
Noninterest earning assets:									
Allowance for loan and lease losses	**(29,091)**			(29,064)			(27,459)		
Other assets	**252,055**			251,452			254,346		
TOTAL ASSETS	**$ 2,832,941**			$ 2,782,829			$ 2,776,969		
Liabilities and Stockholders Equity									
Interest-bearing liabilities:									
Savings accounts	**$ 347,766**	**$ 366**	**0.11%**	$ 330,646	$ 454	0.14%	$ 317,620	$ 608	0.19%
Interest-bearing transaction accounts	**1,171,318**	**4,813**	**0.41%**	1,088,678	5,774	0.53%	1,082,026	8,001	0.74%
Time deposits	**329,355**	**3,165**	**0.96%**	400,442	4,650	1.16%	456,692	6,586	1.44%
Borrowings	**237,814**	**7,102**	**2.99%**	272,744	9,233	3.39%	278,754	10,700	3.84%
Total interest-bearing liabilities	**2,086,253**	**15,446**	**0.74%**	2,092,510	20,111	0.96%	2,135,092	25,895	1.21%
Noninterest-bearing liabilities:									
Demand deposits	**474,579**			422,568			359,915		
Other liabilities	**13,826**			12,776			12,702		
Stockholders equity	**258,283**			254,975			269,260		
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	**$ 2,832,941**			$ 2,782,829			$ 2,776,969		
Net interest income/spread		**96,494**	**3.55%**		98,493	3.67%		100,836	3.76%
Tax equivalent basis adjustment		**981**			1,080			1,082	
NET INTEREST INCOME		**$ 95,513**			$ 97,413			$ 99,754	
Net interest margin(C)			**3.70%**			3.85%			3.95%

(A) Includes non-accrual loans, the effect of which is to reduce the yield earned on loans, and deferred loan fees.
(B) Includes interest-bearing cash accounts.

(C) Net interest income on a tax equivalent basis divided by interest-earning assets.

Interest income on a tax equivalent basis decreased from $118.6 million in 2011 to $111.9 million in 2012, a decrease of $6.7 million, or 6%. The decrease in interest income was due to a 34 basis point decrease in the average yield on interest-earning assets, as a result of loans being refinanced at lower rates and lower yields on new loans and investments. The yield on average loans and leases at 4.85% in 2012 was 39 basis points lower than 2011. The yield on average taxable and tax-exempt investment securities decreased by 39 basis points to 1.97% and 40 basis points to 3.98%, respectively, in 2012.

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Interest income on a tax equivalent basis decreased from $126.7 million in 2010 to $118.6 million in 2011, a decrease of $8.1 million, or 6%. The decrease in interest income was due to a 34 basis point decrease in the average yield on interest-earning assets, as a result of loans being refinanced at lower rates and lower yields on new loans and investments. The yield on average loans and leases at 5.24% in 2011 was 35 basis points lower than 2010. The yield on average taxable and tax-exempt investment securities decreased by 36 basis points to 2.36% and 52 basis points to 4.38%, respectively, in 2011.

Total interest expense decreased from $20.1 million in 2011 to $15.4 million in 2012, a decrease of $4.7 million, or 23%. Average interest-bearing liabilities decreased $6.3 million while the cost of those liabilities decreased from 0.96% in 2011 to 0.74% in 2012. The decrease in yield was due primarily to the continuing low rate environment and a $71.1 million reduction in higher yielding time deposits as customers preferred to keep their deposits in short-term transaction accounts. Additionally, higher yielding average borrowings decreased $34.9 million to $237.8 million in 2012. Contributing to the decrease in borrowings was a payment early in the fourth quarter of 2012 of a $25.8 million subordinated debenture with a yield of 7.535%. The decrease in time deposits and borrowings was offset by increases in savings accounts, interest-bearing transaction accounts, and non-interest bearing deposits of $17.1 million, $82.6 million, and $52.0 million, respectively.

Total interest expense decreased from $25.9 million in 2010 to $20.1 million in 2011, a decrease of $5.8 million, or 22%. Average interest-bearing liabilities decreased $42.6 million and the cost of those liabilities decreased from 1.21% in 2010 to 0.96% in 2011. The decrease in yield was due primarily to the continuing low rate environment and a $56.3 million reduction in higher yielding time deposits as customers preferred to keep their deposits in short-term transaction accounts. The decrease in time deposits was offset by increases in savings accounts, interest-bearing transaction accounts, and non-interest bearing deposits of $13.0 million, $6.7 million, and $62.7 million, respectively.

Net Interest Margin

Net interest margin is calculated by dividing net interest income on a fully taxable equivalent basis by average interest-earning assets. The Company s net interest margin was 3.70%, 3.85% and 3.95% for 2012, 2011 and 2010, respectively. The decrease in net interest margin from 2011 to 2012 and from 2010 to 2011 was primarily a result of the decrease in yield on interest-earning assets. The net interest margins for 2012, 2011 and 2010 would have been 3.78%, 3.94% and 4.02%, respectively, had all of the non-accrual loans performed in accordance with their terms.

Provision for Loan and Lease Losses

In determining the provision for loan and lease losses, management considers national and local economic conditions; trends in the portfolio including orientation to specific loan types or industries; experience, ability and depth of lending management in relation to the complexity of the portfolio; adequacy and adherence to policies, procedures and practices; levels and trends in delinquencies, impaired loans and leases and net charge-offs and the results of independent third party loan review.

The provision for loan and lease losses decreased from $18.8 million in 2011 to $14.9 million in 2012. Net charge-offs decreased from $17.7 million or 0.89% of average loans and leases in 2011 to $14.4 million or 0.69% of average loans and leases in 2012. The lower provision resulted from a decline in non-performing assets and from lower charge-offs during 2012. During the second quarter of 2012, the Company sold a group of primarily non-performing loans with a net book value of $4.5 million and recorded a charge-off of $1.9 million.

The provision for loan and lease losses decreased from $19.3 million in 2010 to $18.8 million in 2011. Net charge-offs increased from $17.5 million or 0.88% of average loans and leases in 2010 to $17.7 million or 0.89% of average loans and leases in 2011.

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Noninterest Income

Noninterest income increased $788,000, or 4%, to $18.9 million in 2012 compared to 2011. Service charges on deposit accounts at $10.5 million increased $242,000, or 2%, due primarily to the implementation of a new demand deposit pricing structure in the second quarter of 2012. Commissions and fees totaled $4.5 million in 2012 and were $788,000 or 21% higher than 2011 due to an increase in investment commission income and loan fees. Other income at $1.0 million in 2012 was $516,000 higher than 2011 primarily due to net gains recorded on the sale of bank owned properties in 2012. Gains on sales of investment securities and gains on leasing related assets decreased $180,000 and $499,000, respectively, from 2011 to 2012. The decline in gains on leasing related assets reflects the reduction in the leasing portfolio. Noninterest income represented 17% of total revenue in 2012.

Noninterest income was $18.1 million in 2011 compared to $19.3 million earned in 2010. The decrease in this category is primarily due to a reduction in gains on leasing related assets and investment securities. In 2011, gains on investment securities totaled $1.2 million, which was a $513,000 reduction from the same period in 2010 and gains on leasing related assets at $974,000 in 2011 were $606,000 lower than in 2010. Additionally, there was $128,000 in other-than-temporary impairment losses taken on the Company s equity securities portfolio in 2010 compared to no losses in 2011. Other income at $526,000 in 2011 was $221,000 lower than 2010 due primarily to a reduction in gains on loans sold. Income on bank owned life insurance in 2011 totaling $1.4 million was $93,000 lower than the same period in 2010 due primarily to decreases in rates on the underlying policies. Commissions and fees at $3.7 million in 2011 were $170,000 greater than the same period in 2010 due primarily to an increase in investment commission income. Noninterest income represented 16% of total revenue in 2011.

Noninterest Expense

Noninterest expense totaling $67.7 million decreased $478,000 in 2012 compared to 2011. FDIC insurance expense at $2.2 million was $627,000 lower than the same period in 2011 as a result of changes made by the FDIC in the method of calculating assessment rates. Collection expense, legal expense and expenses on other real estate and other repossessed assets decreased $127,000, $456,000 and $681,000, respectively, compared to 2011, resulting from the decline in the Company s non-performing assets. During the third quarter of 2011 the Company completed its core deposit intangible amortization, which resulted in a $577,000 decrease in that category. Marketing expense at $2.0 million decreased $375,000 or 16% due to the elimination of several marketing programs in 2012. Net occupancy expense at $7.1 million increased $204,000 compared to 2011 primarily as a result of increases in rental expense and depreciation expense for the new training and operations center, partially offset by a decline in snow removal expenses. Salaries and employee benefits at $38.6 million increased $2.1 million or 6% primarily due to normal salary increases, benefit increases and adjustments made to benefit plans to reflect the current interest rate environment.

Noninterest expense totaling $68.2 million decreased $2.3 million in 2011 compared to 2010. Long term debt prepayment fees in 2011 were $800,000 compared to $1.8 million for the same period in 2010 because the Company prepaid less long term debt in 2011 than in 2010. FDIC insurance expense at $2.8 million was $974,000 lower than the same period in 2010 as a result of changes made by the FDIC in the method of calculating assessment rates. Collection expense at $343,000 decreased $249,000, which reflects lower leasing related collection costs. Stationery, supplies and postage at $1.4 million and marketing expense at $2.4 million decreased $240,000 and $291,000, respectively, in 2011, primarily as a result of costs incurred for the Company s new brand identity project in 2010. During the third quarter of 2011 the Company completed its core deposit intangible amortization, which resulted in a $485,000 decrease in that category. Other real estate and repossessed asset expense at $780,000 increased $297,000 as a result of increased expenses related to other real estate properties.

The efficiency ratio, a non-GAAP measure, expresses the relationship between noninterest expense (excluding other real estate and other repossessed asset expense, long-term debt repayment fees, provision for unfunded lending commitments and core deposit amortization) to total tax-equivalent revenue (excluding gains (losses) on securities). In 2012, the Company s efficiency ratio on a tax equivalent basis was 58.33% compared to 56.87% in 2011 as a result of an increase in adjusted expenses and decline in revenue. The efficiency ratio was 56.4% in 2010.

	For the year ended December 31,				
	2012	**2011**	**2010**	**2009**	**2008**
	(dollars in thousands)				
Calculation of efficiency ratio (a non-GAAP measure)					
Total non-interest expense	**$ 67,673**	$ 68,151	$ 70,405	$ 73,794	$ 60,071
Less:					
Amortization of core deposit intangibles		(577)	(1,062)	(1,062)	(1,062)
Other real estate owned and other repossessed asset expense	**(99)**	(780)	(483)	(1,002)	(155)
Long-term debt prepayment fee	**(782)**	(800)	(1,835)	(3,075)	
Provision for unfunded lending commitments	**(93)**	(375)	(195)	(58)	(76)
Non-interest expense, as adjusted	**$ 66,699**	$ 65,619	$ 66,830	$ 68,597	$ 58,778
Net interest income	**$ 95,513**	$ 97,413	$ 99,754	$ 93,379	$ 88,579
Noninterest income	**18,905**	18,117	19,268	18,857	17,611
Total revenue	**114,418**	115,530	119,022	112,236	106,190
Plus: Tax-equivalent adjustment on municipal securities	**981**	1,080	1,082	1,206	1,287
Less: Gains on sales of investment securities	**(1,049)**	(1,229)	(1,614)	(2,905)	(53)
Total revenue, as adjusted	**$ 114,350**	$ 115,381	$ 118,490	$ 110,537	$ 107,424
Efficiency ratio (Non-GAAP)	**58.33%**	56.87%	56.40%	62.06%	54.72%

Income Taxes

The Company s effective income tax rate was 31.7%, 30.5% and 34.5%, in the years ended December 31, 2012, 2011 and 2010, respectively. The effective tax rate increased from 30.5% in 2011 to 31.7% in 2012 as a result of increased earnings and because of a reduction of tax advantaged items as a percent of pre-tax income. Tax advantaged items include interest income on tax-exempt securities and income on bank owned life insurance. The Company s lower effective tax rate of 30.5% in 2011 compared to 2010 was driven by increased tax benefits attributable to the real estate investment trust (REIT) subsidiary established in December 2010.

Financial Condition

Total assets increased from $2.83 billion on December 31, 2011 to $2.92 billion on December 31, 2012, an increase of $92.8 million, or 3%. Total assets at year-end 2011 increased $33.3 million or 1% from year-end 2010.

Loans and Leases

Lakeland primarily serves Northern New Jersey and the surrounding areas. Its equipment finance division serves a broader market with a primary focus on the Northeast. All of its borrowers are U.S. residents or entities.

Gross loans and leases totaling $2.15 billion as of December 31, 2012, increased $105.9 million or 5% compared to 2011. The increase in gross loans and leases is due primarily to increases in commercial loans secured by real estate and residential mortgages, which was partially offset by a decrease in real estate construction loans. Commercial loans secured by real estate increased from $1.01 billion in 2011 to $1.13 billion

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in 2012, an increase of $112.2 million, or 11%. Residential mortgages at $423.3 million increased $17.0 million or 4% compared to 2011. Real estate construction loans, which include commercial construction loans, at $46.3 million decreased $32.9 million or 42%. Total loans and leases at $2.04 billion as of December, 31 2011 increased $29.0 million, or 1% compared to December 31, 2010 primarily due to increases in commercial loans secured by real estate and commercial and industrial loans, which increased $42.7 million and $15.7 million, respectively, partially offset by a $38.3 million decline in leases, including leases held for sale.

The following table sets forth the classification of Lakeland s gross loans and leases by major category as of December 31 for each of the last five years:

	2012	2011	December 31, 2010 (in thousands)	2009	2008
Commercial, secured by real estate	**$ 1,125,137**	$ 1,012,982	$ 970,240	$ 914,223	$ 815,237
Commercial, industrial and other	**216,129**	209,915	194,259	172,744	143,383
Leases	**26,781**	28,879	65,640	113,160	311,463
Leases held for sale			1,517	7,314	
Real estate residential mortgage	**423,262**	406,222	403,561	382,750	342,660
Real estate construction	**46,272**	79,138	70,775	108,338	102,219
Home equity and consumer	**309,626**	304,190	306,322	315,598	315,704
	2,147,207	2,041,326	2,012,314	2,014,127	2,030,666
Plus deferred costs (fees)	**(364)**	249	2,303	2,908	4,165
Loans and leases net of deferred costs (fees)	**$ 2,146,843**	$ 2,041,575	$ 2,014,617	$ 2,017,035	$ 2,034,831

At December 31, 2012, there were no concentrations of loans or leases exceeding 10% of total loans and leases outstanding other than loans that are secured by real estate. Loan concentrations are considered to exist when there are amounts loaned to a multiple number of borrowers engaged in similar activities which would cause them to be similarly impacted by economic or other related conditions.

The following table sets forth maturities and sensitivity to changes in interest rates in commercial loans in the Company s loan portfolio at December 31, 2012:

	Within one year	After one but within five years (in thousands)	After five years	Total
Commercial, secured by real estate	$ 88,554	$ 196,333	$ 840,250	$ 1,125,137
Commercial, industrial and other	110,938	74,971	30,220	216,129
Real estate construction	19,887	8,144	18,241	46,272
Total	$ 219,379	$ 279,448	$ 888,711	$ 1,387,538
Predetermined rates	$ 30,094	$ 194,830	$ 109,125	$ 334,049
Floating or adjustable rates	189,285	84,618	779,586	1,053,489
Total	$ 219,379	$ 279,448	$ 888,711	$ 1,387,538

Risk Elements

Commercial loans and leases are placed on a non-accrual status with all accrued interest and unpaid interest reversed if (a) because of the deterioration in the financial position of the borrower they are maintained on a cash basis (which means payments are applied when and as received rather than on a regularly scheduled basis), (b) payment in full of interest or principal is not expected, or (c) principal and interest have been in default for a

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period of 90 days or more unless the obligation is both well-secured and in process of collection. Residential mortgage loans are placed on non-accrual status at the time principal and interest have been in default for a period of 90 days or more, except where there exists sufficient collateral to cover the defaulted principal and interest payments, and management s knowledge of the specific circumstances warrant continued accrual. Consumer loans are generally placed on non-accrual status and reviewed for charge-off when principal and interest payments are four months in arrears unless the obligations are well-secured and in the process of collection. Interest thereafter on such charged-off consumer loans is taken into income when received only after full recovery of principal. As a general rule, a non-accrual asset may be restored to accrual status when none of its principal or interest is due and unpaid, satisfactory payments have been received for a sustained period (usually six months), or when it otherwise becomes well-secured and in the process of collection.

The following schedule sets forth certain information regarding Lakeland s non-accrual (including troubled debt restructurings that are on non-accrual) and past due loans and leases and other real estate owned and other repossessed assets as of December 31, for each of the last five years:

	At December 31,				
(dollars in thousands)	**2012**	**2011**	**2010**	**2009**	**2008**
Commercial, secured by real estate	**$ 10,511**	$ 16,578	$ 12,905	$ 20,811	$ 2,642
Commercial, industrial, and other	**1,476**	4,608	1,702	2,047	839
Leases, including leases held for sale	**32**	575	6,277	3,511	8,463
Real estate residential mortgage	**8,733**	11,610	12,834	5,465	1,475
Real estate-construction	**4,031**	12,393	6,321	4,987	2,392
Home equity and consumer	**3,197**	3,252	2,930	1,890	733
Total non-accrual loans and leases	**27,980**	49,016	42,969	38,711	16,544
Other real estate and other repossessed assets	**529**	1,182	1,592	1,864	3,997
TOTAL NON-PERFORMING ASSETS	**$ 28,509**	$ 50,198	$ 44,561	$ 40,575	$ 20,541
Non-performing assets as a percent of total assets	**0.98%**	1.78%	1.60%	1.49%	0.78%
Loans and leases past due 90 days or more and still accruing	**$ 1,437**	$ 1,367	$ 1,218	$ 1,437	$ 825
Troubled debt restructurings, still accruing	**$ 7,336**	$ 8,856	$ 9,073	$ 3,432	$

Non-accrual loans and leases decreased to $28.0 million on December 31, 2012 from $49.0 million at December 31, 2011. Non-performing assets decreased in all categories. Commercial secured by real estate; commercial, industrial and other; construction real estate and residential mortgages decreased $6.1 million, $3.1 million, $8.4 million and $2.9 million, respectively.

Commercial loan non-accruals included 5 loan relationships between $500,000 and $1.0 million totaling $3.4 million, and 5 loan relationships exceeding $1.0 million totaling $6.6 million. The largest of the commercial loan non-accruals was $2.1 million. All non-accrual loans and leases are in various stages of litigation, foreclosure, or workout. Non-accrual loans included $3.4 million and $4.6 million in troubled debt restructurings for the years ended December 31, 2012 and 2011, respectively.

At December 31, 2012, Lakeland had $7.3 million in loans that were restructured and still accruing. Restructured loans are those loans where Lakeland has granted concessions to the borrower in payment terms in rate and/or in maturity as a result of the financial condition of the borrower.

For 2012, the gross interest income that would have been recorded, had the loans and leases classified at year-end as non-accrual been performing in conformance with their original terms, is approximately $2.8 million. The amount of interest income actually recorded on those loans and leases for 2012 was $724,000. The resultant loss of $2.1 million for 2012 compares with prior year losses of $2.4 million for 2011 and $1.8 million for 2010.

As of December 31, 2012, Lakeland had impaired loans and leases totaling $31.5 million (consisting primarily of non-accrual and restructured loans and leases), compared to $43.1 million at December 31, 2011. The valuation allowance of these loans and leases is based primarily on the fair value of the underlying collateral. Based upon such evaluation, $873,000 has been allocated to the allowance for loan and lease losses for impairment at December 31, 2012 compared to $805,000 at December 31, 2011. At December 31, 2012, Lakeland also had $42.7 million in loans and leases that were rated substandard that were not classified as non-performing or impaired compared to $41.7 million at December 31, 2011.

There were no additional loans or leases at December 31, 2012, other than those designated non-performing, impaired or substandard, where the Company was aware of any credit conditions of any borrowers that would indicate a strong possibility of the borrowers not complying with the present terms and conditions of repayment and which may result in such loans or leases being included as non-accrual, past due or renegotiated at a future date.

The following table sets forth for each of the five years ended December 31, 2012, the historical relationships among the amount of loans and leases outstanding, the allowance for loan and lease losses, the provision for loan and lease losses, the amount of loans and leases charged off and the amount of loan and lease recoveries:

			December 31,		
	2012	**2011**	**2010**	**2009**	**2008**
			(dollars in thousands)		
Balance of the allowance at the beginning of the year	**$ 28,416**	$ 27,331	$ 25,563	$ 25,053	$ 14,689
Loans and leases charged off:					
Commercial, secured by real estate	**7,287**	5,352	7,510	2,524	95
Commercial, industrial and other	**949**	5,249	3,298	2,632	379
Leases	**999**	2,858	4,307	22,972	11,211
Leases held for sale				22,122	
Real estate residential mortgage	**1,822**	1,772	397	433	123
Real estate-construction	**2,888**	3,636	1,756	200	119
Home equity and consumer	**2,074**	3,010	2,250	2,499	2,044
Total loans and leases charged off	**16,019**	21,877	19,518	53,382	13,971
Recoveries:					
Commercial, secured by real estate	**280**	2,084	134	135	24
Commercial, industrial and other	**428**	439	62	134	17
Leases	**504**	1,206	1,391	1,777	150
Real estate residential mortgage	**66**	32	7		
Real estate-construction	**43**	67			38
Home equity and consumer	**306**	318	411	231	376
Total Recoveries	**1,627**	4,146	2,005	2,277	605
Net charge-offs:	**14,392**	17,731	17,513	51,105	13,366
Provision for loan and lease losses charged to operations	**14,907**	18,816	19,281	51,615	23,730
Ending balance	**$ 28,931**	$ 28,416	$ 27,331	$ 25,563	$ 25,053

Ratio of net charge-offs to average loans and leases outstanding: