

TF FINANCIAL CORP  
Form 10-Q  
August 14, 2008  
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## SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

### FORM 10-Q

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR  
15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

**For the period ended June 30, 2008**

- or -

**TRANSITION REPORT PURSUANT TO SECTION 13 OR  
15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

**For the transition period from**

**to**

**Commission file number: 0-24168**

## TF FINANCIAL CORPORATION

(Exact Name of Registrant as Specified in Its Charter)

**Delaware**

(State or Other Jurisdiction of Incorporation  
or Organization)

**74-2705050**

(I.R.S. Employer Identification No.)

**3 Penns Trail, Newtown, Pennsylvania**

(Address of Principal Executive Offices)

**18940**

(Zip Code)

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Registrant's telephone number, including area code: **(215) 579-4000**

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  NO

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

Large accelerated filer

Accelerated filer

Non-accelerated filer   
(Do not check if a smaller reporting company)

Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 Exchange Act). YES  NO

Indicate the number of shares outstanding of each of the issuer's classes of common stock as of the latest practicable date:  
**August 8, 2008**

| Class                        | Outstanding      |
|------------------------------|------------------|
| \$.10 par value common stock | 2,802,035 shares |

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32. Certification pursuant of Section 906 of the Sarbanes-Oxley Act of 2002

Table of Contents**TF Financial Corporation and Subsidiaries****CONSOLIDATED BALANCE SHEETS**

|   | Unaudited<br>June 30,<br>2008 | Audited<br>December 31,<br>2007 |
|---|-------------------------------|---------------------------------|
|   | (in thousands)                |                                 |
| <b>ASSETS</b>   |                               |                                 |
| Cash and cash equivalents   | \$ 4,327                      | \$ 5,680                        |
| Investment securities available for sale at fair value  | 31,010                        | 32,363                          |
| Investment securities held to maturity (fair value of \$245 and \$246, respectively)  | 245                           | 244                             |
| Mortgage-backed securities available for sale at fair value   | 87,336                        | 98,178                          |
| Mortgage-backed securities held to maturity (fair value of \$5,408 and \$6,343, respectively)   | 5,271                         | 6,160                           |
| Loans receivable, net   | 549,159                       | 517,027                         |
| Loans receivable held for sale  | 360                           | 1,040                           |
| Federal Home Loan Bank stock at cost  | 9,292                         | 8,782                           |
| Accrued interest receivable   | 2,941                         | 3,036                           |
| Premises and equipment, net   | 5,884                         | 6,267                           |
| Goodwill  | 4,324                         | 4,324                           |
| Bank-owned life insurance   | 16,196                        | 15,881                          |
| Other assets  | 3,242                         | 2,691                           |
| <b>TOTAL ASSETS</b>   | <b>\$ 719,587</b>             | <b>701,673</b>                  |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>   |                               |                                 |
| <b>Liabilities</b>  |                               |                                 |
| Deposits  | \$ 486,994                    | \$ 472,394                      |
| Borrowings from the Federal Home Loan Bank  | 154,703                       | 153,221                         |
| Advances from borrowers for taxes and insurance   | 2,549                         | 2,193                           |
| Accrued interest payable  | 3,641                         | 3,415                           |
| Other liabilities   | 2,639                         | 2,607                           |
| <b>Total liabilities</b>  | <b>650,526</b>                | <b>633,830</b>                  |
| <b>Stockholders' equity</b>   |                               |                                 |
| Preferred stock, no par value; 2,000,000 shares authorized at June 30, 2008 and December 31, 2007, none issued  |                               |                                 |
| Common stock, \$0.10 par value; 10,000,000 shares authorized, 5,290,000 shares issued, 2,648,576 and 2,671,083 shares outstanding at June 30, 2008 and December 31, 2007, respectively, net of shares in treasury 2,487,965 and 2,459,440, respectively | 529                           | 529                             |
| Additional paid-in capital  | 53,782                        | 53,337                          |
| Unearned ESOP shares  | (1,534)                       | (1,595)                         |
| Treasury stock-at cost  | (51,890)                      | (51,216)                        |
| Retained earnings   | 69,135                        | 67,735                          |
| Accumulated other comprehensive loss  | (961)                         | (947)                           |
| <b>Total stockholders' equity</b>   | <b>69,061</b>                 | <b>67,843</b>                   |
| <b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>   | <b>\$ 719,587</b>             | <b>\$ 701,673</b>               |

The accompanying notes are an integral part of these statements



Table of Contents**TF Financial Corporation and Subsidiaries****CONSOLIDATED STATEMENTS OF INCOME****(Unaudited)**

|  | For the three months<br>ended<br>June 30, |              | For the six months<br>ended<br>June 30, |               |
|--|---|--------------|---|---------------|
|  | 2008                                      | 2007         | 2008                                    | 2007          |
|  | (in thousands, except per share data)     |              |   |               |
| Interest income  |   |              |   |               |
| Loans, including fees  | \$ 8,155                                  | \$ 7,986     | \$ 16,338                               | \$ 15,765     |
| Mortgage-backed securities                                     | 1,132                                     | 1,006        | 2,363                                   | 1,939         |
| Investment securities  | 365                                       | 404          | 778                                     | 838           |
| Interest-bearing deposits and other                            | 4   | 19           | 10                                      | 86            |
| <b>TOTAL INTEREST INCOME</b>                                   | <b>9,656</b>                              | <b>9,415</b> | <b>19,489</b>                           | <b>18,628</b> |
| Interest expense   |   |              |   |               |
| Deposits   | 2,926                                     | 3,416        | 6,212                                   | 6,646         |
| Borrowings   | 1,571                                     | 1,056        | 3,203                                   | 2,035         |
| <b>TOTAL INTEREST EXPENSE</b>                                  | <b>4,497</b>                              | <b>4,472</b> | <b>9,415</b>                            | <b>8,681</b>  |
| <b>NET INTEREST INCOME</b>                                     | <b>5,159</b>                              | <b>4,943</b> | <b>10,074</b>                           | <b>9,947</b>  |
| Provision for loan losses                                      | 340                                       |              | 340                                     |               |
| <b>NET INTEREST INCOME AFTER PROVISION FOR<br/>LOAN LOSSES</b> | <b>4,819</b>                              | <b>4,943</b> | <b>9,734</b>                            | <b>9,947</b>  |
| Non-interest income  |   |              |   |               |
| Service fees, charges and other operating income               | 543                                       | 514          | 1,236                                   | 1,061         |
| Bank-owned life insurance                                      | 156                                       | 153          | 315                                     | 301           |
| Gain on sale of loans  | 97  | 63           | 159                                     | 117           |
| Gain on sale of foreclosed real estate                         | 342                                       |              | 342                                     |               |
| Other income   |   |              | 197                                     | 777           |
| <b>TOTAL NON-INTEREST INCOME</b>                               | <b>1,138</b>                              | <b>730</b>   | <b>2,249</b>                            | <b>2,256</b>  |
| Non-interest expense   |   |              |   |               |
| Compensation and benefits                                      | 2,677                                     | 2,680        | 5,215                                   | 5,348         |
| Occupancy and equipment  | 740                                       | 712          | 1,468                                   | 1,404         |
| Professional fees  | 167                                       | 133          | 421                                     | 357           |
| Marketing and advertising                                      | 145                                       | 163          | 289                                     | 326           |
| Other operating  | 603                                       | 580          | 1,201                                   | 1,423         |
| <b>TOTAL NON-INTEREST EXPENSE</b>                              | <b>4,332</b>                              | <b>4,268</b> | <b>8,594</b>                            | <b>8,858</b>  |
| <b>INCOME BEFORE INCOME TAXES</b>                              | <b>1,625</b>                              | <b>1,405</b> | <b>3,389</b>                            | <b>3,345</b>  |

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|                            |          |          |          |          |
|----------------------------|----------|----------|----------|----------|
| Income taxes               | 441      | 368      | 924      | 910      |
| NET INCOME                 | \$ 1,184 | \$ 1,037 | \$ 2,465 | \$ 2,435 |
| Earnings per share basic   | \$ 0.45  | \$ 0.38  | \$ 0.92  | \$ 0.89  |
| Earnings per share diluted | \$ 0.44  | \$ 0.38  | \$ 0.92  | \$ 0.89  |
| Dividends paid per share   | \$ 0.20  | \$ 0.20  | \$ 0.40  | \$ 0.40  |

The accompanying notes are an integral part of these statements

Table of Contents**TF Financial Corporation and Subsidiaries****CONSOLIDATED STATEMENTS OF CASH FLOWS****(Unaudited)**

|  | <b>For the six months<br/>ended<br/>June 30,</b> |              |
|--|--|--------------|
|  | <b>2008</b>                                      | <b>2007</b>  |
|  | <b>(in thousands)</b>                            |              |
| <b>OPERATING ACTIVITIES</b>  |  |              |
| Net income   | \$ 2,465   | \$ 2,435     |
| Adjustments to reconcile net income to net cash provided by operating activities |  |              |
| Amortization (accretion) of:   |  |              |
| Mortgage loan servicing rights   | 79   | 23           |
| Deferred loan origination fees   | 19   | (53)         |
| Premiums and discounts on investment securities, net                             | 44   | 46           |
| Premiums and discounts on mortgage-backed securities, net                        | (96)   | 45           |
| Premiums and discounts on loans, net   | 42   | 67           |
| Discount on wholesale deposits   |  | 12           |
| Provision for loan losses  | 340  |              |
| Depreciation of premises and equipment   | 484  | 442          |
| Increase in value of bank-owned life insurance                                   | (315)  | (301)        |
| Stock grant expense  | 180  | 180          |
| Stock option expense   | 186  | 195          |
| Stock-based benefit programs: ESOP   | 141  | 168          |
| Proceeds from sale of loans originated for sale                                  | 10,968   | 10,523       |
| Origination of loans held for sale   | (10,269)   | (10,370)     |
| Gain on sale of  |  |              |
| Mortgage loans available for sale  | (159)  | (117)        |
| Real estate acquired through foreclosure   | (342)  |              |
| Expense from mortgage loan derivatives   | 6  | (9)          |
| Income associated with forward loan sales  | (1)  | 1            |
| (Increase) decrease in   |  |              |
| Accrued interest receivable  | 95   | 92           |
| Other assets   | (117)  | (1,284)      |
| Increase (decrease) in   |  |              |
| Accrued interest payable   | 226  | 145          |
| Other liabilities  | 32   | (44)         |
| <b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>                                 | <b>4,008</b>                                     | <b>2,196</b> |
| <b>INVESTING ACTIVITIES</b>  |  |              |
| Loan originations  | (88,249)   | (74,639)     |
| Loan principal payments  | 54,471   | 58,950       |
| Principal repayments on mortgage-backed securities held to maturity              | 887  | 964          |
| Principal repayments on mortgage-backed securities available for sale            | 11,171   | 5,310        |
| Purchase of investment securities available for sale                             |  | (771)        |
| Purchase of mortgage-backed securities available for sale                        |  | (13,798)     |
| Proceeds from maturities of investment securities held to maturity               |  | 6,455        |
| Proceeds from maturities of investment available for sale                        | 1,000  |              |
| (Purchase)/redemption of Federal Home Loan Bank stock, net                       | (510)  | 255          |



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|  |          |          |
|--|----------|----------|
| Proceeds from the sale of real estate acquired through foreclosure     | 1,272    |          |
| Purchase of premises and equipment                                     | (101)    | (379)    |
| Maturities of certificates of deposits in other financial institutions |          | 40       |
| NET CASH USED IN INVESTING ACTIVITIES                                  | (20,059) | (17,613) |

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|  | For the six months ended |                |
|--|--------------------------|----------------|
|  | June 30,                 |                |
|  | 2008                     | 2007           |
|  | (in thousands)           |                |
| <b>FINANCING ACTIVITIES</b>  |                          |                |
| Net increase in customer deposits  | 14,600                   | 11,479         |
| Net (decrease) increase in short-term borrowings from the Federal Home Loan Bank | (3,090)                  | 8,366          |
| Proceeds of long-term Federal Home Loan Bank borrowings                          | 14,309                   |                |
| Repayment of long-term Federal Home Loan Bank borrowings                         | (9,737)                  | (9,957)        |
| Net increase in advances from borrowers for taxes and insurance                  | 356                      | 868            |
| Treasury stock acquired  | (683)                    | (2,909)        |
| Exercise of stock options  | 8                        | 1,771          |
| Tax benefit arising from stock compensation                                      |                          | 363            |
| Common stock dividends paid  | (1,065)                  | (1,102)        |
| <b>NET CASH PROVIDED BY FINANCING ACTIVITIES</b>                                 | <b>14,698</b>            | <b>8,879</b>   |
| <b>NET DECREASE IN CASH AND CASH EQUIVALENTS</b>                                 | <b>(1,353)</b>           | <b>(6,538)</b> |
| Cash and cash equivalents at beginning of period                                 | 5,680                    | 12,364         |
| Cash and cash equivalents at end of period                                       | \$ 4,327                 | \$ 5,826       |
| <b>Supplemental disclosure of cash flow information</b>                          |                          |                |
| Cash paid for  |                          |                |
| Interest on deposits and borrowings from Federal Home Loan Bank                  | \$ 9,189                 | \$ 8,536       |
| Income taxes   | \$ 342                   | \$ 180         |
| Non-cash transactions  |                          |                |
| Capitalization of mortgage servicing rights                                      | \$ 140                   | \$ 150         |
| Transfers from loans to real estate acquired through foreclosure                 | \$ 1,236                 | \$             |

The accompanying notes are an integral part of these statements

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**TF FINANCIAL CORPORATION AND SUBSIDIARIES  
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 - PRINCIPLES OF CONSOLIDATION**

The consolidated financial statements as of June 30, 2008 (unaudited) and December 31, 2007 and for the three and six-month periods ended June 30, 2008 and 2007 (unaudited) include the accounts of TF Financial Corporation (the Company) and its wholly owned subsidiaries Third Federal Bank (the Bank), TF Investments Corporation and Penns Trail Development Corporation. The Company's business is conducted principally through the Bank. All significant intercompany accounts and transactions have been eliminated in consolidation.

**NOTE 2 - BASIS OF PRESENTATION**

The accompanying unaudited consolidated financial statements were prepared in accordance with instructions for Form 10-Q and, therefore, do not include all of the disclosures or footnotes required by accounting principles generally accepted in the United States of America (GAAP). In the opinion of management, all adjustments, consisting of normal recurring accruals, necessary for fair presentation of the consolidated financial statements have been included. The results of operations for the period ended June 30, 2008 are not necessarily indicative of the results which may be expected for the entire fiscal year or any other period. For further information, refer to consolidated financial statements and footnotes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2007.

**NOTE 3 - CONTINGENCIES**

The Company, from time to time, is a party to routine litigation that arises in the normal course of business. In the opinion of management, the resolution of this litigation, if any, would not have a material adverse effect on the Company's consolidated financial position or results of operations.

**NOTE 4 - OTHER COMPREHENSIVE INCOME**

The Company follows Statement of Financial Accounting Standard (SFAS) No. 130, Reporting Comprehensive Income. SFAS No. 130 establishes standards to provide prominent disclosure of comprehensive income items. Comprehensive income is the change in equity of a business enterprise during a period from transactions and other events and circumstances from non-owner sources. The components of other comprehensive loss are as follows for the three months ended:

|                              | <b>June 30, 2008</b>     |                              |
|------------------------------|--------------------------|------------------------------|
| <b>Before tax<br/>amount</b> | <b>Tax<br/>(expense)</b> | <b>Net of tax<br/>amount</b> |

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|   | <b>benefit<br/>(in thousands)</b> |               |                   |
|---|-----------------------------------|---------------|-------------------|
| <b>Unrealized losses on securities</b>  |                                   |               |                   |
| Unrealized holding losses arising during period                                     | \$ (1,768)                        | \$ 603        | \$ (1,165)        |
| Pension plan benefit adjustment related to prior service costs and actuarial losses | 34                                | (12)          | 22                |
| <b>Other comprehensive loss, net</b>  | <b>\$ (1,734)</b>                 | <b>\$ 591</b> | <b>\$ (1,143)</b> |

|   | <b>Before tax<br/>amount</b> | <b>June 30, 2007<br/>Tax<br/>(expense)<br/>benefit<br/>(in thousands)</b> | <b>Net of tax<br/>amount</b> |
|---|------------------------------|---|------------------------------|
| <b>Unrealized losses on securities</b>  |                              |   |                              |
| Unrealized holding losses arising during period                                     | \$ (1,122)                   | \$ 381  | \$ (741)                     |
| Pension plan benefit adjustment related to prior service costs and actuarial losses | 55                           | (19)  | 36                           |
| <b>Other comprehensive loss, net</b>  | <b>\$ (1,067)</b>            | <b>\$ 362</b>   | <b>\$ (705)</b>              |

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The components of other comprehensive loss are as follows for the six months ended:

|   | Before tax<br>amount | June 30, 2008<br>Tax<br>(expense)<br>benefit<br>(in thousands) | Net of tax<br>amount |
|---|----------------------|--|----------------------|
| Unrealized losses on securities   |                      |  |                      |
| Unrealized holding losses arising during period                                     | \$ (77)              | \$ 26  | \$ (51)              |
| Pension plan benefit adjustment related to prior service costs and actuarial losses | 55                   | (18)   | 37                   |
| Other comprehensive loss, net   | \$ (22)              | \$ 8   | \$ (14)              |

|   | Before tax<br>amount | June 30, 2007<br>Tax<br>(expense)<br>benefit<br>(in thousands) | Net of tax<br>amount |
|---|----------------------|--|----------------------|
| Unrealized losses on securities   |                      |  |                      |
| Unrealized holding losses arising during period                                     | \$ (872)             | \$ 295   | \$ (577)             |
| Pension plan benefit adjustment related to prior service costs and actuarial losses | 55                   | (19)   | 36                   |
| Other comprehensive loss, net   | \$ (817)             | \$ 276   | \$ (541)             |

**NOTE 5 - EARNINGS PER SHARE**

The following tables illustrate the reconciliation of the numerators and denominators of the basic and diluted earnings per share computations (dollars in thousands, except per share data):

|  | Three months ended June 30, 2008 |  |                     |
|--|----------------------------------|--|---------------------|
|  | Income<br>(numerator)            | Weighted<br>average<br>shares<br>(denominator) | Per share<br>Amount |
| Basic earnings per share   |                                  |  |                     |
| Income available to common stockholders                                    | \$ 1,184                         | 2,660,757                                      | \$ 0.45             |
| Effect of dilutive securities  |                                  |  |                     |
| Stock options and grants   |                                  | 10,011   | (0.01)              |
| Diluted earnings per share   |                                  |  |                     |
| Income available to common stockholders plus effect of dilutive securities | \$ 1,184                         | 2,670,768                                      | \$ 0.44             |

Six months ended June 30, 2008

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|  | Income<br>(numerator) | Weighted<br>average<br>shares<br>(denominator) | Per share<br>Amount |
|--|-----------------------|--|---------------------|
| Basic earnings per share   |                       |  |                     |
| Income available to common stockholders                                    | \$ 2,465              | 2,665,544                                      | \$ 0.92             |
| Effect of dilutive securities  |                       |  |                     |
| Stock options and grants   |                       | 5,477  |                     |
| Diluted earnings per share   |                       |  |                     |
| Income available to common stockholders plus effect of dilutive securities | \$ 2,465              | 2,671,021                                      | \$ 0.92             |

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There were 204,773 options to purchase shares of common stock at an average price range of \$24.71 to \$34.14 per share which were outstanding for the three months and six months ended June 30, 2008 that were not included in the computation of diluted earnings per share because the options' exercise prices were greater than the average market price of the common shares.

|  | <b>Three months ended June 30, 2007</b> |  |                             |
|--|---|--|-----------------------------|
|  | <b>Income<br/>(numerator)</b>           | <b>Weighted<br/>average<br/>shares<br/>(denominator)</b> | <b>Per share<br/>Amount</b> |
| <b>Basic earnings per share</b>  |   |  |                             |
| Income available to common stockholders                                    | \$ 1,037                                | 2,743,959  | \$ 0.38                     |
| <b>Effect of dilutive securities</b>                                       |   |  |                             |
| Stock options and grants   |   | 4,610  |                             |
| <b>Diluted earnings per share</b>  |   |  |                             |
| Income available to common stockholders plus effect of dilutive securities | \$ 1,037                                | 2,748,569  | \$ 0.38                     |

|  | <b>Six months ended June 30, 2007</b> |  |                             |
|--|---------------------------------------|--|-----------------------------|
|  | <b>Income<br/>(numerator)</b>         | <b>Weighted<br/>average<br/>shares<br/>(denominator)</b> | <b>Per share<br/>Amount</b> |
| <b>Basic earnings per share</b>  |                                       |  |                             |
| Income available to common stockholders                                    | \$ 2,435                              | 2,747,498  | \$ 0.89                     |
| <b>Effect of dilutive securities</b>                                       |                                       |  |                             |
| Stock options and grants   |                                       | 2,344  |                             |
| <b>Diluted earnings per share</b>  |                                       |  |                             |
| Income available to common stockholders plus effect of dilutive securities | \$ 2,435                              | 2,749,842  | \$ 0.89                     |

There were 20,128 options to purchase shares of common stock at a price of \$34.14 per share which were outstanding for the three months and six months ended June 30, 2007 that were not included in the computation of diluted earnings per share because the options' exercise prices were greater than the average market price of the common shares.

**NOTE 6 - FAIR VALUE MEASUREMENTS**

On January 1, 2008, the Company adopted Financial Accounting Standards Board (FASB) Statement No. 157 (SFAS 157), Fair Value Measurements. SFAS 157 defines fair value, establishes a framework for measuring fair value and expands the related disclosure requirements. SFAS 157 clarifies that fair value is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. SFAS 157 establishes a fair value measurement hierarchy for inputs in valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (level 1 measurements) and the lowest priority to unobservable inputs (level 3 measurements).

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The fair value hierarchy levels are summarized below:

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2 inputs are inputs that are observable for the asset or liability, either directly or indirectly.
- Level 3 inputs are unobservable and contain assumptions of the party fair valuing the asset or liability.

Determination of the appropriate level within the fair value hierarchy is based on the lowest level of input that is



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significant to the fair value measurement for the instrument or security. Assets and liabilities measured at fair value on a recurring basis segregated by value hierarchy level are summarized below (dollars in thousands):

|   | Quoted<br>Prices in<br>Active<br>Markets<br>for<br>Identical<br>Assets<br>(Level 1) | Significant<br>Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) | Balance as of<br>June 30,<br>2008 |
|---|---|---|--|-----------------------------------|
| <b>Assets</b>                                 |   |   |  |                                   |
| Investment securities available for sale      | \$ 154  | \$ 30,856   | \$   | \$ 31,010                         |
| Mortgage-backed securities available for sale |   | 87,336  |  | 87,336                            |
| Impaired loans                                |   |   | 2,076  | 2,076                             |
| Derivative loan commitments                   |   |   | 3  | 3                                 |
| <b>Liabilities</b>                            |   |   |  |                                   |
| Forward loan sales                            |   |   | 4  | 4                                 |
| Derivative loan commitments                   |   |   | 6  | 6                                 |

Investment securities available for sale and mortgage-backed securities available for sale are valued primarily by a third party pricing agent. Active listed equities are generally classified within Level 1 of the fair value hierarchy. Government-sponsored agency debt securities and corporate bonds are primarily priced through a multi-dimensional relational model, a level 2 hierarchy, which incorporates dealer quotes and other market information including, defined sector breakdown, benchmark yields, base spread, yield to maturity, and corporate actions. Municipal securities are also measured within the level 2 hierarchy using inputs with a series of matrices that reflect benchmark yields, ratings updates, and spread adjustments. Mortgage-backed securities include FNMA and FHLMC certificates and real estate mortgage investment conduits which are valued under a level 2 hierarchy using a matrix correlation to benchmark yields, spread analysis, and prepayment speeds.

Impaired loans are evaluated and valued at the time the loan is identified as impaired, at the lower of the recorded investment in the loan or market value. The loans identified as impaired are real estate secured. Market value is determined by using the value of the collateral securing the loans and is therefore classified as a level 3 hierarchy. The value of the real estate is determined by qualified independent licensed appraisers contracted by the Company to perform the assessment. The appraised value is then discounted based upon management's experience, which includes estimated disposal costs, understanding of the customer and the customer's business as well as economic conditions. Impaired loans are reviewed and evaluated on a quarterly basis for additional impairment and adjusted accordingly, based upon the pertinent conditions.

The fair value of derivative loan commitments and forward loan sales are determined at the time the underlying loan is identified as held for sale with changes in fair value correlated to the change in secondary market loan pricing. The value is adjusted to reflect the Company's historical loan fallout experience which incorporates such factors as changes in market rates, origination channels and loan purpose.

The Company also measures certain other financial assets at fair value on a non-recurring basis in accordance with GAAP. Adjustments may result from application of lower-of-cost or fair value accounting.

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The following table presents additional information about assets measured at fair value on a recurring basis for which the Company has utilized Level 3 inputs to determine fair value (in thousands):

|   | <b>Derivative loan commitments</b> |   |
|---|------------------------------------|---|
| Beginning balance December 31, 2007       | \$                                 | 3 |
| Total gains/(losses) realized/unrealized: |                                    |   |
| Included in earnings                      |                                    |   |
| Included in other comprehensive income    |                                    |   |
| Purchases, issuances, and settlements     |                                    |   |
| Ending balance June 30, 2008              | \$                                 | 3 |

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The following table presents additional information about liabilities measured at fair value on a recurring basis for which the Company has utilized Level 3 inputs to determine fair value (in thousands):

|  | Forward loan sales |   | Derivative loan commitments |   |
|--|--------------------|---|-----------------------------|---|
| Beginning balance December 31, 2007        | \$                 | 3 | \$                          |   |
| Total losses/ (gains) realized/unrealized: |                    |   |                             |   |
| Included in earnings                       |                    | 1 |                             | 6 |
| Included in other comprehensive income     |                    |   |                             |   |
| Purchases, issuances, and settlements      |                    |   |                             |   |
| Ending balance June 30, 2008               | \$                 | 4 | \$                          | 6 |

**NOTE 7 - STOCK BASED COMPENSATION**

The Company has stock benefit plans that allow the Company to grant options and stock to employees and directors. The awards, which have a term of up to 10 years when issued, vest over a three to five year period. The exercise price of each award equals the market price of the Company's stock on the date of the grant. At June 30 2008, there was \$232,000 of total unrecognized compensation cost, net of estimated forfeitures, related to non-vested awards under the Plan. That cost is expected to be recognized over a weighted average period of 8.8 months.

Stock-based compensation expense included in net income related to stock options was \$92,000 and \$96,000 for the quarters ended June 30, 2008 and 2007 respectively, resulting in a tax benefit of \$28,000 and \$30,000, respectively. Stock-based compensation expense included in net income related to stock options was \$186,000 and \$195,000 for the six months ended June 30, 2008 and 2007 respectively, resulting in a tax benefit of \$58,000 and \$60,000, respectively.

Option activity under the Company's stock option plan as of June 30, 2008 is as follows:

|                                      | Number of shares | Weighted average exercise price per share | 2008 Weighted average remaining contractual term (in years) | Aggregate intrinsic value (\$ 000) |
|--------------------------------------|------------------|---|---|------------------------------------|
| Outstanding at January 1, 2008       | 252,576          | \$ 26.56                                  |   |                                    |
| Options granted                      |                  |   |   |                                    |
| Options exercised                    | (425)            | 17.56                                     |   |                                    |
| Options forfeited                    | (5,610)          | 28.27                                     |   |                                    |
| Options expired                      |                  |   |   |                                    |
| Outstanding at June 30, 2008         | 246,541          | \$ 26.54                                  | 3.16  | \$ 296                             |
| Options exercisable at June 30, 2008 | 179,113          | \$ 25.76                                  | 3.08  | \$ 296                             |

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The aggregate intrinsic value in the table above represents the total pre-tax intrinsic value (the difference between the Company's closing stock price on the last trading day of the second quarter and the exercise price, multiplied by the number of in-the money options).

The aggregate intrinsic value of options exercised during the six months ended June 30, 2008 and 2007 was \$2,100 and \$1,085,000, respectively. Exercise of stock options during the six months ended June 30, 2008 and 2007 resulted in cash receipts of \$8,000 and \$1,770,000, respectively.

Stock-based compensation expense included in net income related to stock grants was \$90,000 for each of the quarters ended June 30, 2008 and 2007. Stock-based compensation expense included in net income related to the Company's employee stock ownership plan totaled \$54,000 and \$77,000 for the quarters ended June 30, 2008 and 2007, respectively. Stock-based compensation expense included in net income related to stock grants was \$180,000 for each of the six month periods ended June 30, 2008 and 2007. Stock-based compensation expense included in net income related to the Company's employee stock ownership plan totaled \$109,000 and \$137,000 for the six month periods ended June 30, 2008 and 2007, respectively.

Table of Contents**NOTE 8 - EMPLOYEE BENEFIT PLANS**

Net periodic defined benefit pension cost included the following (in thousands):

|  | <b>Three months ended</b> |             |
|--|---------------------------|-------------|
|  | <b>June 30,</b>           |             |
|  | <b>2008</b>               | <b>2007</b> |
| <b>Components of net periodic benefit cost</b> |                           |             |
| Service cost                                   | \$ 98                     | \$ 84       |
| Interest cost                                  | 62                        | 53          |
| Expected return on plan assets                 | (105)                     | (100)       |
| Amortization of prior service cost             | 8                         | 16          |
| Recognized net actuarial loss                  | 26                        | 13          |
| Net periodic benefit cost                      | \$ 89                     | \$ 66       |

|  | <b>Six months ended</b> |             |
|--|-------------------------|-------------|
|  | <b>June 30,</b>         |             |
|  | <b>2008</b>             | <b>2007</b> |
| <b>Components of net periodic benefit cost</b> |                         |             |
| Service cost                                   | \$ 196                  | \$ 168      |
| Interest cost                                  | 123                     | 106         |
| Expected return on plan assets                 | (210)                   | (200)       |
| Amortization of prior service cost             | 15                      | 30          |
| Recognized net actuarial loss                  | 40                      | 25          |
| Net periodic benefit cost                      | \$ 164                  | \$ 129      |

The employer contribution made for the six months ended June 30, 2008 and 2007 was \$218,000 and \$1,107,000, respectively.

**NOTE 9 - NEW ACCOUNTING PRONOUNCEMENTS**

In February 2008, FASB issued FASB Staff Position (FSP) FAS 140-3, *Accounting for Transfers of Financial Assets and Repurchase Financing Transactions*, which provides guidance on accounting for a transfer of a financial asset and a repurchase financing. The FSP presumes that an initial transfer of a financial asset and a repurchase financing are considered part of the same arrangement under FASB Statement No. 140 *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*. However, if certain criteria are met, the initial transfer and repurchase shall not be evaluated as a linked transaction and therefore evaluated separately under FASB 140. The FSP is effective for repurchase financing in which the initial transfer is entered in fiscal years beginning after November 15, 2008. The Company does not anticipate a material impact on its consolidated financial statements as a result of this statement.

In February 2008, FASB issued FASB Staff Position (FSP) FAS 157-2 which provides a one-year deferral of the effective date for SFAS 157 with respect to all nonfinancial assets and liabilities, except those items recognized or disclosed in the financial statements on a recurring basis (that is at least annually). The FSP is effective upon issuance.

In March 2008, FASB Issued Statement No. 161 (SFAS 161), Disclosures About Derivative Instruments and Hedging Activities an amendment of FASB Statement 133 . The statement requires expanded disclosures about an entity s derivative instruments and hedging activities but does not change SFAS 133 s scope or accounting. This statement is effective for fiscal years and interim periods beginning after November 15, 2008 with early adoption permitted. The Company does not anticipate a material impact as a result of this statement on its consolidated financial statements.

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In April 2008, FASB issued Statement FSP 142-3 which amends the list of factors an entity should consider in developing renewal of extension assumptions used in determining the useful life of recognized intangible assets under Statement 142. The new guidance applies to intangible assets that are acquired individually or with a group of other assets and to intangible assets acquired in both business combinations and asset acquisitions. The FSP is effective for financial statements issued for fiscal years beginning after December 15, 2008 and interim periods within those fiscal years. The guidance must be applied prospectively only to intangible assets acquired after the FSP's effective date.

**NOTE 10 - RECLASSIFICATIONS**

Certain prior period amounts have been reclassified to conform to the current period presentation.

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**TF FINANCIAL CORPORATION AND SUBSIDIARIES**

**ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL POSITION AND RESULTS OF OPERATIONS**

**GENERAL**

The Company may from time to time make written or oral forward-looking statements, including statements contained in the Company's filings with the Securities and Exchange Commission (including this Quarterly Report on Form 10-Q and the exhibits thereto), in its reports to stockholders and in other communications by the Company, which are made in good faith by the Company pursuant to the Safe Harbor Provisions of the Private Securities Litigation Reform Act of 1995.

These forward-looking statements involve risks and uncertainties, such as statements of the Company's plans, objectives, expectations, estimates and intentions that are subject to change based on various important factors (some of which are beyond the Company's control). The following factors, among others, could cause the Company's financial performance to differ materially from the plans, objectives, expectations, estimates and intentions expressed in such forward-looking statements: the strength of the United States economy in general and the strength of the local economies in which the Company conducts operations; the effects of, and changes in, trade, monetary and fiscal policies and laws, including interest rate policies of the Board of Governors of the Federal Reserve System, inflation, interest rate, market and monetary fluctuations; the timely development of and acceptance of new products and services of the Company and the perceived overall value of these products and services by users, including the features, pricing and quality compared to competitors' products and services; the willingness of users to substitute competitors' products and services for the Company's products and services; the success of the Company in gaining regulatory approval of its products and services, when required; the impact of changes in financial services laws and regulations (including laws concerning taxes, banking, securities and insurance); technological changes, acquisitions; changes in consumer spending and saving habits; and the success of the Company at managing the risks involved in the foregoing.

The Company cautions that the foregoing list of important factors is not exclusive. The Company does not undertake to update any forward-looking statement, whether written or oral, that may be made from time to time by or on behalf of the Company.

**Financial Position**

The Company's total assets at June 30, 2008 and December 31, 2007 were \$719.6 million and \$701.7 million, respectively, an increase of \$17.9 million, or 2.6% during the six-month period. Investment securities available for sale decreased \$1.4 million due to maturities of \$1.0 million, a decrease in the fair value of the securities of \$0.3 million, as well as net premium amortization of \$0.1 million. Mortgage-backed securities available for sale decreased by \$10.8 million due to principal repayments received of \$11.2 million offset by an increase in the fair value of the securities of \$0.3 million and net premium amortization of \$0.1 million. Mortgage-backed securities held to maturity decreased by \$0.9 million mainly as a result of principal repayments.



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Loans receivable increased by \$31.5 million during the first six months of 2008. Consumer and single-family residential mortgage loans of \$47.6 million and commercial loans of \$40.7 were originated during the six months of 2008. Principal repayments of loans receivable were \$54.5 million. The Company had \$80.7 million of prime-rate based loans at June 30, 2008. Loans originated for sale during the six months of 2008 totaled \$10.3 million, and there were \$11.0 million in proceeds from the sale of loans in the secondary market during this period.

Total liabilities increased by \$16.7 million during the first six months of 2008. Deposit balances grew by \$14.6 million during the first half of the year; the net result of a \$7.4 million increase in non-interest checking, interest-bearing checking and money market accounts offset by a \$5.1 million decrease in savings accounts. At June 30, 2008, the Bank had \$77.5 million of deposits indexed to the yield of the Merrill Lynch Ready Asset Money Market Fund. Retail certificates of deposit increased \$12.2 million during the first six months of 2008. Advances from the Federal Home Loan Bank increased by \$1.5 million in the first six months of 2008; the result of \$14.3 million in new long term advances less a \$3.1 million decrease in short-term borrowings, less scheduled amortization payments of \$9.7 million.

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Total consolidated stockholder's equity of the Company was \$69.1 million or 9.6 % of total assets at June 30, 2008. During the first six months of 2008, the Company repurchased 28,950 shares of its common stock and issued 425 shares pursuant to the exercise of stock options. At June 30, 2008, there were approximately 132,000 shares available for repurchase under the previously announced share repurchase plan.

During the quarter, the Company closed its branch office on Quakerbridge Road in Mercer County, New Jersey, and reassigned approximately \$9 million in deposits to its nearby offices in Ewing and Hamilton, New Jersey.

**Asset Quality**



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At the end of the first quarter of 2008, the Company completed foreclosure proceedings on two parcels of commercial real estate with a combined loan balance of \$1.5 million. These loans were non-performing at December 31, 2007. One parcel has been recorded as real estate owned totaling \$306,000 and was included in other assets in the consolidated balance sheet at June 30, 2008. As a result of this specific foreclosure, the Bank recorded a charge off in the amount of \$347,000. During the foreclosure proceedings of the second property, a bid from an unrelated party was made which satisfied the outstanding contractual obligations of the borrower with the Bank. This foreclosure and simultaneous sale resulted in a \$342,000 gain which is included in non-interest income of the Company during the second quarter of 2008. The Bank does not anticipate any further charges against the allowance as a result of the foregoing discussed foreclosures. During the first half of 2008 and 2007, the Company's provision for loan losses was \$340,000 and \$0, respectively. With respect to each of the remaining non-performing loans, all of which are real estate secured, the Bank is taking appropriate steps to resolve the individual situations.

The following table sets forth information regarding the Company's asset quality (dollars in thousands):

|  | June 30,<br>2008 | December 31,<br>2007 | June 30,<br>2007 |
|--|------------------|----------------------|------------------|
| Non-performing loans                                       | \$ 2,368         | \$ 5,358             | \$ 4,965         |
| Ratio of non-performing loans to gross loans               | 0.43%            | 1.03%                | 0.99%            |
| Ratio of non-performing loans to total assets              | 0.33%            | 0.76%                | 0.75%            |
| Ratio of total non-performing assets to total assets       | 0.37%            | 0.76%                | 0.75%            |
| Ratio of allowance for loan losses to total loans          | 0.52%            | 0.55%                | 0.57%            |
| Ratio of allowance for loan losses to non-performing loans | 120.1%           | 53.00%               | 57.40%           |

Management maintains an allowance for loan losses at levels that are believed to be adequate; however, there can be no assurances that further additions will not be necessary or that losses inherent in the existing loan portfolio will not exceed the allowance. The following table sets forth the activity in the allowance for loan losses during the periods indicated (in thousands):

|                                      | 2008     | 2007     |
|--------------------------------------|----------|----------|
| Beginning balance, January 1,        | \$ 2,842 | \$ 2,865 |
| Provision                            | 340      |          |
| Less: charge-off's (recoveries), net | 337      | 15       |
| Ending balance, June 30,             | 2,845    | 2,850    |

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**RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED JUNE 30, 2008 AND 2007**

**Net Income.** The Company recorded net income of \$1,184,000, or \$0.44 per diluted share, for the three months ended June 30, 2008 as compared to net income of \$1,037,000, or \$0.38 per diluted share, for the three months ended June 30, 2007.

**Average Balance Sheet**



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The following table sets forth information (dollars in thousands) relating to the Company's average balance sheet and reflects the average yield on assets and average cost of liabilities for the periods indicated. Yield and cost are computed by dividing income or expense by the average daily balance of interest-earning assets or interest-bearing liabilities, respectively, for the three-month periods indicated.

|  | 2008               |          | June 30,            |                    | 2007     |                     | Average<br>yld/cost |
|--|--------------------|----------|---------------------|--------------------|----------|---------------------|---------------------|
|  | Average<br>balance | Interest | Average<br>yld/cost | Average<br>balance | Interest | Average<br>yld/cost |                     |
| <b>ASSETS</b>  |                    |          |                     |                    |          |                     |                     |
| <b>Interest-earning assets:</b>  |                    |          |                     |                    |          |                     |                     |
| Loans receivable(1)  | \$ 545,958         | \$ 8,155 | 6.01%               | \$ 498,321         | \$ 7,986 |                     | 6.43%               |
| Mortgage-backed securities   | 97,397             | 1,132    | 4.67%               | 86,619             | 1,006    |                     | 4.66%               |
| Investment securities(2)   | 41,915             | 482      | 4.63%               | 37,474             | 512      |                     | 5.48%               |
| Other interest-earning assets(3)   | 665                | 4        | 2.42%               | 1,195              | 19       |                     | 6.38%               |
| Total interest-earning assets  | 685,935            | 9,773    | 5.73%               | 623,609            | 9,523    |                     | 6.13%               |
| Non interest-earning assets  | 36,265             |          |                     | 34,032             |          |                     |                     |
| Total assets   | \$ 722,200         |          |                     | \$ 657,641         |          |                     |                     |
| <b>LIABILITIES AND STOCKHOLDERS EQUITY</b>                                       |                    |          |                     |                    |          |                     |                     |
| <b>Interest-bearing liabilities:</b>   |                    |          |                     |                    |          |                     |                     |
| Deposits   | 486,394            | 2,926    | 2.42%               | 481,084            | 3,416    |                     | 2.85%               |
| Borrowings from the FHLB   | 155,675            | 1,571    | 4.06%               | 103,182            | 1,056    |                     | 4.10%               |
| Total interest-bearing liabilities   | 642,069            | 4,497    | 2.82%               | 584,266            | 4,472    |                     | 3.07%               |
| Non interest-bearing liabilities   | 9,934              |          |                     | 8,260              |          |                     |                     |
| Total liabilities  | 652,003            |          |                     | 592,526            |          |                     |                     |
| Stockholders equity  | 70,197             |          |                     | 65,115             |          |                     |                     |
| Total liabilities and stockholders equity  | \$ 722,200         |          |                     | \$ 657,641         |          |                     |                     |
| Net interest income  |                    | \$ 5,276 |                     |                    | \$ 5,051 |                     |                     |
| Interest rate spread(4)  |                    |          | 2.91%               |                    |          |                     | 3.06%               |
| Net yield on interest-earning assets(5)  |                    |          | 3.09%               |                    |          |                     | 3.25%               |
| Ratio of average interest-earning assets to average interest-bearing liabilities |                    |          | 107%                |                    |          |                     | 107%                |

- (1) Nonaccrual loans have been included in the appropriate average loan balance category, but interest on nonaccrual loans has not been included for purposes of determining interest income.
- (2) Tax equivalent adjustments to interest on investment securities were \$117,000 and \$108,000 for the quarter ended June 30, 2008 and 2007, respectively. Tax equivalent interest income is based upon a marginal effective tax rate of 34%.
- (3) Includes interest-bearing deposits in other banks.
- (4) Interest rate spread represents the difference between the average yield on interest-earning assets and the average cost of interest-bearing liabilities.
- (5) Net yield on interest-earning assets represents net interest income as a percentage of average interest-earning assets.

Table of Contents**Rate/Volume Analysis**

The following table presents, for the periods indicated, the change in interest income and interest expense (in thousands) attributed to (i) changes in volume (changes in the weighted average balance of the total interest earning asset and interest bearing liability portfolios multiplied by the prior year rate), and (ii) changes in rate (changes in rate multiplied by prior year volume). Changes attributable to the combined impact of volume and rate have been allocated proportionately based on the absolute value of changes due to volume and changes due to rate.

|                                    | <b>Three months ended June 30,<br/>2008 vs 2007</b> |  |            |
|------------------------------------|---|--|------------|
|                                    | <b>Volume</b>                                       | <b>Increase (decrease) due to<br/>Rate</b> | <b>Net</b> |
| <b>Interest income:</b>            |   |  |            |
| Loans receivable, net              | \$ 2,588  | \$ (2,419)                                 | \$ 169     |
| Mortgage-backed securities         | 123   | 3  | 126        |
| Investment securities (1)          | 264   | (294)                                      | (30)       |
| Other interest-earning assets      | (6)   | (9)  | (15)       |
| Total interest-earning assets      | 2,969   | (2,719)                                    | 250        |
| <b>Interest expense:</b>           |   |  |            |
| Deposits                           | 248   | (738)                                      | (490)      |
| Borrowings from the FHLB           | 597   | (82)                                       | 515        |
| Total interest-bearing liabilities | 845   | (820)                                      | 25         |
| Net change in net interest income  | \$ 2,124  | \$ (1,899)                                 | \$ 225     |

- (1) Tax equivalent adjustments to interest on investment securities were \$117,000 and \$108,000 for the quarters ended June 30, 2008 and 2007, respectively. Tax equivalent interest income is based upon a marginal effective tax rate of 34%.

**Total Interest Income.** Total interest income, on a tax equivalent basis, increased by \$250,000 or 2.6% to \$9.8 million for the quarter ended June 30, 2008 compared with the second quarter of 2007. The average balance of loans outstanding increased between the two periods as a result of loan originations added to the portfolio during the intervening period. However, the average yield on loans decreased 42 basis points primarily as a result of the Company's reduction of its prime rate four times during 2008 and three times during the last two quarters of 2007 by a combined 325 basis points mirroring the action taken by the Federal Open Markets Committee (FOMC) when it acted to reduce the fed funds rate. Interest income from mortgage-backed securities was higher in the second quarter of 2008 in comparison to the same period of 2007 due to purchases of \$19.6 million of securities during the intervening period. Interest income from investment securities decreased slightly as a result of reduced dividends received on FHLB stock despite increased balances of FHLB stock held.

**Total Interest Expense.** Total interest expense increased by \$25,000 to \$4.5 million during the three-month period ended June 30, 2008 as compared with the second quarter of 2007. Interest rates paid on the Bank's deposits dropped significantly during the second quarter of 2008, as rates on deposits indexed to the Merrill Lynch Ready Asset Money Market Fund decreased by 228 basis points during the first six months of 2008. Although the average balance of deposits reflects a \$5.3 million increase in balances, the average deposit balances during the second quarter of 2007 included broker-originated certificates of deposit of \$7.1 million which fully matured during the second and third



quarters of 2007.

Interest expense associated with borrowings from the Federal Home Loan Bank increased \$515,000 between the second quarters of 2008 and 2007. During the intervening period, the Bank increased its borrowings by \$52.5 million from the FHLB to fund loan growth as well as security purchases.

**Non-interest income.** Total non-interest income was \$1.1 million for the second quarter of 2008 compared with \$0.7 million for the same period in 2007. During the second quarter of 2008, non-interest income included the \$342,000 gain on sale of foreclosed real estate.

**Non-interest expense.** Total non-interest expense increased by \$64,000 to \$4.3 million for the three months ended June 30, 2008 compared to the same period in 2007. Legal expenses increased \$25,000 between the two quarters largely due to services rendered in conjunction with non-performing assets.

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**RESULTS OF OPERATIONS FOR THE SIX MONTHS ENDED JUNE 30, 2008 AND 2007**

**Net Income.** The Company recorded net income of \$2,465,000, or \$0.92 per diluted share, for the six months ended June 30, 2008 as compared to net income of \$2,435,000, or \$0.89 per diluted share, for the six months ended June 30, 2007.

**Average Balance Sheet**



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The following table sets forth information (dollars in thousands) relating to the Company's average balance sheet and reflects the average yield on assets and average cost of liabilities for the periods indicated. Yield and cost are computed by dividing income or expense by the average daily balance of interest-earning assets or interest-bearing liabilities, respectively, for the six-month periods indicated.

|   | 2008               |           | June 30,            |                    | 2007      |                     |
|---|--------------------|-----------|---------------------|--------------------|-----------|---------------------|
|   | Average<br>balance | Interest  | Average<br>yld/cost | Average<br>balance | Interest  | Average<br>yld/cost |
| <b>ASSETS</b>   |                    |           |                     |                    |           |                     |
| <b>Interest-earning assets:</b>   |                    |           |                     |                    |           |                     |
| Loans receivable(1)   | \$ 537,411         | \$ 16,338 | 6.11%               | \$ 493,038         | \$ 15,765 | 6.45%               |
| Mortgage-backed securities  | 99,810             | 2,363     | 4.76%               | 83,644             | 1,939     | 4.67%               |
| Investment securities(2)  | 41,850             | 1,012     | 4.86%               | 39,368             | 1,056     | 5.41%               |
| Other interest-earning<br>assets(3)   | 818                | 10        | 2.46%               | 3,571              | 86        | 4.86%               |
| Total interest-earning assets   | 679,889            | 19,723    | 5.83%               | 619,621            | 18,846    | 6.13%               |
| Non interest-earning assets   | 35,344             |           |                     | 34,091             |           |                     |
| Total assets  | \$ 715,233         |           |                     | \$ 653,712         |           |                     |
| <b>LIABILITIES AND STOCKHOLDERS EQUITY</b>  |                    |           |                     |                    |           |                     |
| <b>Interest-bearing liabilities:</b>  |                    |           |                     |                    |           |                     |
| Deposits  | 479,497            | 6,212     | 2.61%               | 478,742            | 6,646     | 2.80%               |
| Borrowings from the FHLB  | 157,363            | 3,203     | 4.09%               | 101,237            | 2,035     | 4.05%               |
| Total interest-bearing<br>liabilities   | 636,860            | 9,415     | 2.97%               | 579,979            | 8,681     | 3.02%               |
| Non interest-bearing<br>liabilities   | 9,285              |           |                     | 8,103              |           |                     |
| Total liabilities   | 646,145            |           |                     | 588,082            |           |                     |
| Stockholders' equity  | 69,088             |           |                     | 65,630             |           |                     |
| Total liabilities and<br>stockholders' equity   | \$ 715,233         |           |                     | \$ 653,712         |           |                     |
| Net interest income   |                    | \$ 10,308 |                     |                    | \$ 10,165 |                     |
| Interest rate spread(4)   |                    |           | 2.86%               |                    |           | 3.12%               |
| Net yield on interest-earning<br>assets(5)  |                    |           | 3.05%               |                    |           | 3.31%               |
| Ratio of average<br>interest-earning assets to<br>average interest-bearing<br>liabilities |                    |           | 107%                |                    |           | 107%                |

- (1) Nonaccrual loans have been included in the appropriate average loan balance category, but interest on nonaccrual loans has not been included for purposes of determining interest income.
- (2) Tax equivalent adjustments to interest on investment securities were \$234,000 and \$218,000 for the six months ended June 30, 2008 and 2007, respectively. Tax equivalent interest income is based upon a marginal effective tax rate of 34%.
- (3) Includes interest-bearing deposits in other banks.
- (4) Interest rate spread represents the difference between the average yield on interest-earning assets and the average cost of interest-bearing liabilities.
- (5) Net yield on interest-earning assets represents net interest income as a percentage of average interest-earning assets.

Table of Contents**Rate/Volume Analysis**

The following table presents, for the periods indicated, the change in interest income and interest expense (in thousands) attributed to (i) changes in volume (changes in the weighted average balance of the total interest earning asset and interest bearing liability portfolios multiplied by the prior year rate), and (ii) changes in rate (changes in rate multiplied by prior year volume). Changes attributable to the combined impact of volume and rate have been allocated proportionately based on the absolute value of changes due to volume and changes due to rate.

|                                    | <b>Six months ended June 30,<br/>2008 vs 2007</b> |  |            |
|------------------------------------|---|--|------------|
|                                    | <b>Volume</b>                                     | <b>Increase (decrease) due to<br/>Rate</b> | <b>Net</b> |
| <b>Interest income:</b>            |   |  |            |
| Loans receivable, net              | \$ 2,455  | \$ (1,882)                                 | \$ 573     |
| Mortgage-backed securities         | 387   | 37   | 424        |
| Investment securities (1)          | 148   | (192)                                      | (44)       |
| Other interest-earning assets      | (46)  | (30)                                       | (76)       |
| Total interest-earning assets      | 2,944   | (2,067)                                    | 877        |
| <b>Interest expense:</b>           |   |  |            |
| Deposits                           | 32  | (466)                                      | (434)      |
| Borrowings from the FHLB           | 1,148   | 20   | 1,168      |
| Total interest-bearing liabilities | 1,180   | (446)                                      | 734        |
| Net change in net interest income  | \$ 1,764  | \$ (1,621)                                 | \$ 143     |

- (1) Tax equivalent adjustments to interest on investment securities were \$234,000 and \$218,000 for the six months ended June 30, 2008 and 2007, respectively. Tax equivalent interest income is based upon a marginal effective tax rate of 34%.

**Total Interest Income.** Total interest income, on a tax equivalent basis, increased by \$877,000 or 4.7% to \$19.7 million for the six months ended June 30, 2008 compared with the first six months of 2007. The average balance of loans outstanding increased as a result of \$52.8 million of loan originations in excess of loan principal payments added to the portfolio during the intervening period. However, the average yield on loans decreased 34 basis points primarily as a result of the Company's reduction of its prime rate four times during 2008 and three times during the last two quarters of 2007 by a combined 325 basis points mirroring the action taken by the FOMC when it acted to reduce the fed funds rate. Interest income from mortgage-backed securities was higher in the first two quarters of 2008 in comparison to the same period of 2007 due to purchases of \$19.6 million of securities during the intervening period. Interest income from investment securities decreased as a result of reduced dividends received on FHLB stock despite increased balances of FHLB stock held.

**Total Interest Expense.** Total interest expense increased by \$734,000 to \$9.4 million during the six-month period ended June 30, 2008 as compared with the first half of 2007. Interest rates paid on the Bank's deposits dropped notably as rates on deposits indexed to the Merrill Lynch Ready Asset Money Market Fund decreased by 228 basis points during the first six months of 2008 and therefore significantly reduced interest expense on deposits. Although the average balance of deposits reflects only a \$755,000 increase in balances, the average deposit balances during the first six months of 2007 included broker-originated certificates of deposit of \$9.4 million which fully matured during the

second and third quarters of 2007.

Interest expense associated with borrowings from the Federal Home Loan Bank increased \$1.2 million between the first six months of 2008 and 2007. During the intervening period, the Bank increased its borrowings by \$56.1 million from the FHLB to fund loan growth as well as security purchases.

**Non-interest income.** Total non-interest income was \$2.2 million for the first six months of 2008 compared with \$2.3 million for the same period in 2007. The first six months of 2008 included a \$197,000 insurance claim recovery related to a 2007 expense sustained as a result of the bankruptcy of one of the Bank's loan servicing agents. Additionally, other income during the first six months of 2008 included \$100,000 of non-recurring income related to the Company's real estate held for development, a \$342,000 gain on the sale of foreclosed real estate and \$61,000 of investment referral commissions. The first six months of 2007 included \$777,000 of non-recurring income from a fraud-related settlement.

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**Non-interest expense.** Total non-interest expense decreased by \$264,000 to \$8.6 million for the six months ended June 30, 2008 compared to the same period in 2007. During 2007, the Bank incurred a \$270,000 loss as the result of the bankruptcy of one of the Bank's loan servicing agents.

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**LIQUIDITY AND CAPITAL RESOURCES**





**Liquidity**



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The Company's liquidity is a measure of its ability to fund loans, pay withdrawals of deposits, and other cash outflows in an efficient, cost-effective manner. The Company's short-term sources of liquidity include maturity, repayment and sales of assets, excess cash and cash equivalents, new deposits, broker deposits, other borrowings, and new borrowings from the Federal Home Loan Bank. There has been no material adverse change during the six-month period ended June 30, 2008 in the ability of the Company and its subsidiaries to fund their operations.

At June 30, 2008, the Company had commitments outstanding under letters of credit of \$1.5 million, commitments to originate loans of \$10.2 million, and commitments to fund undisbursed balances of closed loans and unused lines of credit of \$53.8 million. At June 30, 2008, the Bank had \$1.6 million outstanding commitments to sell loans. There has been no material change during the six months ended June 30, 2008 in any of the Company's other contractual obligations or commitments to make future payments.

### **Capital Requirements**

The Bank was in compliance with all of its capital requirements as of June 30, 2008.

### **CRITICAL ACCOUNTING POLICIES**

Certain critical accounting policies of the Company require the use of significant judgment and accounting estimates in the preparation of the consolidated financial statements and related data of the Company. These accounting estimates require management to make assumptions about matters that are highly uncertain at the time the accounting estimate is made. Management believes that the most critical accounting policy requiring the use of accounting estimates and judgment is the determination of the allowance for loan losses. If the financial position of a significant amount of debtors should deteriorate more than the Company has estimated, present reserves for loan losses may be insufficient and additional provisions for loan losses may be required. The allowance for loan losses was \$2,845,000 at June 30, 2008.

### **ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**



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As a smaller reporting company as defined by Item 10 of Regulation S-K, the Company is not required to provide the information required by this item.

### **ITEM 4T. CONTROLS AND PROCEDURES**

#### **Evaluation of Disclosure Controls and Procedures**

Based on their evaluation of the Company's disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934 (the Exchange Act)), the Company's principal executive officer and principal financial officer have concluded that as of the end of the period covered by this Quarterly Report on Form 10-Q such disclosure controls and procedures are effective to ensure that information required to be disclosed by the Company in the reports it files and submits pursuant to the rules and forms of the SEC is accumulated and communicated to the Company's management including the principal executive officer and principal financial officer, as appropriate, to allow timely decisions regarding required disclosures.

#### **Changes in Internal Controls over Financial Reporting**

During the quarter under report, there was no change in the Company's internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

Table of Contents**TF FINANCIAL CORPORATION AND SUBSIDIARIES****PART II****ITEM 1. LEGAL PROCEEDINGS**

Neither the Company nor its subsidiaries are involved in any pending legal proceedings, other than routine legal matters occurring in the ordinary course of business that in the aggregate involve amounts which are believed by management to be immaterial to the consolidated financial condition or results of operations of the Company.

**ITEM 1A. RISK FACTORS**

As a smaller reporting company as defined by Item 10 of Regulation S-K, the Company is not required to provide the information required by this item.

**ITEM 2. UNREGISTERED SALE OF EQUITY SECURITIES AND USE OF PROCEEDS**

The following table provides information on repurchases by the Company of its common stock in each month for the three months ended June 30, 2008:

| Month                          | Total Number of Shares Purchased | Average Price Paid per Share | Total Number of Shares Purchased as Part of Publicly Announced Plan of Program | Maximum Number of Shares that may yet be Purchased Under the Plans or Programs |
|--------------------------------|----------------------------------|------------------------------|--|--|
| April 1, 2008 - April 30, 2008 |                                  | \$                           |  | 150,457  |
| May 1, 2008 - May 31, 2008     | 3,300                            | \$ 23.52                     | 3,300  | 147,157  |
| June 1, 2008 - June 30, 2008   | 15,150                           | \$ 23.24                     | 15,150   | 132,007  |

**ITEM 3. DEFAULTS UPON SENIOR SECURITIES**

Not applicable.

**ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

None.

**ITEM 5. OTHER INFORMATION**

None.

**ITEM 6. EXHIBITS**

(a) Exhibits

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31. Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32. Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.



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**TF FINANCIAL CORPORATION**

**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this Report to be signed on its behalf by the undersigned, thereunto duly authorized.

Date: August 14, 2008

/s/ Kent C. Lufkin  
Kent C. Lufkin  
President and CEO  
(Principal Executive Officer)

Date: August 14, 2008

/s/ Dennis R. Stewart  
Dennis R. Stewart  
Executive Vice President and  
Chief Financial Officer  
(Principal Financial & Accounting Officer)