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SUSSEX BANCORP
Form 10QSB
August 07, 2002

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D. C. 20549

FORM 10-QSB

(Mark One)

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

For the quarterly period ended June 30, 2002

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 0-29030

SUSSEX BANCORP

(Exact name of registrant as specified in its charter)

New Jersey

22-3475473

(State of other jurisdiction of
incorporation or organization)

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

399 Route 23, Franklin, New Jersey

07416

(Address of principal executive offices)

(Zip Code)

Issuer's telephone number, including area code) (973) 827-2914

(Former name, former address and former fiscal year, if changed since last
report)

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 and 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

As of August 1, 2002 there were 1,661,083 shares of common stock, no
par value, outstanding.

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PART I - FINANCIAL INFORMATION

ITEM 1 - FINANCIAL STATEMENTS

SUSSEX BANCORP CONSOLIDATED BALANCE SHEETS (in Thousands, Except Share Data) (Unaudited)

ASSETS -----	June 30, 2002 -----	December 31, -----
Cash and Due from Banks	\$10,481	\$6,150
Federal Funds Sold	21,215	34,885
Total Cash and Cash Equivalents	31,696	41,035
Time Deposits in Other Banks	6,100	3,100
Securities Available for Sale, at Fair Value	55,639	42,712

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Loans (Net of Unearned Income)	107,616	106,148
Less: Allowance for Loan Losses	1,292	1,143
	-----	-----
Net Loans	106,324	105,005
Other Real Estate Owned	197	187
Premises and Equipment, Net	4,814	4,925
Federal Home Loan Bank Stock, at Cost	667	685
Intangible Assets, Net	677	743
Goodwill	1,757	1,712
Accrued Interest Receivable	1,190	964
Other Assets	2,156	2,275
	-----	-----
Total Assets	211,217	\$203,343
	=====	=====
LIABILITIES AND STOCKHOLDERS' EQUITY		

Liabilities:		
Deposits:		
Noninterest-Bearing Demand	\$27,900	\$26,252
Savings, Club and Interest-Bearing Demand	99,964	89,317
Time of Less than \$100	43,610	48,776
Time of \$100 and Over	14,392	14,209
	-----	-----
Total Deposits	185,866	178,554
Long-Term Debt	10,000	10,000
Other Liabilities	2,548	2,552
	-----	-----
Total Liabilities	198,414	191,106
Stockholders' Equity:		
Common Stock, No Par Value; Authorized 5,000,000 Shares; Issued 1,683,262 in 2002 and 1,672,765 in 2001; Outstanding 1,659,550 in 2002 and 1,659,057 in 2001	7,817	7,732
Retained Earnings	4,871	4,509
Treasury Stock, at cost; 23,712 Shares in 2002 13,708 Shares in 2001	(232)	(127)
Accumulated Other Comprehensive Income, Net of Income Tax	347	123
	-----	-----
Total Stockholders' Equity	12,803	12,237
	-----	-----
Total Liabilities and Stockholders' Equity	211,217	\$203,343
	=====	=====

See Notes to Consolidated Financial Statements

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SUSSEX BANCORP
CONSOLIDATED STATEMENTS OF INCOME
(In Thousands Except Share Data)
(Unaudited)

	Three Months Ended June 30		
	2002	2001	2002
	----	----	----
INTEREST INCOME			
Interest and Fees on Loans	\$1,900	\$2,037	\$3,81
Interest on Securities:			
Taxable	499	595	94
Exempt from Federal Income Tax	116	66	21
Interest on Federal Funds Sold	112	220	23
Interest on Time Deposits	33	46	5
	-----	-----	-----
Total Interest Income	2,660	2,964	5,26
INTEREST EXPENSE			
Interest on Deposits	710	1,356	1,53
Interest on Borrowings	125	125	24
	-----	-----	-----
Total Interest Expense	835	1,481	1,78
Net Interest Income	1,825	1,483	3,47
Provision for Loan Losses	75	63	15
	-----	-----	-----
Net Interest Income After Provision for Loan Losses	1,750	1,420	3,32
NON-INTEREST INCOME			
Service charges on Deposit Accounts	174	139	31
Gain on Sale of Loans Held for Sale	6	5	2
Investment Brokerage Fees	76	52	14
Insurance Commissions and Fees	434	0	86
Other Income	142	149	24
	-----	-----	-----
Total Non-Interest Income	832	345	1,59
NON-INTEREST EXPENSE			
Salaries and Employee Benefits	1,138	755	2,22
Occupancy, Net	149	112	29
Furniture and Equipment	214	158	43
Stationary and Supplies	41	28	7
Advertising and Promotion	131	57	24
Audit and Exams	30	32	6
Amortization of Intangibles	32	21	6
Other Expenses	372	255	72
	-----	-----	-----
Total Non-Interest Expense	2,107	1,418	4,12
Income Before Provision for Income Taxes	475	347	79
Provision for Income Taxes	144	107	23
	-----	-----	-----

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Net Income	\$ 331 =====	\$ 240 =====	\$ 56 =====
Net Income Per Common Share-Basic	\$ 0.20 =====	\$ 0.15 =====	\$ 0.3 =====
Net Income Per Common Share-Diluted	\$ 0.19 =====	\$ 0.14 =====	\$ 0.3 =====

See Notes to Consolidated Financial Statements

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SUSSEX BANCORP
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(In Thousands)
(Unaudited)

	Three Months Ended June 30		Six Months Ended June 30	
	2002 ----	2001 ----	2002 ----	2001 ----
Net Income	\$331	\$240	\$562	\$450
Other comprehensive income, net of tax				
Unrealized gain on available for sale securities	340 ----	54 ----	224 ----	320 ----
Comprehensive income	\$671 =====	\$294 =====	\$786 =====	\$770 =====

See Notes to Consolidated Financial Statements

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SUSSEX BANCORP
CONSOLIDATED STATEMENT OF CHANGES IN
STOCKHOLDERS' EQUITY
(In Thousands Except Share Data)
(Unaudited)

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	Number of Shares Outstanding -----	Common Stock -----	Retained Earnings -----	Trea Sto -----
Balance December 31, 2000	1,498,351	\$ 6,385	\$ 4,027	(\$
Net Income for the Period			450	
Cash Dividends, at \$.07 per share			(115)	
Sale of Common Stock	139,906	1,160		
Stock Options Exercised	2,616	24		
Shares Issued Through Dividend Reinvestment Plan	8,807	71		
Treasury Shares Purchased	(471)			
Change in Unrealized Gain on Securities, Available for Sale				
Balance June 30, 2001	1,649,209 =====	\$ 7,640 =====	\$ 4,362 =====	(\$ =====
Balance December 31, 2001	1,659,057	\$ 7,732	\$ 4,509	(\$
Net Income for the Period			562	
Cash Dividends, at \$.06 per share			(200)	
Stock Options Exercised	4,090	25		
Shares Issued Through Dividend Reinvestment Plan	6,407	60		
Treasury Shares Purchased	(10,004)			
Change in Unrealized Gain on Securities, Available for Sale				
Balance June 30, 2002	1,659,550 =====	\$7,817 =====	\$4,871 =====	 =====

See Notes to Consolidated Financial Statements

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CONSOLIDATED STATEMENTS
OF CASH FLOWS
(Unaudited)

	Six Month June 2002 -----
Cash Flows from Operating Activities:	
Net Income	\$ 562
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:	
Net Loan Origination and Commitment Fees	(13)

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Depreciation and Amortization of Premises and Equipment	290
Amortization of Intangible Assets	65
Net Amortization of Securities	228
Provision for Loan Losses	150
Gain on Sale of Loans Held for Sale	(24)
Origination of Loans Held for Sale	(1,196)
Proceeds of Sales of Loans held for Sale	1,220
Increase in Accrued Interest Receivable	(226)
Increase in Cash Value of Life Insurance Policy	(28)
Decrease (Increase) in Other Assets and Goodwill	(49)
(Decrease) Increase in Other Liabilities	(4)

Net Cash Provided by Operating Activities	975

Cash Flow from Investing Activities:	
Securities Available for Sale:	
Proceeds from Maturities and Paydowns	10,849
Proceeds from Sales/Calls Prior to Maturity	1,000
Purchases	(24,628)
Securities Held to Maturity:	
Proceeds from Maturities	0
Purchases	0
Net Purchases of Time Deposits in Other Banks	(3,000)
Net (Increase) Decrease in Loans Outstanding	(1,456)
Redemption of FHLB Stock	18
Purchase of Premises and Equipment	(179)
Net Increase in Other Real Estate	(10)

Net Cash Used In Investing Activities	(17,406)

Cash Flows from Financing Activities:	
Net Increase in Total Deposits	7,312
Purchase of Treasury Stock	(105)
Sale of Common Stock	0
Exercise of Stock Options	25
Payment of Dividends Net of Reinvestment	(140)

Net Cash Provided by Financing Activities	7,092

Net (Decrease) Increase in Cash and Cash Equivalents	(\$ 9,339)
Cash and Cash Equivalents, Beginning of Period	41,035

Cash and Cash Equivalents, End of Period	\$ 31,696
	=====

See Notes to Consolidated Financial Statements

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

1. Basis of Presentation

Sussex Bancorp ("the Company"), a one-bank holding company, was incorporated in January, 1996 to serve as the holding company for Sussex Bank, ("the Bank"). The Bank is the only active subsidiary of the Company at June 30, 2002. The Bank operates eight banking offices all located in Sussex County and pursuant to an acquisition which was consummated on October 1, 2001, is the parent of Tri-State Insurance Agency, Inc., a full service insurance agency located in Sussex County, New Jersey. The Company is subject to the supervision and regulation of the Board of Governors of the Federal Reserve System (the "FRB"). The Bank's deposits are insured by the Bank Insurance Fund ("BIF") of the Federal Deposit Insurance Corporation ("FDIC") up to applicable limits. The operations of the Company and the Bank are subject to the supervision and regulation of the FRB, FDIC and the New Jersey Department of Banking and Insurance (the "Department").

The consolidated financial statements included herein have been prepared without audit in accordance with the rules and regulations of the Securities and Exchange Commission and reflect all adjustments which, in the opinion of management, are necessary for a fair statement of the results for interim periods. All adjustments made were of a normal recurring nature. Operating results for the six months ended June 30, 2002 are not necessarily indicative of the results that may be expected for the year ended December 31, 2002. These consolidated financial statements should be read in conjunction with the consolidated financial statements and the notes thereto that are included in the Company's Annual Report on Form 10-KSB for the fiscal period ended December 31, 2001.

2. Securities

The amortized cost and approximate market value of securities are summarized as follows (in thousands):

	June 30, 2002		December 31, 2001
	Amortized Cost	Market Value	Amortized Cost
	----	-----	----
Available For Sale:			
US Treasury Securities and Obligations of US Government Corporations and Agencies	\$34,673	\$35,063	\$29,292
Corporate Bonds	7,626	7,799	4,605
Obligations of State and Political Subdivisions	11,804	11,903	7,714
Equity Securities	899	874	899
	-----	-----	-----
Total Available for Sale Securities	\$55,060	\$55,639	\$42,510
	=====	=====	=====

3. Net Income Per Common Share

Basic net income per share of common stock is calculated by dividing net income by the weighted average number of shares of common stock outstanding during the period. Diluted net income per share is calculated by dividing net income by the weighted average number of shares of common

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stock outstanding during the period plus the dilutive effect of potential common shares.

On October 1, 2001, the Company, through its Sussex Bank subsidiary, acquired Tri-State Insurance Agency, Inc. The purchase price paid by the Company for Tri-State was comprised of an upfront cash payment at closing, and deferred payments on the first, second and third anniversaries of the closing. These deferred payments will be satisfied through a mix of cash and common stock of the Company, with the number of shares issued based, in part, upon the then-current market price of the Company's common stock. The deferred payments are subject to downward adjustment based upon the net income of Tri-State as a subsidiary of Sussex Bank. The estimated number of shares to be issued to the former principals of Tri-State on the first three anniversaries of the acquisition will be deemed outstanding for purposes of calculating the Company's diluted earnings per share, although they will not be deemed outstanding until issued for purposes of calculating the Company's basic earnings per share. The estimated number of shares to be issued for purposes of the Company's diluted earnings per share will be calculated based upon Tri-State's earnings to date at the time of calculation and the Company's then current stock price. The actual number of shares issued by the Company to the former principals of Tri-State may vary significantly from these estimates, and will not be known until such time as the shares are actually issued.

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The following table sets forth the computations of basic and diluted earnings per share (dollars in thousands, except per share data):

	Six Months Ended, June 30, 2002			Six Months Ended	
	Income (Numerator)	Shares (Denominator)	Per Share Amount	Income (Numerator)	Sh (Denom
Basic earnings per share:					
Net income applicable to common stockholders	\$ 562	1,657	\$ 0.34 =====	\$ 450	1,
Effect of dilutive securities:					
Stock options	--	18		--	
Deferred common stock payments for purchase of insurance agency	3	57		--	---
Diluted earnings per share:					
Net income applicable to common stockholders and assumed conversions	\$ 565 =====	1,732 =====	\$ 0.33 =====	\$ 450 =====	\$ 1, =====

Three Months Ended, June 30, 2002

Three Months Ende

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	Income (Numerator)	Shares (Denominator)	Per Shares Amount	Income (Numerator)	Sh (Denom
Basic earnings per share:					
Net income applicable to common stockholders	\$ 331	1,655	0.20 =====	\$ 240	1,
Effect of dilutive securities:					
Stock options		18			
Deferred common stock payments for purchase of insurance agency	1	57			
Diluted earnings per share:					
Net income applicable to common stockholders and assumed conversions	\$ 332 =====	1,730 =====	\$ 0.19 =====	\$ 240 =====	1, ==

4. Comprehensive Income

The components of other comprehensive income and related tax effects for the six months ended June 30, 2002 and 2001 are as follows:

	Six Months Ended June 30	
	2002	2001
Unrealized holding gains on available for sale securities	\$377	\$538
Less: reclassification adjustments for gains included in net income	--	--
Net unrealized gains	377	538
Tax effect	153	218
Other comprehensive income, net of tax	\$224 =====	\$320 =====

5. New Accounting Standards

On June 29, 2001, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 141, Business Combinations, which supersedes APB Opinion No. 16, Business Combinations, and FASB Statement No. 38, Accounting for Preacquisition Contingencies of Purchased Enterprises. All business combinations in the scope of this Statement are to be

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accounted for using the purchase method of accounting. The provisions of this Statement apply to all business combinations initiated after June 30, 2001. The Company will apply this new pronouncement on a prospective basis.

On June 29, 2001, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 142, Goodwill and Other Intangible Assets. This Statement supersedes APB Opinion No. 17, Intangible Assets. Under the new standard goodwill will no longer be subject to amortization over its estimated useful life. Rather goodwill will be subject to at least an annual assessment for impairment by applying a fair value test. An acquired intangible asset would be separately recognized if the benefit of the intangible asset is obtained through contractual or other legal rights, or if the intangible asset can be sold, transferred, licensed, rented or exchanged regardless of the acquirers intent to do so. All of the provisions of this Statement should be applied in fiscal years beginning after December 15, 2001, to all goodwill and other intangible assets recognized in an entity's statement of financial position at the beginning of that fiscal year, regardless of when those previously recognized assets were initially recognized. The adoption of this new pronouncement did not have a material impact on the Company's financial position or results of operations.

In June 2001, the Financial Accounting Standards Board issued Statement No. 143, "Accounting for Asset Retirement Obligations," which addresses the financial accounting and reporting for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. This Statement requires that the fair value of a liability for an asset retirement obligation be recognized in the period in which it is incurred if a reasonable estimate of fair value can be made. The associated asset retirement costs are capitalized as part of the carrying amount of the long-lived asset. This Statement will become effective for the Company on January 3, 2003 and is not expected to have a significant impact on the Company's financial condition or results of operations.

In August 2001, the Financial Accounting Standards Board issued Statement No. 144, "Accounting for the Impairment of or Disposal of Long-Lived Assets." This Statement supercedes FASB Statement No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of," and the accounting and reporting provisions of APB Opinion No. 30, "Reporting the Results of Operations-Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions for the Disposal of a Segment of a Business." This Statement also amends ARB No. 51, " Consolidated Financial Statements." The provisions of this Statement were effective for the Company on January 1, 2002, and did not have a significant impact on financial condition or results of operations.

6. Segment Information

The Company's insurance operations are managed separately from the traditional banking and related financial services that the Company also offers. The insurance operation provides commercial, individual, and group benefit plans and personal coverage. Insurance operations commenced on October 1, 2001 when the Company acquired Tri-State Insurance Agency, Inc. Accordingly, segment information for 2001 is not applicable.

Banking and Financial Services	Insurance Services	Total
---	-----------------------	-------

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(Amounts in thousands)

Three months ended June 30, 2002			
Revenues from external sources	\$2,223	\$ 434	\$2,657
Income before income taxes	\$ 413	\$ 62	\$ 475
Six months ended June 30, 2002			
Revenues from external sources	\$4,214	\$ 862	\$5,076
Income before income taxes	\$ 691	\$ 108	\$ 799

7. Subsequent Event

On July 11, 2002 Sussex Capital Trust I, a Delaware statutory business trust and a wholly-owned subsidiary of the Company, issued \$5 million of variable rate capital trust pass-through securities to investors. Sussex Capital Trust I purchased \$5.1 million of variable rate junior subordinated deferrable interest debentures from Sussex Bancorp. The debentures are the sole asset of the Trust. The terms of the junior subordinated debentures are the same as the terms of the capital securities. Sussex Bancorp has also fully and unconditionally guaranteed the obligations of the Trust under the capital securities. The capital securities are redeemable by Sussex Bancorp on or after October 7, 2007, at par or earlier if the deduction of related interest for federal income taxes is prohibited, classification as Tier I Capital is no longer allowed, or certain other contingencies arise. The capital securities must be redeemed upon final maturity of the subordinated debentures on October 7, 2032. Proceeds totaling approximately \$4.8 million were moved to paid in capital at Sussex Bank. Financing costs related to the Company's issuance of mandatory redeemable capital debentures will be amortized over a five-year period and will be included in other assets.

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ITEM 2 - MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

RESULTS OF OPERATIONS

Three and Six Months ended June 30, 2002 and June 30, 2001

CRITICAL ACCOUNTING POLICIES

Disclosure of the Company's significant accounting policies included in Note 2 to the consolidated financial statements of the Company's Annual Report on Form 10-KSB for the year ended December 31, 2001. Some of these policies are particularly sensitive requiring significant judgments, estimates and assumptions to be made by management. Additional information is contained on pages 11 and 15 of this Form 10-QSB for the provision and allowance for loan losses.

OVERVIEW

The Company realized net income of \$331 thousand for the second quarter of 2002, an increase of \$91 thousand from the \$240 thousand reported for the same period in 2001. Basic earnings per share increased from \$0.15 in the second

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quarter of 2001 to \$0.20 for the second quarter of 2002. Diluted earnings per share were \$0.14 in the second quarter of 2001 and increased to \$0.19 in the second quarter of 2002.

For the six months ended June 30, 2002, net income was \$562 thousand, an increase of \$112 thousand from the \$450 thousand reported for the same period in 2001. Basic earnings per share were \$0.34 for the six months ended June 30, 2002 compared to basic earnings per share of \$0.28 for the six-month period ended June 30, 2001. Diluted earnings per share of \$0.33 for the six months ended June 30, 2002 an increase from \$0.27 from the first six months of 2001.

The results reflect a substantial decrease in interest expense due to declining market rates of interest, partially offset by a decrease in interest income, coupled with an increase in non-interest income earned through Tri-State Insurance Agency, Inc. ("Tri-State"). The Company did not acquire Tri-State until October 1, 2001, and so Tri-State's results are not included in the six months ended June 30, 2001.

RESULTS OF OPERATIONS

Interest Income. Total interest income decreased \$304 thousand, or 10.3%, to \$2.7 million for the quarter ended June 30, 2002 from \$3.0 million for the same period in 2001. This decrease was primarily attributable to a 126 basis point decrease in average rate earned, on a fully taxable equivalent basis, from 6.94% during the second quarter of 2001 to 5.68% in the second quarter of 2002. Offsetting the rate decrease was an increase of \$16.7 million in average second quarter interest earning balances from \$174.2 million in 2001 to \$190.9 million in 2002. The effect of the rate decline exceeded the volume increases in average balances. The decline in rates had the greatest effect on federal funds sold. The average rate earned on federal funds sold decreased to 1.77% in the second quarter of 2002 from 4.23% during the second quarter of 2001, while the average balance increased 21.7% to \$25.0 million from \$20.6 million during the same periods. As the inflow of deposits exceeded loan demand during the second three months of 2002, excess funds were invested in federal funds sold and investment securities. The same scenario exists in the loan portfolio where the average rate earned on loans decreased 80 basis points to 7.18% for the second quarter of 2002 from 7.98% in the second quarter of 2001 and average loan balance increased 3.7% from \$102.4 million to \$106.1 million from second quarter 2001 to second quarter 2002. Taxable investment securities average balances increased by \$335 thousand and the average rate earned declined by 97 basis points, lowering income by \$93 thousand. The average balance of tax-exempt securities increased by \$5.3 million from \$6.6 million for the second quarter 2001 to \$11.9 million during the second quarter of 2002. The average rate earned on tax exempt securities increased by 25 basis points and interest income on a tax equivalent basis increased by \$76 thousand in the current quarter compared to the year ago period. As the result of both market changes in interest rates and larger average balances in lower yielding assets, interest income for the second quarter of 2002 declined compared to the second quarter of 2001.

For the six months ended June 30, 2002, interest income, on a fully taxable equivalent basis, decreased \$597 thousand, or 10.0%, to \$5.3 million from the \$5.9 million reported for the same period in 2001. While market rates of interest were falling during the first six months of 2002, average interest earning assets increased \$20.2 million to \$188.8 million from \$168.6 million during the same period in 2001. The average balance in the loan portfolio increased \$3.6 million, tax exempt securities increased \$4.5 million and federal funds sold increased \$9.5 million during the first six months of 2002 over the same period in 2001. The effects of both changing market rates and larger average balances in lower yielding assets, the average yield on interest earning assets on a fully taxable equivalent basis decreased 140 basis points from 7.11% from the first half of 2001 to 5.71% for the same period of 2002.

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Interest Expense. The Company's interest expense for the second quarter of 2002 decreased \$646 thousand, or 43.6% to \$835 thousand from \$1.5 million in the second quarter of 2001, as the average balance of interest bearing liabilities increased \$18.1 million, or 12.2% to \$166.3 million during the second quarter of 2002 from \$148.2 million in the same period of 2001. The increase in the average balance of interest bearing liabilities was more than offset by the reduction in rates, as the average cost of funds declined to 2.01% for the second quarter of 2002 from 4.01% in the second quarter of 2001. Interest expense on time deposits, the largest component of the decrease, declined \$444 thousand, or 50.2% to \$441 thousand as the average balance in time deposits decreased \$7.2 million, or 10.9% in the second quarter of 2002 compared to the same period in 2001. As a result of a large scale marketing promotion for low cost deposits which began in the fourth quarter of 2001, NOW deposit average balances have grown \$16.7 million, or 110.9%, from \$15.0 million during the second quarter 2001 to \$31.7 million in the second quarter of 2002. The interest expense on NOW deposits increased \$10 thousand from the second quarter of 2001, while the average interest rate paid decreased 56 basis points from 1.31% to 0.75% during the same periods. Average savings deposits reflect an increase of \$13.1 million, or 27.0%, in average balances while the average rate paid declined 170 basis points from 3.01% in the second quarter of 2001 to 1.31% in the second quarter of 2002. Average borrowed funds remained constant at \$10 million from second quarter of 2001. The Company entered into three ten year callable Federal Home Loan Bank advances totaling \$10 million in December 2000 at an average rate of 4.95% and quarterly interest expense of \$125 thousand. The FHLB advances were an investment strategy used to payoff short-term borrowings and to have liquidity available to purchase investments.

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For the six months ended June 30, 2002 interest expense decreased \$1.2 million, or 39.7%, to \$1.8 million from \$3.0 million for the same period last year. This decrease was largely due to a decrease in interest expense on time deposits of \$756 thousand, or 43.4%, from \$1.7 million for the first half of 2001 to \$984 thousand during the first six months of 2002, as the average balance in time deposit accounts decreased \$4.6 million, or 7.2%, over the same six-month periods. As market rates of interest declined during the first six months of 2002, the Company shifted it's focus from drawing time deposits on the basis of rate to attracting customers through its new marketing promotion of lower costing NOW and savings accounts. The average balance of NOW deposits increased \$16.6 million, or 109.8%, from \$15.1 million during the first half of 2001 to \$ 31.7 million in the first half of 2002. For the first six months of 2002, the Company's average cost of time deposits was 3.36%, while the average cost of NOW accounts was 0.83%. Savings deposits increased \$12.7 million, or 27.0%, from \$47.2 million during the first six months of 2001 to \$ 59.9 million during the same period of 2002. The Company's borrowed funds remained constant at \$10.0 million during the first six months of 2001 and 2002. The average rate paid on total interest bearing liabilities decreased 198 basis points from 4.17% in the first six months of 2001 to 2.19% during the same period in 2002. This decrease in the average cost of funds was the combination of the Company decreasing its rates of interest paid on interest bearing deposits due to the decline in market rates and the Company's strategy of attracting lower cost deposits and repricing its higher costing time deposit portfolio.

The following table presents, on a tax equivalent basis, a summary of the Company's interest-earning assets and their average yields, and interest-bearing liabilities and their average costs and shareholders' equity for the six months ended June 30, 2002 and 2001. The average balance of loans includes non-accrual loans, and associated yields include loan fees, which are considered adjustment

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to yields.

	Comparative Average Balance Sheets Six Months Ended June 30,			
	2002 Average Balance -----	2002 Interest Income/ Expense -----	Average Rates Earned/ Paid -----	Average Balance -----
	(Dollars in Thousands)			
Assets				
Interest Earning Assets:				
Taxable Loans (net of unearned income)	\$ 106,113	\$ 3,817	7.25%	\$ 102,519
Tax Exempt Securities	11,061	298	5.43%	6,596
Taxable Investment Securities	38,158	932	4.93%	38,155
Federal Funds Sold	27,629	237	1.71%	18,157
Time Deposits in Other Banks	5,078	50	1.99%	2,323
Other (1)	728	15	4.16%	798
	-----	-----		-----
Total Earning Assets	\$ 188,767	\$ 5,349	5.71%	\$ 168,548
Non-Interest Earning Assets	\$ 18,496			\$ 13,119
Allowance for Loan Losses	(\$ 1,219)			(\$ 1,010)
	-----			-----
Total Assets	\$ 206,044			\$ 180,657
	=====			=====
Liabilities and Shareholders' Equity				
Interest Bearing Liabilities:				
NOW Deposits	\$ 31,700	\$ 131	0.83%	\$ 15,113
Savings Deposits	59,908	406	1.37%	47,178
Money Market Deposits	3,642	18	1.00%	7,542
Time Deposits	59,093	984	3.36%	63,683
	-----	-----		-----
Total Interest-Bearing Deposits	154,343	1,539	2.01%	133,516
Borrowed Funds	10,000	249	4.95%	10,000
	-----	-----		-----
Total Interest Bearing Liabilities	\$ 164,343	\$ 1,788	2.19%	\$ 143,516
Non-Interest Bearing Liabilities:				
Demand Deposits	\$ 26,865			\$ 24,832
Other Liabilities	2,435			819
	-----			-----
Total Non-Interest Bearing Liabilities	\$ 29,300			\$ 25,651
Shareholders' Equity	\$ 12,401			\$ 11,490
	-----			-----
Total Liabilities and Shareholders' Equity	\$ 206,044			\$ 180,657
	=====			=====
Net Interest Differential		\$ 3,561		
Net Interest Spread			3.52%	

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Net Yield on Interest-Earning Assets

3.80%

(1) Includes FHLB stock and interest-bearing deposits

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Net-Interest Income. The net interest income for the second quarter of 2002 increased \$342 thousand over the same period last year. This increase was the result of liabilities repricing faster and lower than earning assets in a declining market rate environment and the Company's ability to shift its average balances to lower costing interest bearing liabilities, thereby further reducing its cost of funds. The net interest spread increased, on a fully taxable equivalent basis, by 73 basis points to 3.67% and the net yield on interest-bearing assets increased 47 basis points to 3.97% in the second quarter of 2002 compared to the year ago period.

Net interest income for the six months ended June 30, 2002 increased \$535 thousand, or 18.2%, over the same period last year. The net interest spread increased, on a fully taxable equivalent basis, 57 basis points and the net yield on interest-bearing assets improved by 23 basis points between the first six-month periods of 2001 and 2002. This comparison displays the effect of declining market rates of interest repricing deposit liabilities faster than earning assets during the first six-month periods of 2002 compared to the first six months of 2001.

Provision for Loan Losses. For the three months ended June 30, 2002 the provision for possible loan losses was \$75 thousand compared to \$63 thousand for the second quarter ended June 30, 2001. The provision for possible loan losses was \$150 thousand for the six months ended June 30, 2002 as compared to \$126 thousand for the same period last year. The provision for loan losses reflects management's judgment concerning the risks inherent in the Company's existing loan portfolio and the size of the allowance necessary to absorb the risks, as well as the average balance of the portfolio over both periods. Management reviews the adequacy of its allowance on an ongoing basis and will provide for additional provision in future periods, as management may deem necessary.

Non-Interest Income. For the second quarter of 2002, total non-interest income increased \$487 thousand, or 141.2%, from the same period in 2001. On October 1, 2001 the Company acquired Tri-State and in the second quarter of 2002 the subsidiary contributed \$434 thousand in insurance commission and fee income to non-interest income that was not present in the first quarter of 2001. Investment brokerage fee income increase by \$24 thousand, or 46.2%, to \$76 thousand for the period ending June 30, 2002 compared to \$52 thousand earned during the second quarter of 2001. Service charges on deposit accounts increased \$35 thousand to \$174 thousand and other income decreased \$7 thousand to \$142 thousand for the quarter ended June 30, 2002. This increase in service charges on deposit accounts is credited to the growth in the Company's deposits as a result of the marketing promotion.

For the six months ended June 30, 2002, non-interest income increased \$1.0 million, or 168.9%, from the same period in 2001. Insurance commissions and fees income for the first six months of 2002 resulted in an additional \$862 thousand in non-interest income. Service charges on deposit accounts increased \$54 thousand for the six-month period ending June 30, 2002 over the same period in 2001. This increase was due to increased fees charged on deposit accounts that became effective on April 1, 2001 and growth in deposit account activity during the first six months of 2002 over the first six months of 2001. Investment brokerage fees increased \$62 thousand, or 72.1%, from June 30, 2001 to June 30, 2002. In the first six months of 2002, a \$24 thousand gain on the sale of loans

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held for sale was recorded compared to a \$6 thousand gain on the sale of loans held for sale during the first six months of 2001.

Non-Interest Expense. For the quarter ended June 30, 2002, non-interest expense increased \$689 thousand from the same period last year. The additional non-interest expense in the second quarter 2002 attributed to Tri-State totaled \$388 thousand. Net of Tri-State's salaries and employee benefits, the Company's salaries and employee benefits increased \$119 thousand, or 15.8%, from the addition of three full time equivalent employees and normal salary increases since the quarter ended June 30, 2001. Other non-interest expense increases from second quarter 2001 to second quarter 2002, net of Tri-State's expenses, were advertising and promotion expenses of \$65 thousand due to the deposit promotion which began in the fourth quarter of 2001, furniture and equipment expense of \$43 thousand from computer network upgrades and costs associated with the Bank subsidiary name change from The Sussex County State Bank to Sussex Bank during fourth quarter 2001, and other expenses of \$46 thousand relative to normal expenditures attributed to the growth of the Company.

For the six months ended June 30, 2002, non-interest expense increased \$1.4 million, to \$4.1 million, of which \$754 thousand is attributable to Tri-State and which was not present during the first six months of 2001. Net of Tri-State, non-interest expenses increased \$600 thousand, or 21.6% to \$3.4 million for the first half of 2002 from \$ 2.8 million from the first half of 2001. Salaries and employee benefits increased \$242 thousand, or 16.2%, furniture and fixture expense increased \$85 thousand, or 27.4%, and advertising and promotions increased \$124 thousand, or 124.0% during the first six month of 2002 as compared to the first six months of 2001. As described in the second quarter analysis above, the same explanations for these increases carry forward for the first six months of 2002.

Income Taxes. Income tax expense increased \$37 thousand to \$144 thousand for the three months ended June 30, 2002 as compared to \$107 thousand for the same period in 2001. Income taxes also increased for the six months ended June 30, 2002 to \$237 thousand as compared to \$189 thousand for the six months ended June 30, 2001. The increase in income taxes resulted from a higher level of income before income taxes in 2002 compared to 2001.

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FINANCIAL CONDITION

June 30, 2002 as compared to December 31, 2001

Total assets increased to \$211.2 million at June 30, 2002, a \$7.9 million increase from total assets of \$203.3 million at December 31, 2001. Increases in total assets include net purchases of \$12.9 million in securities available for sale and \$3.0 million in time deposits in other banks. These asset increases were financed through a reduction in federal funds sold of \$13.7 million and an increase in total deposits of \$7.3 million from \$178.6 million at year-end 2001 to \$185.9 million on June 30, 2002. Total stockholder's equity increased \$600 thousand from \$12.2 million at December 31, 2001 to \$12.8 million at June 30, 2002.

Total loans at June 30, 2002 increased \$1.5 million to \$107.6 million from \$106.1 million at year-end 2001. The Company is emphasizing the origination of commercial, industrial, and non-residential real estate loans to increase the yield in its loan portfolio and reduce its dependence on loans secured by 1-4 family properties. The balance in non-residential real estate loans increased

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\$3.7 million from \$34.8 million at December 31, 2001 to \$38.5 million on June 30, 2002 and commercial and industrial loans increased \$1.1 million over the same six-month period. Construction loans have decreased \$2.5 million from \$8.5 million at December 31, 2001 to \$ 6.0 million on June 30, 2002. Other minor shifts in ending balances occurred between December 31, 2001 and March 31, 2002 according to loan demand.

The following schedule presents the components of loans, net of unearned income, for each period presented:

	June 30, 2002		December 31,
	Amount	Percent	Amount
(Dollars In Thousands)			
Commercial and Industrial	\$ 9,137	8.49%	\$ 8,065
Real Estate-Non Residential Properties	38,479	35.76%	34,811
Residential Properties (1-4 Family)	51,230	47.60%	51,433
Construction	6,046	5.62%	8,515
Loans to Individuals	2,091	1.94%	2,245
Other Loans	633	0.59%	1,079
	-----	-----	-----
 Total Loans	 \$107,616 =====	 100.00% =====	 \$106,148 =====

Federal funds sold decreased by \$13.7 million to \$21.2 million at June 30, 2001 from \$34.9 million on December 31, 2001. Despite the decline in the period end balances for federal funds sold, the average balance in federal funds sold for the first half of 2002 was \$27.6 million, an increase of \$9.5 million over the average balance of federal funds sold for the first half of 2001. During 2001 in a declining rate environment, deposits increased faster than investment opportunities and the excess funds were invested in short-term federal funds. These funds were used to purchase investment securities and time deposits in other banks during the first six months of 2002.

Securities, available for sale, at market value, increased \$12.9 million, or 30.3%, from \$42.7 million at year-end 2001 to \$55.6 million on June 30, 2002. The Company purchased \$24.6 million in new securities in the first six months of 2002 and \$11.8 million in available for sale securities matured, were called and were repaid. There were \$377 thousand in recorded unrealized gains in the available of sale portfolio and \$228 thousand in net amortization expenses during the first six months of 2002. There were no held to maturity securities at June 30, 2002 or at year-end 2001.

Total year to date average deposits increased \$15.1 million, or 9.1%, to \$181.2 million during the first six months of 2002 from the twelve-month average of \$166.1 million for the year ended December 31, 2001. NOW deposits increased by \$13.8 million, savings deposits increased by \$9.6 million, and demand deposits increased by \$1.5 million. Offsetting these increases were decreases in money market deposits of \$3.4 million and time deposits of \$6.4 million. As discussed earlier, the increase in demand, NOW and savings deposits was due to an ongoing deposit promotion since the forth quarter of 2001. After aggressively

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pricing time deposits in the first quarter of 2001, many of those deposits have since repriced in the first six months of 2002 at lower market rates of interest and the decrease in the average balance of time deposits reflects the withdrawal of some of the matured, higher priced time deposits. Management continues to monitor the shift in deposits through its Asset/Liability Committee.

The following schedule presents the components of deposits, for each period presented.

	Six Months Ended June 30, 2002		Twelve Months Ended December 31, 2001	
	Average Balance	Percent of Total	Average Balance	Percent of Total
Deposits:				
NOW Deposits	\$ 31,700	17.49%	\$ 17,885	10.76%
Savings Deposits	59,908	33.06%	50,334	30.30%
Money Market Deposits	3,642	2.01%	7,029	4.23%
Time Deposits	59,093	32.61%	65,486	39.42%
Demand Deposits	26,865	14.83%	25,412	15.29%
	-----	-----	-----	-----
Total Deposits	\$181,208	100.00%	\$166,146	100.00%
	=====	=====	=====	=====

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ASSET QUALITY

At June 30, 2002, non-performing loans decreased \$935 thousand to \$1.6 million, as compared to \$2.5 million at December 31, 2001. One construction credit with a value of \$1.5 million at December 31, 2001 was transferred to non-accrual during the third quarter of 2001. As of June 30, 2002 the construction credit has paid down and has a remaining balance of \$302 thousand. Management believes the Bank is adequately collateralized regarding this credit and does not anticipate a loss.

The following table provides information regarding risk elements in the loan portfolio:

	June 30, 2002	December 31, 2001
Non-accrual loans	\$ 1,559	\$ 2,494
Non-accrual loans to total loans	1.45%	2.35%
Non-performing loans to total assets	0.83%	1.32%
Allowance for loan losses as a percentage of non-performing loans	82.87%	45.83%
Allowance for loan losses to total loans	1.20%	1.08%

ALLOWANCE FOR LOAN LOSSES

The allowance for loan losses is maintained at a level considered adequate

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to provide for potential loan losses. The level of the allowance is based on management's evaluation of potential losses in the portfolio, after consideration of risk characteristics of the loans and prevailing and anticipated economic conditions. The allowance for loan losses is increased by provisions charged to expense and reduced by charge-offs, net of recoveries. Although management strives to maintain an allowance it deems adequate, future economic changes, deterioration of borrowers' credit worthiness, and the impact of examinations by regulatory agencies all could cause changes to the Company's allowance for loan losses.

At June 30, 2002, the allowance for possible loan losses was \$1.3 million, an increase of 13.0% from the \$1.1 million at year-end 2001. There were \$2 thousand in charge offs and \$1 thousand in recoveries reported in the first six months of 2002. The allowance for loan losses as a percentage of total loans was 1.20% at June 30, 2002 compared to 1.08% on December 31, 2001.

LIQUIDITY MANAGEMENT

At June 30, 2002, the amount of liquid assets remained at a level management deemed adequate to ensure that contractual liabilities, depositors' withdrawal requirements, and other operational and customer credit needs could be satisfied.

At June 30, 2002, liquid investments totaled \$31.7 million, and all mature within 30 days.

It is management's intent to fund future loan demand primarily with deposits. In addition, the Bank is a member of the Federal Home Loan Bank of New York and as of June 30, 2002, had the ability to borrow a total of \$23.0 million against its one to four family mortgages as collateral for long term advances. The Bank also has available an overnight line of credit in the amount of \$7.9 million. In December of 2000 the Company borrowed against its one to four family mortgages and entered into three long term FHLB advances totaling \$10 million. The three borrowings, which have an average interest rate of 4.95%, mature on December 21, 2010, but are callable beginning in December 2001, 2002 and 2003, respectively. These borrowings were used to restructure maturing short-term debt of \$4 million and make available funds to purchase higher yielding investments.

CAPITAL RESOURCES

Total stockholders' equity increased to \$12.8 million at June 30, 2002 from \$12.2 million at year-end 2001. Activity in stockholder's equity consisted of a net increase in retained earnings of \$362 thousand derived from \$562 thousand in net income earned during the first half of 2002, offset by \$200 thousand in payments for cash dividends. Unrealized gain on securities, available for sale of \$224 thousand, \$25 thousand in stock options exercised and \$60 thousand for shares issued through the dividend reinvestment plan were increases to stockholder's equity, offset by treasury stock purchases of \$105 thousand.

Subsequent to June 30, 2002, the Company raised an additional \$4.8 million, net of offering costs, in tier 1 capital through the issuance of junior subordinated debentures to a statutory trust subsidiary. The subsidiary in turn issued \$5.0 million in variable rate capital trust pass through securities to investors in a private placement. The securities bear an initial rate of 5.51%, which will be adjusted quarterly. The interest rate will be reset based on the three month LIBOR rate plus 365 basis points. The rate is capped at 12.5% through the first five years, and the securities may be called at par any time after October 7, 2007.

At June 30, 2002 each of the Company and the Bank exceeded each of the regulatory capital requirements applicable to it. The table below presents the

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capital ratios at June 30, 2002 for both the Company and the Bank as well as the minimum regulatory requirements.

	Amount -----	Ratio -----	Amount -----	Minimum Ratio -----
The Company:				
Leverage Capital	\$10,007	4.86%	\$ 8,234	4%
Tier 1 - Risk				
Based	10,007	8.36%	4,788	4%
Total Risk-Based	11,299	9.44%	9,577	8%
The Bank:				
Leverage Capital	9,670	4.70%	8,232	4%
Tier 1				
Risk-Based	9,670	8.10%	4,778	4%
Total Risk-Based	10,962	9.18%	9,556	8%

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Part II Other Information

Item 1. Legal Proceedings

The Company and the Bank are periodically involved in various legal proceedings as a normal incident to their businesses. In the opinion of management, no material loss is expected from any such pending lawsuit.

Item 2. Changes in Securities

Not applicable

Item 3. Defaults Upon Served Securities

Not applicable

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

On April 24, 2002, the Registrant held its annual meeting of shareholders to elect members of the Company's Board of Directors whose terms expired. Nominees for election to the Board of Directors received the following votes:

Nominees: -----	For ---	Withhold Authority -----
Richard Scott	1,387,015	4,125
Joseph Zitone	1,387,251	3,890

Item 5. Other Information

On July 11, 2002 Sussex Capital Trust I, a Delaware statutory business trust and a wholly-owned subsidiary of the Company, issued \$5 million of

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variable rate capital trust pass-through securities to investors. Sussex Capital Trust I purchased \$5.1 million of variable rate junior subordinated deferrable interest debentures from Sussex Bancorp. The debentures are the sole asset of the Trust. The terms of the junior subordinated debentures are the same as the terms of the capital securities. Sussex Bancorp has also fully and unconditionally guaranteed the obligations of the Trust under the capital securities. The capital securities are redeemable by Sussex Bancorp on or after October 7, 2007, at par or earlier if the deduction of related interest for federal income taxes is prohibited, classification as Tier I Capital is no longer allowed, or certain other contingencies arise. The capital securities must be redeemed upon final maturity of the subordinated debentures on October 7, 2032. Proceeds totaling approximately \$4.8 million were moved to paid in capital at Sussex Bank. Financing costs related to the Company's issuance of mandatory redeemable capital debentures will be amortized over a five-year period and will be included in other assets. After giving effect to the capital contribution, on a pro forma basis, the Company would have had a leverage ratio of 6.88%, a tier I risk based capital ratio of 11.82% and a total risk based capital ratio of 13.62% and the Bank would have had a leverage ratio of 7.03%, a tier I risk based capital ratio of 12.11% and a total risk based capital ratio of 13.20%, all in excess of the ratio's required to be deemed "well capitalized" for regulatory purposes.

Item 6. Exhibits and Report on form 8-K

(a). Exhibits

Number	Description
99	Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

(b). Reports on Form 8-K

Filing Date	Item Number	Description
April 23, 2002	4	The Registrant announced that it had replaced Arthur Andersen, LLP as its independent auditors with Beard Miller Company LLP.

SIGNATURE

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.

SUSSEX BANCORP

Date:

By: /s/ Candace A. Leatham

 CANDACE A. LEATHAM
 Senior Vice President and

