1ST CONSTITUTION BANCORP
Form 10-K
April 02, 2007

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-K

(Mark One)
x ANNUAL REPORT UNDER SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2006

o TRANSITION REPORT UNDER SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from ________ to _______

Commission file Number: 000-32891

1ST CONSTITUTION BANCORP
(Exact Name of Registrant as Specified in Its Charter)

New Jersey	22-3665653
(State or Other Jurisdiction of Incorporation or Organization)	IRS Employer Identification Number)

2650 Route 130, P.O. Box 634, Cranbury, NJ 08512
(Address of Principal Executive Offices, including Zip Code)

(609) 655-4500
(Registrant's telephone number, including area code)

SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT:

Common Stock, No Par Value

SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE ACT:

Stock Purchase Rights Relating to Common Stock, No Par Value
(Title of Class)

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

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

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

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

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

Large accelerated filer o Accelerated filer o Non-accelerated filer x

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

The aggregate market value of the registrant's common stock held by non-affiliates of the registrant, computed by reference to the price at which the common stock was last sold, or the average bid and asked price of such common stock, as of the last business day of the registrant's most recently completed second quarter, is $57,045,025.

As of March 13, 2007, 3,742,662 shares of the registrant's common stock were outstanding.

Portions of the registrant's definitive Proxy Statement for its 2007 Annual Meeting of Shareholders are incorporated by reference into Part III of this report.

FORM 10-K

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PART I

Item 1. Business.

1st Constitution Bancorp

1st Constitution Bancorp (the "Company") is a bank holding company registered under the Bank Holding Company Act of 1956, as amended. The Company was organized under the laws of the State of New Jersey in February 1999 for the purpose of acquiring all of the issued and outstanding stock of 1st Constitution Bank (the "Bank") and thereby enabling the Bank to operate within a bank holding company structure. The Company became an active bank holding company on July 1, 1999. The Bank is a wholly-owned subsidiary of the Company. Other than its investment in the Bank, the Company currently conducts no other significant business activities.

As of December 31, 2006, the Company, on a consolidated basis, had total assets of approximately $392.7 million, total deposits of approximately $312.7 million, total gross loans of approximately $265.1 million and total shareholders' equity of approximately $35.2 million.

The main office of the Company and the Bank is located at 2650 Route 130 North, Cranbury, New Jersey 08512, and the telephone number is (609) 655-4500.

1st Constitution Bank

The Bank, a commercial bank formed under the laws of the State of New Jersey, engages in the business of commercial and retail banking. As a community bank, the Bank offers a wide range of services (including demand, savings and time deposits and commercial and consumer/installment loans) to individuals, small businesses and not-for-profit organizations principally in Middlesex, Mercer and Somerset Counties, New Jersey. The Bank conducts its operations through its main office located in Cranbury, New Jersey, and operates nine additional branch offices in downtown Cranbury, Hamilton Square, Jamesburg, Montgomery, Perth Amboy, Plainsboro, West Windsor, Fort Lee and Princeton, New Jersey. The Bank's deposits are insured up to applicable legal limits by the Federal Deposit Insurance Corporation ("FDIC").

Management efforts focus on positioning the Bank to meet the financial needs of the communities in Middlesex, Mercer and Somerset Counties and the Fort Lee area of Bergen County and to provide financial services to individuals, families, institutions and small businesses. To achieve this goal, the Bank is focusing its efforts on:

- personal service;

- expansion of its branch network;

- innovative product offerings; and

- technological advances and e-commerce.

Personal Service

The Bank provides a wide range of commercial and consumer banking services to individuals, families, institutions and small businesses in central New Jersey and the Fort Lee area of Bergen County. The Bank's focus is to understand the needs of the community and the customers and tailor products, services and advice to meet those needs. The Bank seeks to provide a high level of personalized banking services, emphasizing quick and flexible responses to customer demands.

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Expansion of Branch Banking

The Bank continually evaluates opportunities for branch bank expansion, either mini branches or full service banks, to continue to grow and meet the needs of the community. During the third quarter of 2006, the Bank relocated its Plainsboro branch office from 10 Schalks Crossing Road to 11 Schalks Crossing Road and opened a new branch office at 180 Main Street, Fort Lee, Bergen County, New Jersey. During the fourth quarter of 2006, the Bank announced that it had entered into a Purchase and Assumption Agreement to acquire all of the deposit liabilities and related assets of the Hightstown, New Jersey branch banking office of Sun National Bank. Pending the receipt of regulatory agency approvals, the transaction is scheduled to close during the first quarter of 2007.

Innovative Product Offerings

In the fourth quarter of 2006, the Bank launched its new EZ Deposit service. This new product allows customers of the Bank to scan checks, using a scanning device furnished by the Bank, at the customer's place of business and transmit them directly to the Bank for deposit into the customer's account. The Check 21 Act allows for the creation of Image Replacement Documents ("IRD") that are the legal equivalent of the original check. Therefore, the check images captured at customer locations are sent electronically to the Bank and customers can reduce the number of trips to the Bank, as deposits are made directly from their place of business to the Bank. The service also has a later deposit time cutoff than branch locations and this allows customers to process deposits and have them posted the same day rather than the following business day.

By the end of 2006, there were 13 EZ Deposit customers using the service and a number of customers requesting the service in 2007. Management believes that there is great customer acceptance of this service and that the demand for this service will be strong in 2007.

Technological Advances and e-Commerce

The Bank recognizes that customers want to receive service via their most convenient delivery channel, be it the traditional branch office, by telephone, ATM, or the internet. For this reason, the Bank continues to enhance its e-commerce capabilities. At www.1stconstitution.com, customers have easy access to online banking, including account access, and to the Bank's bill payment system. Consumers can apply online for loans and interact with senior management through the e-mail system. Business customers have access to cash management information and transaction capability through the Bank's online Business Express product offering. This overall expansion in electronic banking offers the Bank's customers another means to access the Bank's services easily and at their own convenience.

Competition

The Bank experiences substantial competition in attracting and retaining deposits and in making loans. In attracting deposits and borrowers, the Bank competes with commercial banks, savings banks, and savings and loan associations, as well as regional and national insurance companies and non-bank financial institutions, regulated small loan companies and local credit unions, regional and national issuers of money market funds and corporate and government borrowers. Within the direct market area of the Bank, there are a significant number of offices of competing financial institutions. In New Jersey generally, and in the Bank's local market specifically, large commercial banks, as well as savings banks and savings and loan associations, including Provident Savings Bank and Hudson City Savings Bank, hold a dominant market share and there has been significant merger activity in the last few years, creating even larger competitors.

Locally, the Bank's most direct competitors include Bank of America, PNC Bank, Wachovia Bank, and Sovereign Bank. The Bank is at a competitive disadvantage compared with these larger national and regional commercial and savings banks. By virtue of their larger capital, asset size or reserves, many of such institutions have substantially

greater lending limits (ceilings on the amount of credit a bank may provide to a single customer that are linked to the institution's capital) and other resources than the Bank. Many such institutions are empowered to offer a wider range of services, including trust services, than the Bank and, in some cases, have lower funding costs (the price a bank must pay for deposits and other borrowed monies used to make loans to customers) than the Bank. In addition to having established deposit bases and loan portfolios, these institutions, particularly large national and regional commercial and savings banks, have the financial ability to finance extensive advertising campaigns and to allocate considerable resources to locations and products perceived as profitable.

In addition, non-bank financial institutions offer services that compete for deposits with the Bank. For example, brokerage firms and insurance companies offer such instruments as short-term money market funds, corporate and government securities funds, mutual funds and annuities. It is expected that competition in these areas will continue to increase. Some of these competitors are not subject to the same degree of regulation and supervision as the Company and the Bank and therefore may be able to offer customers more attractive products than the Bank.

However, management of the Bank believes that loans to small and mid-sized businesses and professionals, which represent the main commercial loan business of the Bank, are not always of primary importance to the larger banking institutions. The Bank competes for this segment of the market by providing responsive personalized services, local decision-making, and knowledge of its customers and their businesses.

Lending Activities

The Bank’s lending activities include both commercial and consumer loans. Loan originations are derived from a number of sources including real estate broker referrals, mortgage loan companies, direct solicitation by the Bank’s loan officers, existing depositors and borrowers, builders, attorneys, walk-in customers and, in some instances, other lenders. The Bank has established disciplined and systematic procedures for approving and monitoring loans that vary depending on the size and nature of the loan.

Commercial Lending

The Bank offers a variety of commercial loan services including term loans, lines of credit, and loans secured by equipment and receivables. A broad range of short-to-medium term commercial loans, both secured and unsecured, are made available to businesses for working capital (including inventory and receivables), business expansion (including acquisition and development of real estate and improvements), and the purchase of equipment and machinery. The Bank also makes construction loans to real estate developers for the acquisition, development and construction of residential subdivisions.

Commercial loans are granted based on the borrower’s ability to generate cash flow to support its debt obligations and other cash related expenses. A borrower’s ability to repay commercial loans is substantially dependent on the success of the business itself and on the quality of its management. As a general practice, the Bank takes as collateral a security interest in any available real estate, equipment, inventory, receivables or other personal property of its borrowers, although occasionally the Bank makes commercial loans on an unsecured basis. Generally, the Bank requires personal guaranties of its commercial loans to offset the risks associated with such loans.

Residential Consumer Lending

A portion of the Bank’s lending activities consists of the origination of fixed and adjustable rate residential first mortgage loans secured by owner-occupied property located in the Bank’s primary market areas. Home mortgage lending is unique in that a broad geographic territory may be serviced by originators working from strategically placed offices either within the Bank’s traditional banking facilities or from affordable storefront locations in commercial buildings. The Bank also offers construction loans, second mortgage home improvement loans and home equity lines of credit.

The Bank finances the construction of individual, owner-occupied houses on the basis of written underwriting and construction loan management guidelines. First mortgage construction loans are made to contractors secured by real estate that is both a pre-sold and a “speculation” basis. Such loans are also made to qualified individual borrowers and are generally supported by a take-out commitment from a permanent lender. The Bank makes residential construction loans to individuals who intend to erect owner occupied housing on a purchased parcel of real estate. The construction phase of these loans has certain risks, including the viability of the contractor, the contractor’s ability to complete the project and changes in interest rates.

In most cases, the Bank will sell its mortgage loans with terms of 15 years or more in the secondary market. The sale to the secondary market allows the Bank to hedge against the interest rate risks related to such lending operations. This brokerage arrangement allows the Bank to accommodate its clients' demands while eliminating the interest rate risk for the 15- to 30- year period generally associated with such loans.

The Bank in most cases requires borrowers to obtain and maintain title, fire, and extended casualty insurance, and, where required by applicable regulations, flood insurance. The Bank maintains its own errors and omissions insurance policy to protect against loss in the event of failure of a mortgagor to pay premiums on fire and other hazard insurance policies. Mortgage loans originated by the Bank customarily include a "due on sale" clause, which gives the Bank the right to declare a loan immediately due and payable in certain circumstances, including, without limitation, upon the sale or other disposition by the borrower of the real property subject to a mortgage. In general, the Bank enforces due on sale clauses. Borrowers are typically permitted to refinance or repay loans at their option without penalty.

Non-Residential Consumer Lending

Non-residential consumer loans made by the Bank include loans for automobiles, recreation vehicles, and boats, as well as personal loans (secured and unsecured) and deposit account secured loans. The Bank also conducts various indirect lending activities through established retail companies in its market areas. Non-residential consumer loans are attractive to the Bank because they typically have a shorter term and carry higher interest rates than are charged on other types of loans. Non-residential consumer loans, however, do pose additional risk of collectibility when compared to traditional types of loans, such as residential mortgage loans granted by commercial banks.

Consumer loans are granted based on employment and financial information solicited from prospective borrowers as well as credit records collected from various reporting agencies. Stability of the borrower, willingness to pay and credit history are the primary factors to be considered. The availability of collateral is also a factor considered in making such a loan. The Bank seeks collateral that can be assigned and has good marketability with a clearly adequate margin of value. The geographic area of the borrower is another consideration, with preference given to borrowers in the Bank's primary market areas.

Supervision and Regulation

Banking is a complex, highly regulated industry. The primary goals of the bank regulatory scheme are to maintain a safe and sound banking system and to facilitate the conduct of monetary policy. In furtherance of those goals, Congress has created several largely autonomous regulatory agencies and enacted a myriad of legislation that governs banks, bank holding companies and the banking industry. This regulatory framework is intended primarily for the protection of depositors and not for the protection of the Company's shareholders. Descriptions of, and references to, the statutes and regulations below are brief summaries thereof, and do not purport to be complete. The descriptions are qualified in their entirety by reference to the specific statutes and regulations discussed.

State and Federal Regulations

The Company is a bank holding company within the meaning of the Bank Holding Company Act of 1956, as amended (the "BHCA"). As a bank holding company, the Company is subject to inspection, examination and supervision by the Board of Governors of the Federal Reserve System (the "Federal Reserve Board") and is required to file with the Federal Reserve Board an annual report and such additional information as the Federal Reserve Board may require pursuant to the BHCA. The Federal Reserve Board may also make examinations of the Company and its subsidiaries. The Company is subject to capital standards similar to, but separate from, those applicable to the Bank.

Under the BHCA, bank holding companies that are not financial holding companies generally may not acquire the ownership or control of more than 5% of the voting shares, or substantially all the assets, of any company, including a bank or another bank holding company, without the Federal Reserve Board's prior approval. The Company has not applied to become a financial holding company but did obtain such approval to acquire the shares of the Bank. A bank holding company that does not qualify as a financial holding company is generally limited in the types of activities in which it may engage to those that the Federal Reserve Board had recognized as permissible for bank holding companies prior to the date of enactment of the Gramm-Leach-Bliley Financial Services Modernization Act of 1999. For example, a holding company and its banking subsidiary are prohibited from engaging in certain tie-in arrangements in connection with any extension of credit or lease or sale of any property or the furnishing of services. At present, the Company does not engage in any significant activity other than owning the Bank.

In addition to federal bank holding company regulation, the Company is registered as a bank holding company with the New Jersey Department of Banking and Insurance (the "Department"). The Company is required to file with the Department copies of the reports it files with the federal banking and securities regulators.

Capital Adequacy

The Company is required to comply with minimum capital adequacy standards established by the Federal Reserve Board. There are two basic measures of capital adequacy for bank holding companies and the depository institutions that they own: a risk based measure and a leverage measure. All applicable capital standards must be satisfied for a bank holding company to be considered in compliance.

The Federal Deposit Insurance Corporation Improvement Act of 1991 ("FDICIA") required each federal banking agency to revise its risk-based capital standards to ensure that those standards take adequate account of interest rate risk, concentration of credit risk and the risks of non-traditional activities. In addition, pursuant to FDICIA, each federal banking agency has promulgated regulations, specifying the levels at which a bank would be considered "well capitalized," "adequately capitalized," "undercapitalized," "significantly undercapitalized," or "critically undercapitalized," ar to take certain mandatory and discretionary supervisory actions based on the capital level of the institution.

The regulations implementing these provisions of FDICIA provide that a bank will be classified as "well capitalized" if it (i) has a total risk-based capital ratio of at least 10.0 percent, (ii) has a Tier 1 risk-based capital ratio of at least 6.0 percent, (iii) has a Tier 1 leverage ratio of at least 5.0 percent, and (iv) meets certain other requirements. A bank will be classified as "adequately capitalized" if it (i) has a total risk-based capital ratio of at least 8.0 percent, (ii) has a Tier 1 risk-based capital ratio of at least 4.0 percent, (iii) has a Tier 1 leverage ratio of (a) at least 4.0 percent, or (b) at least 3.0 percent if the institution was rated 1 in its most recent examination and is not experiencing or anticipating significant growth, and (iv) does not meet the definition of "well capitalized." A bank will be classified as "undercapitalized" if it (i) has a total risk-based capital ratio of less than 8.0 percent, (ii) has a Tier 1 risk-based capital ratio of less than 4.0 percent, or (iii) has a Tier 1 leverage ratio of (a) less than 4.0 percent, or (b) less than 3.0 percent if the institution was rated 1 in its most recent examination and is not experiencing or anticipating significant growth. A bank will be classified as "significantly undercapitalized" if it (i) has a total risk-based capital ratio of less than 6.0 percent, (ii) has a Tier 1 risk-based capital ratio of less than 3.0 percent, or (iii) has a Tier 1 leverage ratio of less than 3.0 percent. An institution will be classified as "critically undercapitalized" if it has a tangible equity to total assets ratio that is equal to or less than 2.0 percent. An insured depository institution may be deemed to be in a lower capitalization category if it receives an unsatisfactory examination.

As of December 31, 2006, the Bank's capital ratios exceed the requirements to be considered a well capitalized institution under these regulations.

The risk-based capital guidelines for bank holding companies such as the Company currently require a minimum ratio of total capital to risk-weighted assets (including off-balance sheet activities, such as standby letters of credit) of 8%.

At least half of the total capital is required to be Tier 1 capital, consisting principally of common shareholders' equity, non-cumulative perpetual preferred stock, a limited amount of cumulative perpetual preferred stock and minority interest in the equity accounts of consolidated subsidiaries, less goodwill. The remainder of the total capital (Tier 2 capital) may consist of a limited amount of subordinated debt and intermediate-term preferred stock, certain hybrid capital instruments and other debt securities, perpetual preferred stock and a limited amount of the general loan loss allowance. At December 31, 2006, the Company maintained a Tier 1 capital ratio of 15.42% and total qualifying capital ratio of 20.23%.

In addition to the risk-based capital guidelines, the federal banking regulators established minimum leverage ratio (Tier 1 capital to total assets) guidelines for bank holding companies. These guidelines provide for a minimum leverage ratio of 3% for those bank holding companies which have the highest regulatory examination ratings and are not contemplating or experiencing significant growth or expansion. All other bank holding companies are required to maintain a leverage ratio of at least 1% to 2% above the 3% stated minimum. The Company's leverage ratio at December 31, 2006 was 12.18%.

On April 10, 2002, 1ST Constitution Capital Trust I ("Trust I"), a statutory business trust and a wholly owned subsidiary of the Company, issued $5.0 million of variable rate Trust Preferred Securities in a pooled institutional placement transaction maturing April 22, 2032. These Subordinated Debentures constitute the sole assets of Trust I. These Subordinated Debentures are redeemable in whole or part prior to maturity after April 22, 2007. Trust I is obligated to distribute all proceeds of a redemption of these Subordinated Debentures, whether voluntary or upon maturity, to holders of the Trust Preferred Securities. The Company's obligation with respect to the Trust Preferred Securities and the Subordinated Debentures, when taken together, provides a full and unconditional guarantee on a subordinated basis by the Company of the obligations of Trust I to pay amounts when due on the Trust Preferred Securities. On February 23, 2007, the Company notified Wilmington Trust Company, as Indenture Trustee, of the Company's intention to redeem on April 22, 2007 the debt securities issued by the Company to Trust I.

On May 30, 2006, 1ST Constitution Bancorp established 1ST Constitution Capital Trust II, a Delaware business trust subsidiary ("Trust II"), for the sole purpose of issuing $18 million of trust preferred securities (the "Capital Securities"). The Capital Securities were issued in connection with a pooled offering involving approximately 50 other financial institution holding companies. All of the Capital Securities were sold to a single pooling vehicle. The proceeds from the sale of the Capital Securities were loaned to the Company under 30-year floating rate junior subordinated debentures issued to Trust II by the Company. The debentures are the only asset of Trust II. Interest payments on the debentures flow through Trust II to the pooling vehicle. Payments of distributions by Trust II to the pooling vehicle are guaranteed by the Company.

Management has determined that Trust I and Trust II (together the "Trusts") qualify as variable interest entities under FASB Interpretation 46 ("FIN 46"). The Trusts issued mandatorily redeemable preferred stock to investors and loaned the proceeds to the Company. Each of the Trusts holds, as its sole asset, subordinated debentures issued by the Company. Subsequent to the issuance of FIN 46 and the establishment of Trust I, the FASB issued a revised interpretation, FIN 46(R), the provisions of which were required to be applied to certain variable interest entities, including Trust I, by March 31, 2004, at which time Trust I was deconsolidated.

In March 2005, the Federal Reserve Board adopted a final rule that would continue to allow the inclusion of trust preferred securities of the kind issued by the Trusts in Tier 1 capital, but with stricter quantitative limits. Under the final rule, after a five-year transition period, the aggregate amount of trust preferred securities and certain other capital elements would be limited to 25% of Tier 1 capital elements, net of goodwill. The amount of trust preferred securities and certain other elements in excess of the limit could be included in Tier 2 capital, subject to restrictions. Based on the final rule, the Company included all of its $23.7 million in trust preferred securities in Tier 1 capital at December 31, 2006. Management has evaluated the effects of the final rule and does not anticipate a material impact on its capital ratios by the end of the transition period.

Restrictions on Dividends

The primary source of cash to pay dividends, if any, to the Company's shareholders and to meet the Company's obligations is dividends paid to the Company by the Bank. Dividend payments by the Bank to the Company are subject to the New Jersey Banking Act of 1948 (the "Banking Act") and the Federal Deposit Insurance Act (the "FDIA"). Under the Banking Act and the FDIA, the Bank may not pay any dividends if after paying the dividend, it would be undercapitalized under applicable capital requirements. In addition to these explicit limitations, the federal regulatory agencies are authorized to prohibit a banking subsidiary or bank holding company from engaging in an unsafe or

unsound banking practice. Depending upon the circumstances, the agencies could take the position that paying a dividend would constitute an unsafe or unsound banking practice.

It is the policy of the Federal Reserve Board that bank holding companies should pay cash dividends on common stock only out of income available over the immediately preceding year and only if prospective earnings retention is consistent with the organization's expected future needs and financial condition. The policy provides that bank holding companies should not maintain a level of cash dividend that undermines the bank holding company's ability to serve as a source of strength to its banking subsidiary. A bank holding company may not pay dividends when it is insolvent.

The Company has never paid a cash dividend and the Company's Board of Directors has no plans to pay a cash dividend in the foreseeable future. The Bank paid a stock dividend every year from 1993 to 1999, when it was acquired by the Company. The Company has paid a stock dividend every year since its formation in 1999. From 1999 through 2006, the Company paid a 5% stock dividend each year. On December 21, 2006, the Company declared a 6% stock dividend, which was paid on January 31, 2007 to shareholders of record as of the close of business on January 23, 2007. The Company also declared a two-for-one stock split on January 20, 2005, which was paid on February 28, 2005 to shareholders of record on February 10, 2005. All share and per share data has been retroactively adjusted for stock dividends.

Priority on Liquidation

The Company is a legal entity separate and distinct from the Bank. The rights of the Company as the sole shareholder of the Bank, and therefore the rights of the Company's creditors and shareholders, to participate in the distributions and earnings of the Bank when the Bank is not in bankruptcy, are subject to various state and federal law restrictions as discussed above under the heading "Restrictions of Dividends." In the event of a liquidation or other resolution of an insured depository institution such as the Bank, the claims of depositors and other general or subordinated creditors are entitled to a priority of payment over the claims of holders of an obligation of the institution to its shareholders (the Company) or any shareholder or creditor of the Company. The claims on the Bank by creditors include obligations in respect of federal funds purchased and certain other borrowings, as well as deposit liabilities.

Financial Institution Legislation

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

- allows bank holding companies meeting management, capital and Community Reinvestment Act standards to engage in a substantially broader range of non-banking activities than is permissible for a bank holding company, including insurance underwriting and making merchant banking investments in commercial and financial companies; if a bank holding company elects to become a financial holding company, it files a certification, effective in 30 days, and thereafter may engage in certain financial activities without further approvals;

- allows banks to establish subsidiaries to engage in certain activities which a financial holding company could engage in, if the bank meets certain management, capital and Community Reinvestment Act standards;

- allows insurers and other financial services companies to acquire banks and removes various restrictions that currently apply to bank holding company ownership of securities firms and mutual fund advisory companies; and establishes the overall regulatory structure applicable to financial holding companies that also engage in insurance and securities operations.

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

The Modernization Act also amends the BHCA and the Bank Merger Act to require the federal banking agencies to consider the effectiveness of a financial institution's anti-money laundering activities when reviewing an application under these acts.

Additional proposals to change the laws and regulations governing the banking and financial services industry are frequently introduced in Congress, in the state legislatures and before the various bank regulatory agencies. The likelihood and timing of any such changes and the impact such changes might have on the Company cannot be determined at this time.

The Sarbanes-Oxley Act of 2002 ("Sarbanes-Oxley Act"), which became law on July 30, 2002, added new legal requirements affecting corporate governance, accounting and corporate reporting for companies with publicly traded securities.

The Sarbanes-Oxley Act provides for, among other things:

· a prohibition on personal loans made or arranged by the issuer to its directors and executive officers (except for loans made by a bank subject to Regulation O);

· independence requirements for audit committee members;

· disclosure of whether at least one member of the audit committee is a "financial expert" (as such term is defined by the SEC) and if not, why not;

· independence requirements for outside auditors;

· a prohibition by a company's registered public accounting firm from performing statutorily mandated audit services for the company if the company's chief executive officer, chief financial officer, comptroller, chief accounting officer or any person serving in equivalent positions had been employed by such firm and participated in the audit of such company during the one-year period preceding the audit initiation date;

· certification of financial statements and reports on Forms 10-K, 10-KSB, 10-Q, and 10-QSB by the chief executive officer and the chief financial officer;

· the forfeiture of bonuses or other incentive-based compensation and profits from the sale of an issuer's securities by directors and senior officers in the twelve month period following initial publication of any financial statements that later require restatement due to corporate misconduct;

· disclosure of off-balance sheet transactions;

· two-business day filing requirements for insiders filing Forms 4;

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

· "real time" filing of periodic reports;

· posting of certain SEC filings and other information on the company website;

· the reporting of securities violations "up the ladder" by both in-house and outside attorneys;

· restrictions on the use of non-GAAP financial measures;

- the formation of a public accounting oversight board; and
- various increased criminal penalties for violations of securities laws.

Additionally, Section 404 of the Sarbanes-Oxley Act requires that a public company subject to the reporting requirements of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), include in its annual report (i) a management’s report on internal control over financial reporting assessing the company’s internal controls, and (ii) an auditor’s attestation report, completed by the registered public accounting firm that prepares or issues an accountant’s report which is included in the company’s annual report, attesting to the effectiveness of management’s internal control assessment. Because we are neither a “large accelerated filer” nor an “accelerated filer”, under current rules, we are not required to provide management’s report on internal control over financial reporting until we file our annual report for 2007 and compliance with the auditor’s attestation report requirement is not required until we file our annual report for 2008.

Each of the national stock exchanges, including the Nasdaq Global Market where the Company’s common stock is listed, have implemented new corporate governance rules, including rules strengthening director independence requirements for boards, and the adoption of charters for the nominating, corporate governance, and audit committees. The rule changes are intended to, among other things, make the board of directors independent of management and allow shareholders to more easily and efficiently monitor the performance of companies and directors. These increased burdens have increased the Company’s legal and accounting fees and the amount of time that the Board of Directors and management must devote to corporate governance issues.

Effective August 29, 2002, as directed by Section 302(a) of Sarbanes-Oxley, the Company’s chief executive officer and chief financial officer are each required to certify that the Company’s Quarterly and Annual Reports do not contain any untrue statement of a material fact. The rules have several requirements, including having these officers certify that: they are responsible for establishing, maintaining and regularly evaluating the effectiveness of the Company’s internal controls; they have made certain disclosures to the Company’s auditors and the audit committee of the Board of Directors about the Company’s internal controls; and they have included information in the Company’s Quarterly and Annual Reports about their evaluation and whether there have been significant changes in the Company’s internal controls or in other factors that could significantly affect internal controls subsequent to the evaluation.

As part of the USA Patriot Act, signed into law on October 26, 2001, Congress adopted the International Money Laundering Abatement and Financial Anti-Terrorism Act of 2001 (the “Act”). The Act authorizes the Secretary of the Treasury, in consultation with the heads of other government agencies, to adopt special measures applicable to financial institutions such as banks, bank holding companies, broker-dealers and insurance companies. Among its other provisions, the Act requires each financial institution: (i) to establish an anti-money laundering program; (ii) to establish due diligence policies, procedures and controls that are reasonably designed to detect and report instances of money laundering in United States private banking accounts and correspondent accounts maintained for non-United States persons or their representatives; and (iii) to avoid establishing, maintaining, administering, or managing correspondent accounts in the United States for, or on behalf of, a foreign shell bank that does not have a physical presence in any country. In addition, the Act expands the circumstances under which funds in a bank account may be forfeited and requires covered financial institutions to respond under certain circumstances to requests for information from federal banking agencies within 120 hours.

The Department of Treasury has issued regulations implementing the due diligence requirements. These regulations require minimum standards to verify customer identity and maintain accurate records, encourages cooperation among financial institutions, federal banking agencies, and law enforcement authorities regarding possible money laundering or terrorist activities, prohibits the anonymous use of “concentration accounts,” and requires all covered financial institutions to have in place an anti-money laundering compliance program.

The Bank, a New Jersey-chartered commercial bank, is subject to supervision and examination by the New Jersey Department of Banking and Insurance. The Bank is also subject to regulation by the FDIC, which is its principal federal bank regulator.

The Bank must comply with various requirements and restrictions under federal and state law, including the maintenance of reserves against deposits, restrictions on the types and amounts of loans that may be granted and the interest that may be charged thereon, limitations on the types of investments that may be made and the services that may be offered, and restrictions on dividends as described in the preceding section. Consumer laws and regulations also affect the operations of the Bank. In addition to the impact of regulation, commercial banks are affected significantly by the actions of the Federal Reserve Board which influence the money supply and credit availability in the national economy.

Community Reinvestment Act

Under the Community Reinvestment Act ("CRA"), as implemented by FDIC regulations, a bank has a continuing and affirmative obligation, consistent with its safe and sound operation, to help meet the credit needs of its entire community, including low- and moderate-income neighborhoods. CRA does not establish specific lending requirements or programs for financial institutions nor does it limit an institution's discretion to develop the types of products and services that it believes are best suited to its particular community, consistent with CRA. CRA requires the FDIC to assess an institution's record of meeting the credit needs of its community and to take such record into account in its evaluation of certain applications by the applicable institution. The CRA requires public disclosure of an institution's CRA rating and requires that the FDIC provide a written evaluation of an institution's CRA performance utilizing a four-tiered descriptive rating system. An institution's CRA rating is considered in determining whether to grant charters, branches and other deposit facilities, relocations, mergers, consolidations and acquisitions. Performance less than satisfactory may be the basis for denying an application. At its last CRA examination, the Bank was rated "satisfactory" under CRA.

Insurance of Deposits

The Bank's deposits are insured up to a maximum of $100,000 per depositor under the Deposit Insurance Fund. The FDICIA is applicable to depository institutions and deposit insurance. The FDICIA requires the FDIC to establish a risk-based assessment system for all insured depository institutions. Under this legislation, the FDIC is required to establish an insurance premium assessment system based upon: (i) the probability that the insurance fund will incur a loss with respect to the institution, (ii) the likely amount of the loss, and (iii) the revenue needs of the insurance fund. In compliance with this mandate, the FDIC has developed a matrix that sets the assessment premium for a particular institution in accordance with its capital level and overall rating by the primary regulator. Under the matrix as currently in effect, the assessment rate ranges from 0 to 27 basis points of assessed deposits. The Bank is also subject to a quarterly FICO assessment.

Employees

The Company has two paid employees. Banking operations are conducted by the Bank, and as of December 31, 2006, the Bank had 88 full-time employees and 12 part-time employees. Neither the Bank's nor the Company's employees are represented by any collective bargaining group. The Bank and the Company each considers its relations with such employees to be good.

Forward Looking Statements

When used in this and in future filings by the Company with the Securities and Exchange Commission, in the Company's press releases and in oral statements made with the approval of an authorized executive officer of the Company, the words or phrases "will," "will likely result," "could," "anticipates," "believes," "continues," "expects," "pla continue," "is anticipated," "estimated," "project" or "outlook" or similar expressions (including confirmations by an authorize executive officer of the Company of any such expressions made by a third party with respect to the Company) are intended to identify forward-looking statements. The Company wishes to caution readers not to place undue reliance on any such forward-looking statements, each of which speak only as of the date made. Such statements are subject to

certain risks and uncertainties that could cause actual results to differ materially from historical earnings and those presently anticipated or projected.

Factors that may cause actual results to differ from those results expressed or implied, include, but are not limited to, those listed below under "Risk Factors"; the overall economy and the interest rate environment; the ability of customers to repay their obligations; the adequacy of the allowance for loan losses; competition; significant changes in accounting, tax or regulatory practices and requirements; and technological changes. Although management has taken certain steps to mitigate any negative effect of the aforementioned items, significant unfavorable changes could severely impact the assumptions used and have an adverse effect on profitability. Such risks and other aspects of the Company's business and operations are described in "Business", "Risk Factors" and "Management's Discussion and Analysis of Financial Condition and Results of Operation." The Company has no obligation to publicly release the result of any revisions which may be made to any forward-looking statements to reflect anticipated or unanticipated events or circumstances occurring after the date of such statements.

Item 1A. Risk Factors.

The common stock of the Company is speculative in nature and involves a significant degree of risk. The risk factors below are not listed in order of importance.

The Company Faces Significant Competition.

The Company faces significant competition from many other banks, savings institutions and other financial institutions which have branch offices or otherwise operate in the Company's market area. Non-bank financial institutions, such as securities brokerage firms, insurance companies and money market funds, engage in activities which compete directly with traditional bank business which has also led to greater competition. Many of these competitors have substantially greater financial resources than the Company, including larger capital bases that allow them to attract customers seeking larger loans than the Company is able to accommodate and the ability to aggressively advertise their products. There can be no assurance that the Company and the Bank will be able to successfully compete with these entities in the future. See "BUSINESS -- Competition."

The Company's Business is Affected by Economic Conditions and Related Uncertainties.

Commercial banking is affected, directly and indirectly, by local, domestic, and international economic and political conditions, and by government monetary and fiscal policies. Conditions such as inflation, recession, unemployment, volatile interest rates, tight money supply, scarce natural resources, real estate values, international conflicts and other factors beyond the control of the Company may adversely affect the potential profitability of the Company. A downtrend in several areas, such as real estate, construction and consumer spending, could have a material adverse impact on the Company's ability to maintain or increase profitability.

The Company is Subject to Interest Rate Risk.

The Company's earnings are largely dependent upon its net interest income. Net interest income is the difference between interest income earned on interest-earning assets such as loans and securities and interest expense paid on interest-bearing liabilities such as deposits and borrowed funds. Interest rates are highly sensitive to many factors that are beyond the Company's control, including general economic conditions and policies of various governmental and regulatory agencies and, in particular, the Board of Governors of the Federal Reserve System. Changes in monetary policy, including changes in interest rates, could influence not only the interest the Company receives on loans and securities and the amount of interest it pays on deposits and borrowings, but such changes could also affect (i) the Company's ability to originate loans and obtain deposits, (ii) the fair value of the Company's financial assets and liabilities, and (iii) the average duration of the Company's mortgage-backed securities portfolio. If the interest rates paid on deposits and other borrowings increase at a faster rate than the interest rates received on loans and other investments, the Company's net interest income, and therefore earnings, could be adversely affected. Earnings could also be adversely affected if the interest rates received on loans and other investments fall more quickly than the interest rates paid on deposits and other borrowings.

Although management believes it has implemented effective asset and liability management strategies to reduce the potential effects of changes in interest rates on the Company's results of operations, any substantial, unexpected, prolonged change in market interest rates could have a material adverse effect on the Company's financial condition and results of operations.

The Company is Subject to Risks Associated With Speculative Construction Lending.

The risks associated with speculative construction lending include the borrower's inability to complete the construction process on time and within budget, the sale of the project within projected absorption periods, the economic risks associated with real estate collateral, and the potential of a rising interest rate environment. Such loans may include financing the development and/or construction of residential subdivisions. This activity may involve financing land purchase, infrastructure development (i.e. roads, utilities, etc.), as well as construction of residences or multi-family dwellings for subsequent sale by developer/builder. Because the sale of developed properties is integral to the success of developer business, loan repayment may be especially subject to the volatility of real estate market values. Management has established underwriting and monitoring criteria to minimize the inherent risks of speculative commercial real estate construction lending. Further, management concentrates lending efforts with developers demonstrating successful performance on marketable projects within the Bank's lending areas.

Federal and State Government Regulation Impact the Company's Operations.

The operations of the Company and the Bank are heavily regulated and will be affected by present and future legislation and by the policies established from time to time by various federal and state regulatory authorities. In particular, the monetary policies of the Federal Reserve Board have had a significant effect on the operating results of banks in the past and are expected to continue to do so in the future. Among the instruments of monetary policy used by the Federal Reserve Board to implement its objectives is changes in the discount rate charged on bank borrowings. It is not possible to predict what changes, if any, will be made to the monetary policies of the Federal Reserve Board or to existing federal and state legislation or the effect that such changes may have on the future business and earnings prospects of the Company.

The Company and the Bank are subject to examination, supervision and comprehensive regulation by various federal and state agencies. Compliance with the rules and regulations of these agencies may be costly and may limit growth and restrict certain activities, including payment of dividends, investments, loans and interest rate charges, interest rates paid on deposits, and locations of offices. The Bank is also subject to capitalization guidelines set forth in federal legislation. See "BUSINESS -- Supervision and Regulation."

The laws and regulations applicable to the banking industry could change at any time, and we cannot predict the impact of these changes on our business and profitability. Because government regulation greatly effects the business and financial results of all commercial banks and bank holding companies, the cost of compliance could adversely affect the Company's ability to operate profitably.

If Economic Conditions Deteriorate, Particularly in the Bank's Market Area, Our Results of Operations and Financial Condition Could Be Adversely Affected as Borrowers' Ability to Repay Loans Declines and the Value of the Collateral Securing Our Loans Decreases.

Our financial results may be adversely affected by changes in prevailing economic conditions, particularly in the Bank's market area, including decreases in real estate values, changes in interest rates which may cause a decrease in interest rate spreads, adverse employment conditions, the monetary and fiscal policies of the federal government and other significant external events.

Decreases in local real estate values would adversely affect the value of property used as collateral for our loans. Adverse changes in the economy also may have a negative effect on the ability of our borrowers to make timely repayments of their loans, which would have an adverse impact on our earnings.

If Our Allowance For Loan Losses is Not Sufficient to Cover Actual Loan Losses, Our Earnings Could Decrease.

We make various assumptions and judgments about the collectibility of our loan portfolio, including the creditworthiness of our borrowers and the value of the real estate and other assets serving as collateral for the repayment of many of our loans. In determining the amount of the allowance for loan losses, we review our loans and our loss and delinquency experience, and we evaluate economic conditions. If our assumptions are incorrect, our allowance for loan losses may not be sufficient to cover losses inherent in our loan portfolio, resulting in additions to our allowance. Material additions to our allowance would materially decrease our net income.

In addition, bank regulators periodically review our allowance for loan losses and may require us to increase our provision for loan losses or recognize further loan charge-offs. Any increase in our allowance for loan losses or loan charge-offs as required by these regulatory authorities might have a material adverse effect on our financial condition and results of operations.

Item 1B. Unresolved Staff Comments

Not Applicable.

Item 2. Properties.

General

The Company’s and the Bank’s principal office in Cranbury, New Jersey (the “Principal Office”), which it occupies under a lease that expires in December 2010, provides for an aggregate monthly rental of $16,619, subject to annual rental increases plus real estate taxes and certain common space charges allocated by the landlord. This lease grants the Bank two additional five-year renewal periods. The Bank also has the right of first refusal to purchase the premises of which the Principal Office is a part on the same terms and conditions as contained in any bona fide offer for the premises. In 2003, the Bank entered into a five-year lease for an additional 1,900 square feet of office space in this building for an aggregate monthly rental of $2,216 per month, subject to annual rental increases. This lease grants the Bank two additional five-year renewal periods.

The Bank leases approximately 2,400 square feet for its branch office in Montgomery Township, New Jersey for an aggregate monthly rental of $5,845. This lease expires on September 30, 2007.

In September 2005, the Bank exercised its right of first refusal option granted under the existing lease agreement and purchased the land and building comprising its branch office in downtown Cranbury, New Jersey. The Bank had previously leased this 3,780 square feet branch office.

In December 2005, the Bank elected to exercise its option for the early termination of the lease for its branch located in Plainsboro, New Jersey. The Bank applied for and received regulatory agency approval to relocate this branch into the Plainsboro Village Center which was accomplished in June 2006. The Bank entered into a 15 year lease for approximately 2,500 square feet with two drive-through lanes in the multi-tenant retail/office building. The Bank has two five year renewal options for this space. The aggregate monthly payment for this lease is $7,381 with annual escalations.

The Bank entered into a lease for the branch located in Hamilton Square, New Jersey in April 1999. This lease expires in July 2014 and provides for a rental of approximately 4,170 square feet. The Bank has two five-year renewal options for this space. The aggregate monthly rental payment for this lease is $9,683, with annual escalations.

In January 2004, the Bank entered into a two-year lease for a new Loan Production Office in Fort Lee, New Jersey. The lease provided for the rental of 1,567 square feet with an aggregate monthly rental of $2,873 in the first year and

$2,938 in the second year. In December 2005, the Bank entered into a lease to house a de novo branch plus the loan production office in Fort Lee, New Jersey. The Bank applied for and received regulatory agency approval to relocate the loan production office and establish a de novo branch which was opened in November 2006. This lease expires in February 2014 and provides for the rental of 3,100 square feet on the ground floor plus 800 square feet in the basement. The aggregate monthly rental payment for this lease is $6,458, with annual escalations.

In June 2004, the Bank commenced the lease for the West Windsor, New Jersey branch. The lease expires in July 2019 and provides for a rental of approximately 3,000 square feet. The lease provides for three five-year renewal options for this space. The aggregate monthly rental payment for this lease is $2,083, with annual escalations.

In August 2004, the Bank commenced the lease for the Perth Amboy, New Jersey branch. This lease expires in August 2019 and provides for a rental of approximately 3,000 square feet The lease provides for two seven and one-half year renewal options for this space. The aggregate monthly rental payment for this lease is $6,250, with annual escalations.

In June 2004, the Bank completed the construction and renovation project associated with opening a branch office in Jamesburg, New Jersey. The Bank purchased the site at 1 Harrison Street in 2002.

Management believes the foregoing facilities are suitable for the Company's and the Bank's present and projected operations.

Item 3. Legal Proceedings.

The Company may, in the ordinary course of business, become a party to litigation involving collection matters, contract claims and other legal proceedings relating to the conduct of its business. The Company may also have various commitments and contingent liabilities which are not reflected in the accompanying consolidated statement of condition. Management is not aware of any present legal proceedings or contingent liabilities and commitments that would have a material impact on the Company's financial position or results of operations.

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

No matters were submitted to a vote of the Company's shareholders during the fourth quarter of the fiscal year ended December 31, 2006.

PART II

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

The common stock of the Company trades on the Nasdaq Global Market under the trading symbol "FCCY". The following are the high and low sales prices per share for 2006 and 2005, as reported on the Nasdaq Global Market.

	2006			2005		
	High	Low		High	Low	
First Quarter	$19.76	$16.18	(1)	$18.40	$14.28	(1)
Second Quarter	$18.64	$16.48	(1)	18.18	14.99	(1)
Third Quarter	$17.92	$16.22	(1)	18.75	15.75	(1)
Fourth Quarter	$18.84	$16.51	(1)	18.82	14.98	(1)

(1) Prices have been retroactively adjusted for the 6% stock dividend declared December 21, 2006 and paid January 31, 2007 to shareholders of record on January 23, 2007.

As of March 6, 2007, there were approximately 334 holders of the Company's common stock.

The Company paid a 6% stock dividend on January 31, 2007 and a 5% stock dividend on January 31, 2006. The Company has never paid a cash dividend and there are no plans to pay a cash dividend at this time. All per share data has been retroactively adjusted for stock dividends. The Company will retain its earnings in order to provide capital for growth of the Bank.

Issuer Purchases of Equity Securities

In 2005, the Board of Directors authorized a stock repurchase program under which the Company may repurchase in open market or privately negotiated transactions up to 5% of its common shares outstanding at that date. The Company undertook this repurchase program in order to increase shareholder value. The following table provides common stock repurchases made by or on behalf of the Company during the three months ended December 31, 2006.

Issuer Purchases of Equity Securities (1)

Period		Total Number of Shares Purchased	Average Price Paid Per Share	Total Number of Shares Purchased As Part of Publicly Announced Plan or Program	Maximum Number of Shares That May Yet be Purchased Under the Plan or Program
Beginning	Ending				
October 1, 2006	October 31, 2006	3,016	$17.52	3,016	169,135
November 1, 2006	November 30, 2006	3,694	$18.12	3,694	165,441
December 1, 2006	December 31, 2006	-	-	-	165,441
	Total	6,710	$17.85	6,710	165,441

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(1) The Company’s common stock repurchase program covers a maximum of 175,271 shares of common stock of the Company, representing 5% of the outstanding common stock of the Company on July 21, 2005 as adjusted for the 6% stock dividend declared December 21, 2006 and paid January 31, 2007.

Item 6. Selected Financial Data.

The following selected financial data should be read in conjunction with the Company’s Consolidated Financial Statements and the accompanying notes presented elsewhere herein.

For years ended December 31	2006	2005	2004	2003	2002	Five Year Compounded Growth Rate
Highlights						
Net income	$5,332,844	$4,560,127	$3,837,714	$3,228,500	$2,687,322	19.9%
Return on average assets	1.40%	1.31%	1.22%	1.18%	1.06%	
Return on average equity	16.62%	16.49%	15.54%	14.85%	14.09%	
Net interest margin	5.03%	4.78%	4.25%	3.94%	3.87%	
Income Statement Data						
Net interest income	$17,787,685	$15,299,893	$12,470,773	$10,012,780	$9,209,044	17.2%
Provision for loan losses	893,500	405,000	240,000	240,000	240,000	
Non-interest income	2,591,009	2,646,861	2,557,242	2,401,349	1,525,526	
Non-interest expenses	12,037,856	10,887,225	8,989,961	7,168,722	6,287,881	
Balance Sheet Data at December 31						
Total assets	$392,677,546	$372,495,466	$335,830,440	$293,483,174	$273,862,343	11.0%
Total deposits	312,724,422	305,809,467	276,887,033	245,353,724	224,149,464	10.0%
Total gross loans	265,142,313	240,014,349	210,653,051	163,950,306	151,049,736	16.2%
Shareholders' equity	35,196,570	29,796,867	26,790,384	25,585,256	20,994,842	15.4%
Allowance for loan losses	3,228,360	2,361,375	2,005,169	1,786,632	1,669,882	15.0%
Share Information [1]						
Earnings per share - basic	$1.45	$1.25	$1.05	$0.89	$0.75	18.2%
Earnings per share - diluted	$1.41	$1.20	$1.02	$0.84	$0.71	18.3%
Book value per share	$9.40	$8.18	$7.28	$6.45	$5.81	13.3%
Average diluted shares Outstanding	3,772,182	3,803,871	3,799,270	3,825,688	3,808,305	
Capital Ratios[2]						
Total capital to risk-weighted assets	20.23%	13.30%	13.99%	14.94%	14.75%	
Tier 1 capital to risk-weighted assets	15.42%	12.47%	13.17%	14.06%	13.84%	
Tier 1 capital to average assets	12.18%	9.76%	10.16%	9.74%	9.64%	

[1] All share information has been restated for the effect of a 6% stock dividend declared on December 21, 2006 and paid on January 31, 2007 to shareholders of record on January 23, 2007.

[2] Capital ratios are for the Company. See footnote 15 to the financial statements for capital ratios of the Company and the Bank.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operation.

This discussion should be read in conjunction with the consolidated financial statements, notes and tables included elsewhere in this report. Throughout the following sections, the "Company" refers to 1ST Constitution Bancorp and its wholly owned subsidiaries, 1ST Constitution Bank, 1ST Constitution Capital Trust I, and 1ST Constitution Capital Trust II, the "Bank" refers to 1ST Constitution Bank, and the "Trusts" refers to 1ST Constitution Capital Trust I and 1ST Constitution Capital Trust II, collectively. The purpose of this discussion and analysis is to assist in the understanding and evaluation of the Company's financial condition, changes in financial condition and results of operations.

Executive Summary

The Company reported net income for the 12 months ended December 31, 2006 of $5,332,844, an increase of 16.9% from the $4,560,127 reported for the 12 months ended December 31, 2005. Diluted net income per share was $1.41 for the year ended December 31, 2006 compared to $1.20 reported for the year ended December 31, 2005. Basic net income per share for the year ended December 31, 2006 was $1.45 as compared to the $1.25 reported for the year ended December 31, 2005. The Company has achieved a five-year compounded growth rate for net income of 19.9% over the 2001-2006 period. All share information has been restated for the effect of a 6% stock dividend declared on December 21, 2006 and paid on January 31, 2007 to shareholders of record on January 23, 2007.

Key performance ratios continued to improve in the 2006 fiscal year as compared to the prior year. Return on average assets ("ROA") and return on average equity ("ROE") were 1.40% and 16.62%, respectively, for the year ended December 31, 2006, compared to 1.31% and 16.49%, respectively, for the year ended December 31, 2005.

The Company's record earnings for the 2006 fiscal year reflect continuing momentum across a broad range of product and service offerings. Increased lending activity, coupled with increases in deposits through branch network expansion and secondary market loan sales volume, fueled both the record earnings and balance sheet growth.

The Company's net interest income for the year ended December 31, 2006 was $17,787,685, an increase of 16.3% from the $15,299,893 reported for the year ended December 31, 2005. For the year ended December 31, 2006, the Company's net interest margin increased to 5.03% compared to 4.78% reported for the year ended December 31, 2005. During 2004, a rising interest rate environment evolved during the latter half of the year and continued through the first half of 2006. The Federal Reserve Bank's Open Market Committee ("FOMC") held eight meetings in 2004, 2005 and 2006. Beginning with the June 30, 2004 meeting, the FOMC increased short-term interest rates by 25 basis points and continued with a series of 16 consecutive 25 basis point increases in each of the subsequent meetings through June 2006. The FOMC then made no changes to short-term rates at any of the remaining four meetings in 2006. The immediate benefit of the interest rate increases to the Company's investment security purchases and floating rate assets resulted in an 106 basis point increase in the yield on total interest-earning assets for 2006. In addition, management's ability to lag the interest rate increases on deposits coupled with a tight discipline in deposit pricing resulted in an increase of 25 basis points in the Company's net interest margin for the year ended December 31, 2006 when compared to the year ended December 31, 2005. Management expects the FOMC to continue to hold interest rates at their current level in early 2007 and has structured the Company's balance sheet in a moderately asset sensitive position in response to this present market rate environment.

Driven by construction loan growth, the Bank's loan portfolio increased 8.6% at December 31, 2006 as compared to December 31, 2005. At December 31, 2006, total loans outstanding (including loans held for sale) reached $278,751,255 compared to $256,772,083 at December 31, 2005. The Bank's deposit base increased by $6,914,955 to $312,724,422 at December 31, 2006 from $305,809,467 at December 31, 2005. Management strategically priced deposit products to be competitive with other financial institutions with branch locations in its market yet still maintain a strong net interest margin to support earnings growth.

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Management believes that the Company has positioned itself for continued success with the combination of a strong capital base, a commitment to provide exceptional customer service, and a commitment to maintain the technology necessary to provide its customers with easy access to the financial products and services offered by the Bank.

Critical Accounting Policies and Estimates

"Management's Discussion and Analysis of Financial Condition and Results of Operation" is based upon the Company's consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires the Company to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses. Note 1 to the Company's Consolidated Financial Statements for the year ended December 31, 2006 contains a summary of the Company's significant accounting policies. Management believes the Company's policy with respect to the methodology for the determination of the allowance for loan losses involves a higher degree of complexity and requires management to make difficult and subjective judgments which often require assumptions or estimates about highly uncertain matters. Changes in these judgments, assumptions or estimates could materially impact results of operations. This critical policy and its application is periodically reviewed with the Audit Committee and the Board of Directors. The provision for loan losses is based upon management's evaluation of the adequacy of the allowance, including an assessment of known and inherent risks in the portfolio, giving consideration to the size and composition of the loan portfolio, actual loan loss experience, level of delinquencies, detailed analysis of individual loans for which full collectibility may not be assured, the existence and estimated net realizable value of any underlying collateral and guarantees securing the loans, and current economic and market conditions. Although management uses the best information available to it, the level of the allowance for loan losses remains an estimate which is subject to significant judgment and short-term change. Various regulatory agencies, as an integral part of their examination process, periodically review the Company's allowance for loan losses. Such agencies may require the Company to make additional provisions for loan losses based upon information available to them at the time of their examination. Furthermore, the majority of the Company's loans are secured by real estate in the State of New Jersey. Accordingly, the collectibility of a substantial portion of the carrying value of the Company's loan portfolio is susceptible to changes in local market conditions and may be adversely affected should real estate values decline or the Central New Jersey area experience an adverse economic shock. Future adjustments to the allowance for loan losses may be necessary due to economic, operating, regulatory and other conditions beyond the Company's control.

Results of Operations

The Company reported record earnings of $5,332,844, or $1.41 per share (diluted), for the year ended December 31, 2006 compared to $4,560,127, or $1.20 per share (diluted), in 2005. Net income and diluted earnings per share grew 16.9% and 17.5%, respectively, for the year ended December 31, 2006. The Company posted net income of $3,837,714, or $1.02 per share (diluted), for the year ended December 31, 2004. All share information has been restated for the effect of a 6% stock dividend declared on December 21, 2006 and paid on January 31, 2007 to shareholders of record on January 23, 2007.

Net Interest Income

Net interest income, the Company's largest and most significant component of operating income, is the difference between interest and fees earned on loans and other earning assets, and interest paid on deposits and borrowed funds. This component represented 87.3% of the Company's net revenues for the year ended December 31, 2006. Net interest income also depends upon the relative amount of interest earning assets, interest-bearing liabilities, and the interest rate earned or paid on them.

The following tables set forth the Company's consolidated average balances of assets and liabilities and shareholders' equity as well as interest income and expense on related items, and the Company's average yield or rate for the years ended December 31, 2006, 2005 and 2004. The average rates are derived by dividing interest income and expense by

the average balance of assets and liabilities, respectively.

Average Balance Sheets with Resultant Interest and Rates

(yields on a tax-equivalent basis)	2006			2005			2004		
	Average Balance	**Interest**	**Average Rate**	**Average Balance**	**Interest**	**Average Rate**	**Average Balance**	**Interest**	**Avera Rat**
Assets:									
Federal Funds Sold/Short-Term Investments	$ 1,457,568	$ 85,012	5.83%	$ 850,741	$ 27,181	3.19%	$ 976,584	$ 10,977	1.1
Investment Securities:									
Collateralized Mortgage Obligations / Mortgage Backed Securities	70,048,748	3,448,780	4.92%	75,758,305	3,017,885	3.98%	87,636,728	3,196,936	3.6
Obligations of States and Political Subdivisions (4)	16,198,497	895,172	5.53%	18,975,766	978,099	5.15%	10,132,976	571,410	5.6
Total	86,247,245	4,343,952	5.04%	94,734,071	3,995,984	4.22%	97,769,704	3,768,346	3.8
Loan Portfolio:									
Construction	125,022,769	11,129,600	8.90%	94,253,131	7,010,571	7.44%	76,191,687	4,108,903	5.3
Residential Real Estate	8,072,109	517,146	6.41%	9,127,634	572,844	6.28%	9,448,423	645,026	6.8
Commercial and Commercial Real Estate	99,521,245	7,706,864	7.74%	93,871,685	6,831,503	7.28%	82,412,002	5,985,833	7.2
Installment	2,013,438	167,126	8.30%	2,394,026	200,020	8.35%	3,255,459	264,074	8.1
All Other Loans	37,111,086	3,645,808	9.82%	31,772,196	3,007,190	9.46%	27,144,851	2,418,231	8.9
Total (1)	271,740,647	23,166,544	8.53%	231,418,672	17,622,128	7.61%	198,452,422	13,422,067	6.7
Total Interest-Earning Assets	**359,445,460**	**27,595,508**	**7.68%**	**327,003,484**	**21,645,293**	**6.62%**	**297,198,710**	**17,201,390**	**5.7**
Allowance for Loan Losses	(2,662,370)			(2,177,263)			(1,909,294)		
Cash and Due From Banks	9,391,415			9,130,543			7,853,303		
Other Assets	15,422,593			12,893,312			10,815,249		
Total Assets	**$ 381,597,098**			**$ 346,850,076**			**$ 313,957,968**		
Liabilities and Shareholders' Equity:									
Interest-Bearing Liabilities:									

Money Market and NOWAccounts	$ 87,135,125	$ 1,455,755	1.67%	$ 101,189,352	$ 1,211,901	1.20%	$ 96,113,368	$ 986,531	1.0
Savings Accounts	44,867,384	939,324	2.09%	33,671,684	409,397	1.22%	26,890,218	136,530	0.5
Certificates of Deposit	58,183,657	2,907,883	5.00%	77,183,169	2,383,392	3.09%	74,136,634	1,917,353	2.5
Certificates of Deposit of $100,000 and Over	43,870,647	1,385,118	3.16%	9,771,290	309,159	3.16%	10,156,576	260,109	2.5
Other Borrowed Funds	32,539,699	1,687,749	5.19%	31,143,663	1,363,507	4.38%	24,812,983	981,689	3.9
Trust Preferred Securities	14,863,014	1,141,668	7.68%	5,000,000	350,823	7.02%	5,000,000	263,083	5.2
Total Interest-Bearing Liabilities	**281,459,526**	**9,517,497**	**3.38%**	**257,959,158**	**6,028,179**	**2.34%**	**237,109,779**	**4,545,295**	**1.9**
Net Interest Spread (2)			**4.30%**			**4.28%**			**3.8**
Non-interest Bearing Demand Deposits	63,040,519			57,792,902			49,622,127		
Other Liabilities	5,013,813			3,447,534			2,536,002		
Total Liabilities	349,513,857			319,199,594			289,267,908		
Shareholders' Equity	32,083,240			27,650,482			24,690,060		
Total Liabilities and Shareholders' Equity	**$ 381,597,097**			**$ 346,850,076**			**$ 313,957,968**		
Net Interest Margin (3)		**$ 18,078,011**	**5.03%**		**$ 15,617,114**	**4.78%**		**$ 12,656,095**	**4.2**

(1) Loan origination fees are considered an adjustment to interest income. For the purpose of calculating loan yields, average loan balances include nonaccrual loans with no related interest income.
(2) The interest rate spread is the difference between the average yield on interest earning assets and the average rate paid on interest bearing liabilities.
(3) The net interest margin is equal to net interest income divided by average interest earning assets.
(4) Tax equivalent basis.

Changes in net interest income and margin result from the interaction between the volume and composition of interest earning assets, interest bearing liabilities, related yields, and associated funding costs. The Rate/Volume Table demonstrates the impact on net interest income of changes in the volume of interest earning assets and interest bearing liabilities and changes in interest rates earned and paid.

The Company’s net interest income increased on a tax equivalent basis by $2,460,897, or 15.8%, to $18,078,011 for the year ended December 31, 2006, from the $15,617,114 reported for the year ended December 31, 2005. As indicated in the Rate/Volume Table, the principal factor contributing to the 2006 increase in net interest income was an increase in the interest income of $3,368,409, resulting from increased balances in the loan portfolio components. This was partially offset by an increase in interest expense resulting from increases in the rates paid on deposit components.

The Company’s net interest income on a tax-equivalent basis increased by $2,961,019, or 23.4%, to $15,617,114 for the year ended December 31, 2005, from the $12,656,095 reported for the year ended December 31, 2004. As indicated in the Rate/Volume Table, the principal factor contributing to the 2005 increase in net interest income was an increase in the interest income of $2,319,709, resulting from increased balances in the loan portfolio components. This was partially offset by an increase in interest expense resulting from increases in the rates paid on deposit components.

Rate/Volume Table	**Amount of Increase (Decrease)**					
	Year Ended December 31, 2006 versus 2005 Due to Change in:			Year Ended December 31, 2005 versus 2004 Due to Change in:		
(Tax-equivalent basis)	Volume	Rate	Total	Volume	Rate	Total
Interest Income:						
Loans:						
Construction	$ 2,516,095	$ 1,602,934	$ 4,119,029	$ 1,156,625	$ 1,745,044	$ 2,901,668
Residential Real Estate	(67,564)	11,866	(55,698)	(20,216)	(51,966)	(72,182)
Commercial and Commercial Real Estate	427,419	447,942	875,361	829,188	16,482	845,670
Installment	(31,770)	(1,115)	(32,894)	(71,867)	7,813	(64,054)
All Other Loans	524,238	114,380	638,618	425,979	162,981	588,960
Total Loans	3,368,409	2,176,006	5,544,415	2,319,709	1,880,353	4,200,063
Investment Securities :						
Collat. Mortg. Obligations / Mortg. Backed Securities	(281,233)	712,128	430,895	(450,907)	271,857	(179,050)
States and political subdivisions	(155,035)	72,108	(82,927)	477,537	(70,849)	406,688
Total Investment Securities	(436,268)	784,236	347,968	26,630	201,008	227,638
Federal Funds Sold / Short-Term Investments	30,300	27,531	57,831	(4,011)	20,215	16,204
Total Interest Income	2,962,440	2,987,774	5,950,214	2,342,328	2,101,576	4,443,904
Interest Expense :						
Money Market and NOW Accounts	(168,651)	412,505	243,854	51,775	173,595	225,370
Savings Accounts	186,786	343,141	529,927	58,265	214,602	272,867

Certificates of Deposit	(1,340,184)	1,864,675	524,491	83,271	382,768	466,039
Certificates of Deposit of $100,000 And Over	1,268,520	(192,561)	1,075,959	(9,825)	58,874	49,049
Other Borrowed Funds	61,146	263,096	324,242	262,592	119,226	381,818
Trust Preferred Securities	757,845	33,000	790,845	-	87,740	87,740
Total interest expense	765,462	2,723,856	3,489,318	446,078	1,036,805	1,482,883
Net Interest Income	$ 765,461	$ 2,723,857	$ 3,489,318	$ 446,078	$ 1,036,805	$ 1,482,884

Average interest earning assets increased by $32,441,976, or 9.9%, to $359,445,460 for the year ended December 31, 2006 from $327,003,484 for the year ended December 31, 2005, consisting primarily of an increase for 2006 of $40,321,975 in loans partially offset by a decrease of $8,486,826 in investment securities compared to 2005. Led by the construction loans component, the Bank's average total loan portfolio grew by 17.4% and loan yields averaged 8.53% for the year ended December 31, 2006, 92 basis points higher than for the year ended December 31, 2005. This increase was primarily the result of 2006 loan growth at floating yields amid the increasing interest rate environment that continued during the first half of the year. The Bank's average investment securities portfolio decreased 9.0%, and the yield on that portfolio increased 82 basis points for the year ended December 31, 2006 compared to the year ended December 31, 2005. Net premium amortization for the year ended December 31, 2006 was $41,405 compared to $139,507 for the year ended December 31, 2005. Overall, the yield on interest earning assets increased 106 basis points to 7.68% in the 2006 fiscal year from 6.62% in the 2005 fiscal year.

Average interest earning assets increased by $29,805,774, or 10.0%, to $327,003,484 for the year ended December 31, 2005 from $297,198,710 for the year ended December 31, 2004, consisting primarily of an increase in 2005 of $32,966,250 in loans partially offset by a decrease of $3,035,633 in investment securities compared to 2004. Led by the construction component, the Bank's average total loan portfolio grew by 16.6%, and loan yields averaged 7.61%, in 2005, 85 basis points higher than 2004. This increase was primarily the result of 2005 loan growth at floating yields amid the increasing interest rate environment that continued during the year. The Bank's average investment securities portfolio decreased 3.1%, and the yield on that portfolio increased 37 basis points in 2005 compared to 2004, primarily as a result of the reduced level of premium amortization on mortgage-backed securities due to the rising rate environment that continued throughout the year during 2005. Net premium amortization for 2005 was $139,507 compared to $350,168 for 2004. Overall, the yield on interest earnings assets increased 83 basis points to 6.62% in 2005 from 5.79% in 2004.

Interest expense increased by $3,489,318, or 57.9%, to $9,517,497 for the year ended December 31, 2006, from $6,028,179 for the year ended December 31, 2005. This increase in interest expense is principally attributable to higher levels of interest-bearing liabilities priced at a higher market interest rate level. Savings accounts increased on average by $11,195,700 in 2006, or 33.2%, as compared to 2005, contributing to the funding of loan portfolio growth. The cost on these deposits increased 87 basis points in 2006 from 2005. Average interest bearing liabilities rose 9.1% in 2006 from 2005. The cost of total interest-bearing liabilities increased 104 basis points to 3.38% in 2006 from 2.34% in 2005.

Interest expense increased by $1,482,884, or 32.6%, to $6,028,179 for the year ended December 31, 2005, from $4,545,295 for the year ended December 31, 2004. This increase in interest expense is principally attributable to higher levels of interest-bearing liabilities priced at a higher market interest rate level. Savings accounts increased on average by $6,781,466 in 2005 as compared to 2004, contributing to the funding of loan portfolio growth. The cost on these deposits increased 71 basis points in 2005 from 2004. Average interest bearing liabilities rose 8.8% in 2005 from 2004. The cost of total interest-bearing liabilities decreased 43 basis points to 2.34% in 2005 from 1.91% in 2004.

Average non-interest bearing demand deposits increased by $5,247,617, or 9.1%, to $63,040,519 for the year ended December 31, 2006 from $57,792,902 for the year ended December 31, 2005. Expansion of the branch network and the resulting new business relationships have generated most of this increase. Throughout the comparative periods, increases in average non-interest bearing deposits contributed to the increases in net interest income.

Non-Interest Income

Non-interest income decreased by $55,852, or 2.1%, to $2,591,009 for the year ended December 31, 2006 from $2,646,861 for the year ended December 31, 2005. Non-interest income in 2005 increased by $89,618, or 3.5%, from a total of $2,557,242 for 2004.

Service charges on deposit accounts represent a significant source of non-interest income. Service charge revenues decreased by $22,033, or 3.2%, to $668,071 for the year ended December 31, 2006 from $690,104 for the year ended December 31, 2005. Service charge revenue totaled $514,494 in 2004. This component of non-interest income represented 25.8%, 26.1%, and 20.1% of the total non-interest income for the years ended December 31, 2006, 2005, and 2004, respectively. Service charge income decreased in 2006 principally due to management's actions to restructure service charges and fees based on the results of a comparative study of market fees performed in early 2005. During 2005, new fees were assessed on accounts overdrawn for drawing on uncollected funds and for processing incoming wire transfers. Service charge income decreased in 2004 as a result of the Bank waiving service charges on new accounts during the period of branch expansion, and a decreasing number of accounts subject to service charges. Management continues to utilize a strategy of requiring compensating balances from its commercial customers. Those who meet balance requirements are not assessed service charges.

Gains on sales of loans held for sale decreased by $371,790, or 25.7%, to $1,072,731 for the year ended December 31, 2006, from $1,444,521 for the year ended December 31, 2005. Gains on sales of loans held for sale totaled $1,373,660 in 2004. Market interest rates on 30-year fixed rate mortgages fell consistently during 2004, and into the first half of 2005. Consumer refinance of home loans, which, along with a strong housing market, led to the Bank achieving high levels in mortgage origination volumes and mortgage loan sale gains, as newly-originated loans were sold at higher than normal spreads due to the consistently lower level of market interest rates. The rising rate environment that evolved during late 2004 and continued throughout the first half of 2006 has significantly impacted the mortgage market and resultant secondary loan sales for 2006 as long term rates have increased.

Non-interest income also includes income from bank-owned life insurance ("BOLI") which amounted to $350,476 for the year ended December 31, 2006 compared to $235,430 for the year ended December 31, 2005. The Bank purchased $6.0 million in tax-free BOLI assets in 2002 and $2.0 million in 2005, which partially offset the cost of employee benefit plans and reduced the overall effective tax rate. The Bank also generates non-interest income from a variety of fee-based services. These include safe deposit rentals, wire transfer service fees and Automated Teller Machine fees for non-customers. Deposit and service fee charges are reviewed and adjusted as needed from time to time by management to reflect current costs incurred by the Bank to offer the products or services and prices charged by competitor financial institutions amid the Bank's competitive market.

The Company recorded net losses on sales of securities available for sale of $99,714 for the year ended December 31, 2006 and $271,871 for the year ended December 31, 2005. The Company recorded net gains on sales of securities available for sale of $27,545 in 2004. These portfolio transactions in 2006, 2005 and 2004 were primarily the result of modest portfolio restructurings. Their purpose was to improve the Company's longer-term interest rate risk position.

Non-Interest Expenses

Non-interest expenses increased by $1,150,631, or 10.6%, to $12,037,856 for the year ended December 31, 2006, from $10,887,225 for the year ended December 31, 2005. Non-interest expenses in 2005 increased 21.1% to $10,887,225 from $8,989,961 in 2004. The largest increase in non-interest expenses for 2006 compared to 2005 was in salaries and employees benefits. To a lesser extent, occupancy, and other non-interest expenses also reflect increases for the comparable periods. The largest increase in non-interest expenses in 2005 compared to 2004 was in salaries and employee benefits and, to a lesser extent, other non-interest expenses, as indicated in the table below. The following table presents the major components of non-interest expenses for the years 2004 through 2006.

Non-interest Expenses

	2006	2005	2004
Salaries and employee benefits	$ 6,799,619	$ 5,894,200	$ 4,955,587
Occupancy expense	1,434,728	1,365,930	1,071,463
Equipment expense	507,402	491,735	464,928
Marketing	258,012	292,352	274,095
Date processing services	733,954	623,001	636,076
Regulatory, professional and other fees	802,309	1,102,691	542,001
Office expense	470,211	401,490	462,586
All other expenses	1,031,621	715,826	583,225
Total	$ 12,037,856	$ 10,887,225	$ 8,989,961

Salaries and employee benefits, which represent the largest portion of non-interest expenses, increased by $905,419, or 15.4%, to $6,799,619 for the year ended December 31, 2006 compared to $5,894,200 for the year ended December

31, 2005. The 2006 increase is primarily due to (a) increased staffing levels for all of 2006 as a result of the opening of two new branch locations (b) normal employee salary increases. These expenses increased in 2005 by $938,613, or 18.9%, over the $4,955,587 reported for 2004. The increase in the level of salaries and employee benefits for 2005 versus 2004 reflects the increase in staffing levels due to the branch expansion program plus normal salary increases. Salaries and employee benefits as a percentage of average assets were 1.78% for 2006, 1.70% for 2005 and 1.58% for 2004. As the result of the adoption by the Company as of January 1, 2006 of Financial Accounting Standards Board Statement No. 123(R), *Share Based Payment*, the Company is required to recognize for the first time the expense of stock options. For the year ended December 31, 2006, the expense amounted to $95,230, which represented all the unvested and issued stock options outstanding on December 31, 2006 plus all stock options issued in 2006.

For the year ended December 31, 2006, occupancy expense increased by $68,798, or 5.0%, to $1,434,728 from $1,365,930 for the year ended December 31, 2005. During June 2006, the Bank opened the new Plainsboro branch which is now relocated in the newly constructed Plainsboro Village Center. This expanded location allows the Bank to offer drive-through banking plus ATM services that were not available at the previous location. The current period increase in occupancy costs is primarily attributable to this branch relocation project. In addition, the relocation and expansion of our Fort Lee loan production office to a full service branch of the Bank was completed in early November 2006. Certain costs related to this relocation have been incurred prior to the actual opening of this branch.

The occupancy expense component of total non-interest expense as a percentage of average assets was 0.38% for the year ended December 31, 2006, 0.39% for the year ended December 31, 2005 and 0.34% for the year ended December 31, 2004, respectively.

Data processing service expense increased by $110,953, or 17.8%, to $733,954 for the year ended December 31, 2006 compared to $623,001 for the year ended December 31, 2005 as the Company incurred operating costs to bring the two new branch locations online during 2006 as well upgrading existing systems throughout the year.

The Bank’s ratio of non-interest expense to average assets has remained consistently favorable at 3.16% for the year ended December 31, 2006 compared to 3.14% for the year ended December 31, 2005 and 2.86% for the year ended December 31, 2004.

An important industry productivity measure is the efficiency ratio. The efficiency ratio is calculated by dividing total operating expenses by net interest income and other income. An increase in the efficiency ratio indicates that more resources are being utilized to generate the same or greater volume of income, while a decrease would indicate a more efficient allocation of resources. The Bank’s efficiency ratio decreased for the year ended December 31, 2006 to 59.1% compared to 60.7% for the year ended December 31, 2005 and 59.8% for the year ended December 31, 2004.

Financial Condition

Cash and Cash Equivalents

At December 31, 2006, cash and cash equivalents totaled $10,361,812 compared to $12,137,750 at December 31, 2005. Cash and cash equivalents at December 31, 2006 consisted of cash and due from banks of $10,336,334 and federal funds sold/short-term investments of $25,478. The corresponding balances at December 31, 2005 were $9,394,929 and $2,742,821, respectively.

Investment Securities

The Bank’s investment securities portfolio amounted to $89,675,804, or 22.8% of total assets at December 31, 2006, compared to $90,995,028, or 24.4% of total assets at December 31, 2005. On an average balance basis, the investment securities portfolio represented 24.0% and 29.0% of average interest-earning assets for the years ended December 31, 2006 and 2005, respectively. The average yield earned on the portfolio was 5.04% for the year ended December 31, 2006, an increase of 82 basis points from 4.22% earned for the year ended December 31, 2005.

Securities available for sale are investments that may be sold in response to changing market and interest rate conditions or for other business purposes. Securities available for sale consist primarily of U.S. Government and Federal agency securities as well as mortgage-backed securities. Activity in this portfolio is undertaken primarily to manage liquidity and interest rate risk and to take advantage of market conditions that create economically more attractive returns. At December 31, 2006, available-for-sale securities amounted to $70,421,328, an increase of $1,184,670 from December 31, 2005. The Company recorded net losses on sales of securities available for sale of $99,714 for 2006 and $271,871 for 2005.

<u>2006</u>	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale-				
U. S. Treasury securities and				
obligations of U.S. Government				
sponsored corporations and agencies	$ 35,625,182	$ 124,144	$ (694,261)	$ 35,055,065
Mortgage backed securities	28,305,557	113,353	(216,111)	28,202,799
Obligations of State and				
Political subdivisions	3,655,197	15,902	(31,749)	3,639,350
FHLB stock and other securities	3,554,759	304	(30,949)	3,524,115
	$ 71,140,695	$ 253,703	$ (973,070)	$ 70,421,328
Held to maturity-				
Mortgage backed securities	$ 5,540,670	$ 2,015	$ 175,826)	$ 5,366,859
Obligations of State and				
Political subdivisions	13,713,806	131,955	(47,941)	13,797,820
	$ 19,254,476	$ 133,970	$ (223,767)	$ 19,164,679

<u>2005</u>	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale-				
U. S. Treasury securities and				
obligations of U.S. Government				
sponsored corporations and agencies	$ 34,032,814	$ 7,198	$ (977,560)	$ 33,062,452
Mortgage backed securities	29,250,341	90,286	(302,193)	29,038,434
Obligations of State and				
Political subdivisions	3,855,987	1,333	(65,063)	3,792,257
FHLB stock and other securities	3,371,673	-	(28,158)	3,343,515

	$	70,510,815	$	98,817	$	(1,372,974)	$	69,236,658
Held to maturity-								
Mortgage backed securities	$	5,807,730	$	7,233	$	(206,275)	$	5,608,688
Obligations of State and								
Political subdivisions		15,950,640		108,525		(146,827)		15,912,338
	$	21,758,370	$	115,758	$	(353,102)	$	21,521,026

2004	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale-				
U. S. Treasury securities and				
obligations of U.S. Government				
sponsored corporations and agencies	$ 57,848,615	$ 85,649	$ 538,057	$ 57,396,206
Mortgage backed securities	20,877,821	412,179	53,848	21,236,152
Obligations of State and				
Political subdivisions	3,883,354	3,070	47,662	3,838,762
FHLB stock and other securities	3,149,734	0	32,205	3,117,529
	$ 85,759,524	$ 500,897	$ 671,772	$ 85,588,649
Held to maturity-				
Mortgage backed securities	$ 604,705	$ 24,174	$ 0	$ 628,879
Obligations of State and				
Political subdivisions	11,562,432	164,247	63,308	11,553,371
	$ 12,167,137	$ 188,421	$ 63,308	$ 12,292,250

Proceeds from maturities and prepayments of securities available for sale amounted to $13,736,214 for the year ended December 31, 2006 and $17,074,576 for the year ended December 31, 2005. At December 31, 2006, the portfolio had net unrealized losses of $719,367, compared to net unrealized losses of $1,274,157 at December 31, 2005. These unrealized losses are reflected net of tax in shareholders' equity as other comprehensive income (loss).

Securities held to maturity, which are carried at amortized historical cost, are investments for which there is the positive intent and ability to hold to maturity. The held-to-maturity portfolio consists primarily of obligations of states and political subdivisions. At December 31, 2006, securities held to maturity were $19,254,476, a decrease of $2,503,894 from $21,758,370 at December 31, 2005. The fair value of the held-to-maturity portfolio at December 31, 2006 was $19,164,679, resulting in a net unrealized loss of $89,796.

The amortized cost, estimated fair value and weighted average yield of investment securities at December 31, 2006, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. Federal Home Loan Bank stock is included in "Held to maturity - Due in one year or less."

	Amortized Cost	Estimated Fair Value	Weighted Average Yield*
Available for sale-			
Due in one year or less	$ 1,301,989	$ 1,301,354	5.27%

Due after one year through five years		17,420,177		17,352,325	4.67%
Due after five years through ten years		15,836,536		15,698,842	4.22%
Due after ten years		36,581,993		36,068,807	4.73%
Total	$	71,140,695	$	70,421,328	5.01%
Held to maturity-					
Due in one year or less	$	2,363,612	$	2,351,783	3.47%
Due after one year through five years		2,839,631		2,838,985	5.38%
Due after five years through ten years		3,615,640		3,625,656	5.52%
Due after ten years		10,435,593		10,348,255	5.59%
Total	$	19,254,476	$	19,164,679	5.41%

* computed on a tax equivalent basis.

Loans

The loan portfolio, which represents the Bank's largest asset, is a significant source of both interest and fee income. Elements of the loan portfolio are subject to differing levels of credit and interest rate risk. The Bank's primary lending focus continues to be construction loans (wholesale and retail), commercial loans, owner-occupied commercial mortgage loans and tenanted commercial real estate loans. Total loans averaged $271,740,647 for the year ended December 31, 2006, an increase of $40,321,975, or 17.4%, compared to an average of $231,418,672 for the year ended December 31, 2005. Growth in the average loan portfolio balance was generated primarily by an increase of $30,769,638, or 32.6%, in construction loans. At December 31, 2006, total loans amounted to $265,142,313 compared to $240,014,349 at December 31, 2005, an increase of $25,127,964, or 10.5%. The average yield earned on the loan portfolio was 8.53% for the year ended December 31, 2006 compared to 7.61% for the year ended December 31, 2005, an increase of 92 basis points. This increase is primarily due to the rising interest rate environment that evolved during the last half of 2004 and continued throughout the first half of 2006.

The following table represents the components of the loan portfolio for the dates indicated.

	December 31,									
	2006		2005		2004		2003		2002	
	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%
Construction loans	$ 125,268,871	47%	$ 109,862,614	46%	$ 88,027,024	42%	$ 56,971,265	35%	$ 32,342,880	21%
Residential real estate loans	7,670,370	3%	8,602,975	4%	9,815,366	5%	8,059,032	5%	9,023,228	6%
Commercial and commercial real estate loans	114,897,040	44%	104,448,196	43%	96,021,077	46%	83,840,831	51%	89,415,759	59%
Loans to individuals	16,728,025	6%	16,441,994	7%	16,002,619	7%	13,236,895	8%	14,851,742	10%
Lease financing	0	0%	21,073	0%	74,543	0%	1,054,198	1%	4,773,528	4%
Deferred loan fees	404,074	0%	466,678	0%	512,416	0%	442,212	0%	412,961	0%
All other loans	173,933	0%	170,819	0%	200,118	0%	345,873	0%	229,638	0%
Total	$ 265,142,313	100%	$ 240,014,349	100%	$ 210,653,051	100%	$ 163,950,306	100%	$ 151,049,736	100%

The rising interest rate environment that existed throughout the first half of 2006, especially the rising average prime rate, and competitive loan pricing resulted in the increased portfolio components discussed in the following paragraphs.

Commercial and commercial real estate loans averaged $99,521,245 for the year ended December 31, 2006, an increase of $5,649,560, or 6.0%, compared to $93,871,685 for the year ended December 31, 2005. Commercial loans consist primarily of loans to small and middle market businesses and are typically working capital loans used to finance inventory, receivables or equipment needs. These loans are generally secured by business assets of the commercial borrower. The average yield on the commercial and commercial real estate loan portfolio increased 46 basis points to 7.74% for 2006 from 7.28% for 2005.

Construction loans averaged $125,022,769 for the year ended December 31, 2006, an increase of $38,186,361, or 25.9%, compared to $94,253,131 for the year ended December 31, 2005. Generally, these loans represent owner-occupied or investment properties and usually complement a broader commercial relationship between the bank and the borrower. Construction loans are structured to provide for advances only after work is completed and inspected by qualified professionals. The average yield on the construction loan portfolio increased 146 basis points to 8.90% for 2006 from 7.44% for 2005.

Residential loans averaged $8,072,109 for the year ended December 31, 2006, a decrease of $1,055,525, or 11.6%, compared to $9,127,634 for the year ended December 31, 2005. These loans consist primarily of residential mortgage loans secured by residential real estate. The average yield on this portfolio increased 13 basis points to 6.41% for 2006 from 6.28% for 2005.

The following table provides information concerning the interest rate sensitivity of the Bank's commercial and commercial real estate loans and construction loans at December 31, 2006.

	Maturity Range			
Type	Within One Year	After One But Within Five Years	After Five Years	Total
Commercial & commercial real estate	$ 25,571,909	$ 16,962,095	$ 72,363,036	$ 114,897,040
Construction	114,958,027	9,420,908	889,936	125,268,871
Total	$ 140,529,936	$ 26,383,003	$ 73,252,972	$ 240,165,911
Fixed rate loans	$ 6,787,253	$ 12,692,806	$ 6,224,384	$ 25,704,443
Floating rate loans	133,742,683	13,690,197	67,028,588	214,461,468
Total	$ 140,529,936	$ 26,383,003	$ 73,252,972	$ 240,165,911

Non-Performing Assets

Non-performing assets consist of non-performing loans and other real estate owned. Non-performing loans are composed of (1) loans on a non-accrual basis, (2) loans which are contractually past due 90 days or more as to interest and principal payments but have not been classified as non-accrual, and (3) loans whose terms have been restructured to provide a reduction or deferral of interest on principal because of a deterioration in the financial position of the borrower.

The Bank's policy with regard to non-accrual loans is that generally, loans are placed on a non-accrual status when they are 90 days past due unless these loans are well secured and in the process of collection or, regardless of the past due status of the loan, when management determines that the complete recovery of principal or interest is in doubt. Consumer loans are generally charged off after they become 120 days past due. Subsequent payments on loans in non-accrual status are credited to income only if collection of principal is not in doubt.

Non-performing loan increased by $3,359,850 to $4,193,209 at December 31, 2006 from $833,359 at December 31, 2005. This increase is primarily due to an increase of $3,360,059 in non-accrual loans to $4,193,209 at December 31, 2006 compared to $833,150 at December 31, 2005. The increase in non-accrual loans is primarily related to the Bank's construction lending activities totaling $3,422,118 being designated as non-accrual. The largest segment of the increase represents unfinished residential construction where litigation has been commenced and work out negotiations are in process. The balance of the non-performing loans are centered in completed residential and commercial properties which are in foreclosure. The table below sets forth non-performing assets and risk elements in the Bank's portfolio by type for the years indicated. As the table demonstrates, non-performing loans to total loans increased to 1.58% at December 31, 2006 from 0.35% at December 31, 2005 for the reasons previously stated, but loan quality is still considered to be strong. This was accomplished through quality loan underwriting, a proactive approach to loan monitoring and aggressive workout strategies.

Non-performing assets increased by $3,359,850 to $4,193,209 at December 31, 2006 from $833,359 at December 31, 2005. Non-performing assets represented 1.07% of total assets at December 31, 2006 and 0.22% at December 31, 2005. Non-performing loans as a percentage of total loans were 1.58% at December 31, 2006, compared to 0.35% at December 31, 2005.

The Bank had no loans classified as restructured loans at December 31, 2006 or 2005.

At December 31, 2006, the Bank had no loans that were 90 days or more past due but still accruing interest income compared to $209 of loans in this category of non-performing loans at December 31, 2005. Management's decision to accrue income on these loans was based on the level of collateral and the status of collection efforts.

Non-Performing Assets and Loans

	2006	2005	2004	2003	2002
Non-Performing loans:					
Loans 90 days or more past due and still accruing	$ 0	$ 209	$ 63,130	$ 0	$ 2,156
Non-accrual loans	4,193,209	833,150	1,049,411	330,783	156,156
Total non-performing loans	4,193,209	833,359	1,112,541	330,783	158,312
Other real estate owned	0	0	0	8,971	9,492
Total non-performing assets	$ 4,193,209	$ 833,359	$ 1,112,541	$ 339,754	$ 167,804
Non-performing loans to total loans	1.58%	0.35%	0.53%	0.20%	0.10%
Non-performing assets to total assets	1.07%	0.22%	0.33%	0.12%	0.06%

Management takes a proactive approach in addressing delinquent loans. The Company's President meets weekly with all loan officers to review the status of credits past-due ten days or more. An action plan is discussed for each of the loans to determine the steps necessary to induce the borrower to cure the delinquency and restore the loan to a current status. Also, delinquency notices are system generated when loans are five days past-due and again at 15 days past-due.

In most cases, the Company's collateral is real estate and when the collateral is foreclosed upon, the real estate is carried at the lower of fair market value less estimated selling costs, or at cost. The amount, if any, by which the recorded amount of the loan exceeds the fair market value of the asset is a loss which is charged to the allowance for loan losses at the time of foreclosure or repossession. Resolution of a past-due loan can be delayed if the borrower files a bankruptcy petition because collection action cannot be continued unless the Company first obtains relief from the automatic stay provided by the bankruptcy code.

Allowance for Loan Losses and Related Provision

The allowance for loan losses is maintained at a level sufficient to absorb estimated credit losses in the loan portfolio as of the date of the financial statements. The allowance for loan losses is a valuation reserve available for losses incurred or inherent in the loan portfolio and other extensions of credit. The determination of the adequacy of the allowance for loan losses is a critical accounting policy of the Company.

The Company's primary lending emphasis is the origination of commercial and commercial real estate loans including construction loans. Based on the composition of the loan portfolio, the primary risks inherent in it are deteriorating credit quality, increases in interest rates, a decline in the economy, and a decline in New Jersey real estate market values. Any one or a combination of these events may adversely affect the loan portfolio and may result in increased delinquencies, loan losses and increased future provision levels.

All or part of the principal balance of commercial and commercial real estate loans, and construction loans are charged off to the allowance as soon as it is determined that the repayment of all, or part, of the principal balance is highly unlikely. Consumer loans are generally charged off no later than 120 days past due on a contractual basis, earlier in the event of bankruptcy, or if there is an amount deemed uncollectible. Because all identified losses are

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

Management reviews the adequacy of the allowance on at least a quarterly basis to ensure that the provision for loan and lease losses has been charged against earnings in an amount necessary to maintain the allowance at a level that is adequate based on management's assessment of probable estimated losses. The Company's methodology for assessing the adequacy of the allowance for loan and lease losses consists of several key elements. These elements include a specific reserve for doubtful or high risk loans, an allocated reserve, and an unallocated portion. The Company consistently applies the following comprehensive methodology.

During the quarterly review of the allowance for loan and lease losses, the Company considers a variety of factors that include:

- General economic conditions.
- Trends in charge-offs.
- Trends and levels of delinquent loans.
- Trends and levels of non-performing loans, including loans over 90 days delinquent.
- Trends in volume and terms of loans.
- Levels of allowance for specific classified loans.
- Credit concentrations.

The specific reserve for high risk loans is established for specific commercial loans, commercial real estate loans, and construction loans which have been identified by management as being high risk loan assets. These high risk loans are assigned a doubtful risk rating grade because the loan has not performed according to payment terms and there is reason to believe that repayment of the loan principal in whole, or part, is unlikely. The specific portion of the allowance is the total amount of potential unconfirmed losses for these individual doubtful loans. To assist in determining the fair value of loan collateral, the Company often utilizes independent third party qualified appraisal firms which in turn employ their own criteria and assumptions that may include occupancy rates, rental rates, and property expenses, among others.

The second category of reserves consists of the allocated portion of the allowance. The allocated portion of the allowance is determined by taking pools of loans outstanding that have similar characteristics and applying historical loss experience for each pool. This estimate represents the potential unconfirmed losses within the portfolio. Individual loan pools are created for commercial and commercial real estate loans, construction loans, and for the various types of loans to individuals. The historical estimation for each loan pool is then adjusted to account for current conditions, current loan portfolio performance, loan policy or management changes, or any other factor which may cause future losses to deviate from historical levels.

The Company also maintains an unallocated allowance. The unallocated allowance is used to cover any factors or conditions which may cause a potential loan loss but are not specifically identifiable. It is prudent to maintain an unallocated portion of the allowance because no matter how detailed an analysis of potential loan losses is performed, these estimates by definition lack precision. Management must make estimates using assumptions and information which is often subjective and changing rapidly. At December 31, 2006, management believed that the allowance for loan losses and non-performing loans was adequate.

While management uses the best information available to make such evaluations, future additions to the allowance may be necessary based on changes in economic conditions. In addition, various regulatory agencies, as an integral part of their examination process, periodically review the Bank’s allowance for loan losses. Such agencies may require the Bank to recognize additions to the allowance based on their judgments of information available to them at the time of their examination.

The table below presents, for the years indicated, an analysis of the allowance for loan losses and other related data.

Allowance for Loan Losses

	2006	2005	2004	2003	2002
Balance, beginning of period	$ 2,361,375	$ 2,005,169	$ 1,786,632	$ 1,669,882	$ 1,414,495
Provision charged to operating expenses	893,500	405,000	240,000	240,000	240,000
Loans charged off:					
Construction loans	-	-	-	-	-
Residential real estate loans	-	-	-	-	-
Commercial and commercial real estate loans	(11,154)	(39,150)	(17,070)	(115,698)	(7,034)
Loans to individuals	(18,314)	(13,653)	(5,203)	(7,968)	(1,148)
Lease financing	-	-	-	-	-
All other loans	-	-	-	-	-
	(29,468)	(52,803)	(22,273)	(123,666)	(8,182)
Recoveries:					
Construction loans	-	-	-	-	-
Residential real estate loans	-	-	-	-	-
Commercial and commercial real estate loans	153	1,498	750		20,296
Loans to individuals	2,800	2,511	60	416	3,273
Lease financing	-	-	-	-	-
All other loans	-	-	-	-	-
	2,953	4,009	810	416	23,569
Net (charge offs) / recoveries	(26,515)	(48,794)	(21,463)	(123,250)	15,387
Balance, end of period	$ 3,228,360	$ 2,361,375	$ 2,005,169	$ 1,786,632	$ 1,669,882
Loans:					
At year end	$ 278,751,255	$ 256,772,083	$ 220,580,932	$ 163,950,306	$ 151,049,736
Average during the year	271,740,647	231,418,672	198,452,421	170,191,619	145,159,286
Net (charge offs) recoveries to average loans outstanding	(0.01%)	(0.02%)	(0.01%)	0.07%	(0.01%)
Allowance for loan losses to:					
Total loans at year end	1.16%	0.92%	0.91%	1.09%	1.11%
Non-performing loans	76.99%	283.36%	180.23%	540.12%	270.16%

At December 31, 2006, the allowance for loan losses was $3,228,360 compared to $2,361,375 at December 31, 2005, an increase of $866,985, or 36.7%. The ratio of the allowance for loan losses to total loans at December 31, 2006 and 2005 was 1.16% and 0.92%, respectively. The allowance for loan losses as a percentage of non-performing loans was 76.99% at December 31, 2006, compared to 283.36% at December 31, 2005. Management believes the quality of the loan portfolio remains strong and that the allowance for loan losses is adequate in relation to credit risk exposure levels.

The provision for loan losses was $893,500 and $405,000, respectively, for the years ended December 31, 2006 and 2005. Management considers a complete review of the following specific factors in determining the provision for loan losses: historical losses by loan category, non-accrual loans, problem loans as identified through internal classifications, collateral values, and the growth and size of the portfolio. In addition to these factors, management takes into consideration current economic conditions and local real estate market conditions. The increase in the provision for the year ended December 31, 2006 was primarily due to inherent risk related to loan growth and increased watch list loans. Management believes the quality of the loan portfolio remains sound, the determination of the provision for loan losses amount was primarily due to the manageable balances in non-accrual loans and management's assessment of economic conditions in the Bank's marketplace.

The following table describes the allocation of the allowance for loan losses among the various categories of loans and certain other information as of the dates indicated. The allocation is made for analytical purposes and is not necessarily indicative of the categories in which future losses may occur. The total allowance is available to absorb losses from any segment of loans.

Allocation of the Allowance for Loan Losses

	December 31, 2006		December 31, 2005		December 31, 2004		December 31, 2003		December 31, 2002	
	Amount	% of loans in each category to total loans	Amount	% of loans in each category to total loans	Amount	% of loans in each category to total loans	Amount	% of loans in each category to total loans	Amount	% of loans in each category to total loans
Balance at end of period applicable to:										
Domestic:										
Commercial and commercial real estate loans	$ 1,131,536	44%	$ 1,393,210	43%	$ 1,183,050	46%	$ 1,054,113	51%	$ 985,231	60%
Construction loans	1,696,175	47%	578,537	46%	491,266	42%	375,193	35%	350,675	21%
Residential real estate loans	61,634	3%	141,683	4%	120,310	5%	107,198	5%	100,193	6%
Loans to individuals	139,055	6%	236,138	7%	200,517	7%	178,663	8%	166,988	10%
Lease financing	-	0%	4,723	0%	4,010	0%	53,599	1%	50,096	3%
Unallocated	200,230	N/A	7,084	N/A	6,016	N/A	17,866	N/A	16,699	N/A
	$ 3,228,360	100%	$ 2,361,375	100%	$ 2,005,169	100%	$ 1,786,632	100%	$ 1,669,882	100%

Deposits

Deposits, which include demand deposits (interest bearing and non-interest bearing), savings and time deposits, are a fundamental and cost-effective source of funding. The Bank offers a variety of products designed to attract and retain customers, with the Bank's primary focus being on building and expanding long-term relationships. Deposits in the year ended December 31, 2006 averaged $297,097,332, an increase of $17,488,935, or 6.3%, compared to $279,608,397 in the year ended December 31, 2005. At December 31, 2006, total deposits were $312,724,422, an increase of $6,914,955, or 2.3%, from $305,809,467 at December 31, 2005. The average rate paid on the Bank's interest-bearing deposit balances for 2006 was 2.86%, increasing from the 1.94% average rate for 2005. Total interest bearing deposits increased by $5,296,312, or 2.2%, to $248,418,977 at December 31, 2006 from $243,122,665 at December 31, 2005.

The significant contributors to the increased level of deposit growth in the year ended December 31, 2006 were an increase in average certificates of deposit of $100,000 or more, followed by increases in non-interest bearing demand deposits and savings deposits, offset by declines in other time deposits and interest-bearing demand deposits.

Time deposits consists primarily of retail certificates of deposit and certificates of deposit of $100,000 and over. Time deposits at December 31, 2006 were $112,675,086, an increase of $21,579,753, or 23.7%, from $91,095,333 at December 31, 2005. The retail certificates of deposit component of time deposits decreased by $18,999,512, or 24.6%, to an average of $58,183,657 for 2006 from an average of $77,183,169 for 2005. The average cost of these deposits increased by 191 basis points to 5.00% for 2006 from 3.09% for 2005. Certificates of deposit of $100,000 and over increased by $34,099,357 to an average of $43,870,647 for 2006 from an average of $9,771,290 for 2005. The average cost for these deposits remained unchanged at 3.16% for 2006 and 3.16% for 2005. Certificates of deposit of $100,000 and over are a less stable funding source and are used primarily as an alternative to other sources of borrowed funds.

Average non-interest bearing demand deposits increased by $5,248,392, or 9.1%, to $63,040,519 for the year ended December 31, 2006 from $57,792,127 for the year ended December 31, 2005. At December 31, 2006, non-interest bearing demand deposits totaled $64,305,445, an increase of 2.6% compared to $62,686,802 at December 31, 2005. Non-interest bearing demand deposits represent a stable, interest-free source of funds. Growth in business and personal checking accounts through the Bank’s marketing programs generated most of the current year increase.

Savings accounts increased by $4,083,288, or 8.2%, to $53,630,726 at December 31, 2006 from $49,547,438 at December 31, 2005. The average balance of savings accounts for 2006 increased by $11,195,700 to $44,867,384 compared to an average balance of $33,671,684 for 2005.

Interest bearing demand deposits, which include interest-bearing checking, money market and the Bank's premier money market product, 1ST Choice accounts, decreased by $38,148,833, or 37.7%, to an average of $63,040,519 for 2006 from an average of $101,189,352 in 2005. The average cost of interest bearing demand deposits increased 47 basis points to 1.67% for 2006 compared to 1.20% for 2005.

The following table illustrates the components of average total deposits for the dates indicated.

Average Deposit Balances

	2006		2005		2004	
	Average Balance	Percentage of Total	Average Balance	Percentage of Total	Average Balance	Percentage of Total
Non-interest bearing demand Deposits	$63,040,519	21.22%	$57,792,902	20.67%	$49,622,127	19.31%
Interest bearing demand deposits	87,135,125	29.33%	101,189,352	36.19%	96,113,368	37.41%
Savings deposits	44,867,384	15.10%	33,671,684	12.04%	26,890,218	10.47%
Certificates of deposit of $100,000 or more	43,870,647	14.77%	9,771,290	3.49%	10,156,576	3.95%
Other time deposits	58,183,657	19.58%	77,183,169	27.60%	74,136,634	28.86%
Total	$297,097,332	100.00%	$279,608,397	100.00%	$256,918,923	100.00%

Borrowings

Borrowings are mainly comprised of Federal Home Loan Bank ("FHLB") borrowings and overnight funds purchased. These borrowings are primarily used to fund asset growth not supported by deposit generation. The average balance of other borrowed funds increased by $1,396,036, or 4.5%, to $32,539,699 for the year ended December 31, 2006 from the average balance of $31,143,663 for the year ended December 31, 2005. This increase is primarily due to the fact that loan portfolio growth exceeded deposit growth. The average cost of other borrowed funds increased 81 basis points to 5.19% for 2006 compared to 4.38% for 2005.

The balance of other borrowings was $17,200,000 at December 31, 2006, consisting of long-term FHLB borrowings of $15,500,000 and overnight funds purchased of $1,700,000. The balance of other borrowings at December 31, 2005 consisted of FHLB borrowings of $23,500,000 and overnight funds purchased of $5,000,000. The average cost of other borrowed funds increased 81 basis points to 5.19% for 2006 compared with 4.38% for 2005.

During 2000, the Bank purchased three ten-year fixed rate convertible advances from the FHLB. These advances, in the amounts of $2,500,000, $5,000,000, and $5,000,000 bear interest at the rates of 5.50%, 5.34%, and 5.06%, respectively. These advances are convertible quarterly at the option of the FHLB.

These advances are fully secured by marketable securities and qualifying one-to-four family mortgage loans.

Securities sold under agreements to repurchase are summarized as follows:

	2006	2005	2004
Balance outstanding at year end	-	-	-
Weighted average interest rate at year end	-	-	1.27%
Average daily balance outstanding during year	-	-	$ 1,674,172
Weighted average interest rate during year	-	-	1.28%
Highest month-end outstanding balance	-	-	$ 1,941,042

Shareholders' Equity and Dividends

Shareholders' equity increased by $5,399,703, or 18.1%, to $35,196,570 at December 31, 2006, from $29,796,867 at December 31, 2005. Book value per common share increased by $1.22, or 14.9%, to $9.40 at December 31, 2006 from $8.18 at December 31, 2005. The increase in shareholders' equity and book value per share resulted primarily from net income of $5,332,844, less the effect of stock buybacks, the unrealized holding loss on securities held for resale and an increase in accumulated and other comprehensive loss of $499,194 as a result of the adoption of SFAS No. 158 in the fourth quarter of 2006 (see Note 1 of the Notes to Consolidated Financial Statements on page F-11). The ratio of shareholders' equity to total assets was 8.96%, 8.00% and 7.98% at December 31, 2006, 2005, and 2004, respectively.

During the period January 1, 2002 through December 31, 2006, the Company achieved a five year compounded growth rate for shareholders' equity of 19.9%. The Company's book value per share has also increased over this period at a compounded growth rate of 13.3%. In lieu of cash dividends, the Company (and its predecessor the Bank) has declared a stock dividend every year since 1992 and has paid such dividends every year since 1993. A 6% stock dividend was declared in 2006 and paid in 2007 and a 5% stock dividend was declared in each of the years 2005 and 2004 and paid in each of the years 2006 and 2005, respectively.

The Company's common stock is quoted on the Nasdaq Global Market under the symbol "FCCY".

The Company and the Bank are subject to various regulatory capital requirements administered by the Federal Reserve Board and the Federal Deposit Insurance Corporation. For information on regulatory capital, see Note 15 of the Notes to Consolidated Financial Statements on page F-25.

Off-Balance Sheet Arrangements and Contractual Obligations

Off-Balance Sheet Arrangements

The following table shows the amounts and expected maturities of significant commitments as of December 31, 2006. Further discussion of these commitments is included in Note 13 to the Consolidated Financial Statements.

	One Year or Less	One to Three Years	Three to Five Years	Over Five Years	Total
Standby letters of credit	$ 5,999,658	$ 0	$ 0	$ 0	$ 5,999,658
Commitments to extend credit	$ 104,050,000	$ 0	$ 0	$ 0	$ 104,050,000
Commitments to sell residential loans	$ 13,608,942	$ 0	$ 0	$ 0	$ 13,608,942

Contractual Obligations

The following table shows the significant contractual obligations of the Company by expected payment period as of December 31, 2006. Further discussion of these commitments is included in Note 13 to the Consolidated Financial Statements.

Contractual Obligation	Total	Less Than One Year	One to Three Years	Three to Five Years	Over Five Years
Long-term debt obligations	$15,500,000	$0	$3,000,000	$12,500,000	$0
Operating lease obligation	$5,581,372	$663,526	$1,225,353	$1,041,269	$2,651,224
Purchase obligations	$861,000	$789,000	$72,000	$0	$0
Certificates of deposit	$112,675,086	$98,524,127	$11,692,690	$2,458,269	$0
Redeemable subordinated debentures	$23,712,000	$5,155,000	$0	$0	$18,557,000

Long-term debt obligations includes fixed term borrowings from the Federal Home Loan Bank. The borrowings have defined terms and under certain circumstances are callable at the option of the lender. Operating leases represent obligations entered into by the Company for the use of land and premises. The leases generally have escalation terms based upon certain defined indices. Purchase obligations represent legally binding and enforceable agreements to purchase goods and services from third parties and consists primarily of contractual obligations under data processing service agreements.

On February 23, 2007, the Company delivered a notice of redemption effective April 22, 2007 of $5,155,000 of floating rate debentures due to mature on April 22, 2032.

The Company also has commitments and obligations under its employee benefit plans as described in Note 11 to the Consolidated Financial Statements.

Liquidity

Liquidity measures the ability to satisfy current and future cash flow needs as they become due.

Liquidity management refers to the Company's ability to support asset growth while satisfying the borrowing needs and deposit withdrawal requirements of customers. In addition to maintaining liquid assets, factors such as capital position, profitability, asset quality and availability of funding affect a bank's ability to meet its liquidity needs. On the asset side, liquid funds are maintained in the form of cash and cash equivalents, federal funds sold, investment securities held to maturity maturing within one year, securities available for sale and loans held for sale. Additional asset-based liquidity is derived from scheduled loan repayments as well as investment repayments of principal and interest from mortgage-backed securities. On the liability side, the primary source of liquidity is the ability to generate core deposits. Short-term borrowings are used as supplemental funding sources when growth in the core deposit base does not keep pace with that of earnings assets.

The Bank has established a borrowing relationship with the FHLB and a correspondent bank which further supports and enhances liquidity. At December 31, 2006, the Bank maintained an Overnight Line of Credit at the FHLB in the amount of $16,176,500 plus a One-Month Overnight Repricing Line of Credit of $10,176,500. Advances issued under these programs are subject to FHLB stock level and collateral requirements. Pricing of these advances may fluctuate based on existing market conditions. The Bank also maintains an unsecured Federal funds line of $13,500,000 with a correspondent bank.

The Consolidated Statements of Cash Flows present the changes in cash from operating, investing and financing activities. At December 31, 2006, the balance of cash and cash equivalents was $10,361,812.

Net cash provided by operating activities totaled $8,355,014 for the year ended December 31, 2006 compared to net cash used in operations of $548,080 for the year ended December 31, 2005. The primary source of funds is net income from operations adjusted for provision for loan losses, depreciation expenses, and net amortization of premiums on securities. During 2006, lower volume of originations of loans held for sale resulted in less cash being used in this operating activity.

Net cash used in investing activities decreased by $2,423,884, or 9.0%, to $24,486,184 for the year ended December 31, 2006 from $26,910,068 for the year ended December 31, 2005. The decrease in cash usage for 2006 compared to 2005 resulted from decreases in loans and purchases of securities.

Net cash provided by financing activities decreased by $17,316,257, or 54.7%, to $14,355,232 for the year ended December 31, 2006 from $31,671,489 for the year ended December 31, 2005. The cash provided in 2006 resulted primarily from the issuance of trust preferred securities.

The securities portfolios are also a source of liquidity, providing cash flows from maturities and periodic repayments of principal. For the year ended December 31, 2006, prepayments and maturities of investment securities totaled $16,219,982. Another source of liquidity is the loan portfolio, which provides a flow of payments and maturities.

Interest Rate Sensitivity Analysis

The largest component of the Bank's total income is net interest income, and the majority of the Bank's financial instruments are composed of interest rate-sensitive assets and liabilities with various terms and maturities. The primary objective of management is to maximize net interest income while minimizing interest rate risk. Interest rate risk is derived from timing differences in the repricing of assets and liabilities, loan prepayments, deposit withdrawals, and differences in lending and funding rates. Management actively seeks to monitor and control the mix of interest rate-sensitive assets and interest rate-sensitive liabilities.

The following tables set forth certain information relating to the Bank's financial instruments that are sensitive to changes in interest rates, categorized by expected maturity or repricing and the fair value of such instruments at December 31, 2006.

Interest Rate Sensitivity Analysis At December 31, 2006

($ in thousands)	Interest Sensitivity Period				Total Within One Year	One Year To Two Years	Non-interest Sensitive and Over Two Years	Total
	30 Day	90 Day	180 Day	365 Day				
Earning Assets:								
Total Investment Securities	$ 1,540	$ 2,883	$ 1,925	$ 7,139	$ 13,487	$ 20,523	$ 55,666	$ 89,676
Loans	169,679	5,675	5,848	11,242	192,444	16,849	55,849	265,142
Other Interest-earning assets	14,109	-	-	-	14,109	-	23,751	37,860
	185,328	8,558	7,773	18,381	220,040	37,372	135,266	392,678
Source of Funds:								
Savings and time deposits	37,323	26,753	37,463	26,140	127,679	20,372	27,767	175,818
Other interest-bearing liabilities	50,405	18,000	5,000	3,000	76,405	15,318	21,078	112,801
Non-interest-bearing sources	-	-	-	-	-	-	104,059	104,059
	87,728	44,753	42,463	29,140	204,084	35,690	152,904	392,678

Asset (Liability) Sensitivity Gap:								
Period Gap	$ 97,600	($36,195)	($34,690)	($10,759)	$ 15,956	$ 1,682	($17,638)	$ 0
Cumulative Gap	$ 97,600	$ 61,405	$ 26,715	$ 15,956	$ 15,956	$ 17,638		
Cumulative Gap to Total Assets	24.8%	15.6%	6.8%	4.1%	4.1%	4.5%		

The Bank continually evaluates interest rate risk management opportunities, including the use of derivative financial instruments. Management believes that hedging instruments currently available are not cost-effective, and therefore has focused its efforts on increasing the Bank's spread by attracting lower-costing retail deposits.

In addition to utilizing the gap ratio for interest rate risk assessment, management utilizes simulation analysis whereby the model estimates the variance in net income with a change in interest rates of plus or minus 200 basis points over 12 and 24 month periods. Given recent simulations, net interest income would be within policy guidelines regardless of the direction of market rates.

Recent Accounting Pronouncements

In February, 2006, the FASB issued SFAS No. 155, "Accounting for Certain Hybrid Financial Instruments - an amendment of FASB Statements No. 133 and 140: ("SFAS 155"), to simplify and make more consistent the accounting for certain financial instruments. SFAF 155 amends SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" ("SFAS 133") and permits fair value re-measurement for any hybrid financial instrument with an embedded derivative that otherwise would require bifurcation, provided that the whole instrument is accounted for on a fair value basis. Prior to fair value measurement, interests in securitized financial assets must be evaluated to identify interests containing embedded derivatives requiring bifurcation. The amendments to SFAS 133 also clarify which interest-only and principal-only strips are not subject to the requirements of SFAS 133, and that concentration of credit risk in the form of subordination are not embedded derivatives. SFAS 155 amends SFAS 140 to allow a qualifying special-purpose entity to hold a derivative financial instrument that pertains to a beneficial interest other than another derivative financial instrument. SFAS 155 applies to all financial instruments acquired or issued after the beginning of an entity's first fiscal year that begins after September 15, 2006, with earlier application allowed. SFAS 155 is not expected to have a material impact on the Company's results of operations or financial condition.

In March 2006, the Financial Accounting Standards Board (FASB) issued Statement No. 156 (SFAS 156), Amending "Accounting for separately Recognized Assets and Servicing Liabilities". SFAS 156 amends SFAS No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities." SFAS 156 permits, but does not require, an entity to choose either the amortization method or the fair value measurement method for measuring each class of separately recognized servicing assets and servicing liabilities. SFAS 156 is effective for fiscal years beginning after September 15, 2006 and is not expected to have a material impact on the Company's consolidated financial statements.

In July 2006, FASB issued FASB Interpretation (FIN) 48, "Accounting for Uncertainty in Income Taxes: an interpretation of FASB Statement No. 109, "Accounting for Income Taxes." FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an entity's financial statements in accordance with Statement of SFAS No. 109. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006 and is currently under evaluation by the Company to determine the impact on the Company's consolidated financial statements.

In September 2006, FASB Issued Statement No. 157 (SFAS 157), "FairValue Measurements" which is effective for fiscal years beginning after November 15, 2007 and for interim periods within those years. This statement defines fair value, establishes a framework for measuring fair value and expands the related disclosure requirements. The Company is currently evaluating the impact the adoption of SFAS No. 157 will have on its consolidated financial statements.

In September 2006, FASB Issued Statement No. 158 (SFAS 158),"Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans—an amendment of FASB Statements No. 87, 88, 106, and 132(R)". SFAS 158 requires an employer to recognize the overfunded or underfunded status of a defined benefit postretirement plan (other than a multiemployer plan) as an asset or liability in its statement of financial position and to recognize changes in that funded status in the year in which the changes occur through comprehensive income. This Statement also improves financial reporting by requiring an employer to measure the funded status of a plan as of the date of its year-end statement of financial position, with limited exceptions. An employer with publicly traded equity securities is required to initially recognize the funded status of a defined benefit postretirement plan and to provide the required disclosures as of the end of the fiscal year ending after December 15, 2006. See Note 1 of the Notes to Consolidated Financial Statements on page F-11 for the effect the adoption of SFAS No. 158 had on the consolidated financial statements.

In September 2006, the SEC staff issued Staff Accounting Bulletin No. 108 "Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements." SAB 108 was issued to provide consistency among registrants in the quantification of financial statement misstatements. SAB 108 established an approach that requires quantification of financial statement misstatements based on the effects of the misstatement on each of the company's financial statements and the related disclosures. SAB 108 allows registrants to initially apply the approach either by (1) retroactively adjusting prior financial statements as if the approach had always been used or (2) recording the cumulative effect of initially applying the approach as adjustments to the carrying values of assets and liabilities as of January 1, 2006 with the related offset recorded to the opening balance of retained earnings. Use of the "cumulative effect" transition requires full disclosure as to the nature and amount of each individual error being corrected. The Company adopted SAB No. 108 as of December 31, 2006. The adoption of SAB No. 108 by the Company did not have a material effect on the Company's consolidated financial statements.

At its September 2006 meeting, the Emerging Issues Task Force ("EITF") reached a final consensus on Issue 06-04, "*Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements.*" In accordance with the EITF consensus, an agreement by an employer to share a portion of the proceeds of a life insurance policy with an employee during the postretirement period is a postretirement benefit arrangement required to be accounted for under SFAS No. 106 and, therefore, a liability for the postretirement obligation must be recognized under SFAS No. 106 if the benefit is offered under an arrangement that constitutes a plan or under APB No. 12 if it is not part of a plan. The provisions of Issue 06-04 are to be applied through either a cumulative -effect adjustment to retained earnings as of the beginning of the year of adoption or retrospective application. Issue 06-04 is effective for annual or interim reporting periods beginning after December 15, 2007. The application of Issue 06-04 is not expected to have a material effect on the Company's financial position or results of operations.

At its September 2006 meeting, the EITF reached a final consensus on Issue 06-05, "*Accounting for Purchases of Life Insurance -Determining the Amount That Could be Realized in Accordance with FASB Technical Bulletin No. 85-4.*" Issue 06-05 concludes that in determining the amount that could be realized under an insurance contract accounted fro under FASB Technical Bulletin No. 85-4, "*Accounting for Purchases of Life Insurance,*" the policyholder should (1) consider any additional amounts included in the contractual terms of the policy; (2) assume the surrender value on an individual life-by individual-life policy basis; and (3) not discount the cash surrender value component of the amount that could be realized when contractual restrictions on the ability to surrender a policy exist. Issue 06-05 should be adopted through either (1) a change in accounting principle through a cumulative-effect adjustment to retained earnings as of the beginning of the year of adoption or (2) a change in accounting principle through retrospective application to all prior periods. Issue 06-05 is effective for fiscal years beginning after December 15, 2006. The application of Issue 06-05 is not expected to have a material effect on the Company's financial position or results of operations.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk.

Market Risk Analysis

To measure the impacts of longer-term asset and liability mismatches beyond two years, the Company utilizes Modified Duration of Equity and Economic Value of Portfolio Equity ("EVPE") models. The modified duration of equity measures the potential price risk of equity to changes in interest rates. A longer modified duration of equity indicates a greater degree of risk to rising interest rates. Because of balance sheet optionality, an EVPE analysis is also used to dynamically model the present value of asset and liability cash flows, with rates ranging up or down 200 basis points. The economic value of equity is likely to be different as interest rates change. Results falling outside prescribed ranges require action by Management. At December 31, 2006 and 2005, the Company's variance in the economic value equity as a percentage of assets with an instantaneous and sustained parallel shift of 200 basis points is within the negative 3% guideline, as shown in the tables below.

The market capitalization of the Company should not be equated to the EVPE, which only deals with the valuation of balance sheet cash flows using conservative assumptions. Calculated core deposit premiums may be less than what is available in an outright sale. The model does not consider potential premiums on floating rate loan sales, the impact of overhead expense, non-interest income, taxes, industry market price multiples and other factors reflected in the market capitalization of a company.

Market Risk Analysis
December 31, 2006

Change in Interest Rates	Flat	-200bp	+200bp
Economic Value of Portfolio Equity	$ 47,670,000	$ 46,869,000	$ 44,183,000
Change		($800,000)	($3,487,000)
Change as a % of assets		(-0.20%)	(-0.89%)

December 31, 2005

Change in Interest Rates	Flat	-200bp	+200bp
Economic Value of Portfolio Equity	$ 44,923,000	$ 43,305,000	$ 42,049,000
Change		($1,617,000)	($2,873,000)
Change as a % of assets		(-0.43%)	(-0.77%)

Item 8. Financial Statements and Supplementary Data.

Reference is made to Item 15(a)(1) and (2) to page F-1 for a list of financial statements and supplementary data required to be filed pursuant to this Item 8. The information required by this Item 8 is provided on pages F-1 through F-23 hereof.

Item 9. Changes In and Disagreements with Accountants on Accounting and Financial Disclosure.

Not applicable.

Item 9A. Controls and Procedures.

The Company's Chief Executive Officer and Chief Financial Officer, with the assistance of other members of the Company's management, have evaluated the effectiveness of the Company's disclosure controls and procedures as of the end of the period covered by this Annual Report on Form 10-K. Based on such evaluation, the Company's Chief Executive Officer and Chief Financial Officers have concluded that the Company's disclosure controls and procedures are effective.

The Company's Chief Executive Officer and Chief Financial Officer have also concluded that there have not been any changes in the Company's internal control over financial reporting during the quarter ended December 31, 2006 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Because the Company is not an "Accelerated Filer" as defined in Rule 12b-2 of the Exchange Act, the Company is not presently required to file *Management's annual report on internal control over financial reporting* and the *Attestation report of the registered public accounting firm* required by Item 308(a) and (b) of Regulation S-K promulgated under the Securities Act of 1933, as amended. Under current rules, because the Company is neither a "large accelerated filer"

nor an “accelerated filer”, the Company is not required to provide management’s report on internal control over financial reporting until the Company files its annual report for 2007 and compliance with the auditor’s attestation report requirement is not required until the Company files its annual report for 2008. The Company currently expects to comply with these requirements at such time as the Company is required to do so.

Item 9B. Other Information.

None.

PART III

Item 10. Directors, Executive Officers and Corporate Governance.

The information required by this item is incorporated by reference to the Company's Proxy Statement for its 2007 Annual Meeting of Shareholders under the caption "Directors and Executive Officers."

Item 11. Executive Compensation.

The information required by this item is incorporated by reference to the Company's Proxy Statement for its 2007 Annual Meeting of Shareholders under the caption "Executive Compensation."

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Shareholder Matters.

Equity Compensation Plan Information

The following table provides information about the Company's common stock that may be issued upon the exercise of options, warrants and rights under all of the Company's equity compensation plans as of December 31, 2006. The information in the table has been adjusted for the 6% stock dividend declared December 21, 2006 and paid January 31, 2007 to shareholders of record on January 23, 2007.

Plan category	Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)	Weighted-average exercise price of outstanding options, warrants and rights (b)	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c)
Equity compensation plans approved by security holders (1)	70,610	$14.20	352,600
Equity compensation plans not approved by security holders (2)	62,241	$6.49	-
Total	132,851	$10.58	352,600

(1) Includes the Company's 1990 Employee Stock Option Plan for Key Employees, 1996 Employee Stock Option Plan, 2000 Employee Stock Option and Restricted Stock Plan, 2005 Equity Incentive Plan and 2006 Directors Stock Plan.

The 1990 Employee Stock Option Plan for Key Employees was adopted by the Board of the Bank and approved by the shareholders of the Bank in March 1990. The 1996 Employee Stock Option Plan was adopted by the Board of the Bank and approved by shareholders of the Bank in March 1997. In 1999, as part of the formation of the Company as a

holding company for the Bank, these plans were each amended so that no further grants may be made thereunder, and each option to purchase one share of Bank common stock was converted into an option to purchase one share of Company common stock.

The Company's 2000 Employee Stock Option and Restricted Stock Plan was adopted by the Board of the Company and approved by the shareholders in April 2000, the Company's 2005 Equity Incentive Plan was adopted by the Board of the Company on February 17, 2005 and approved by the shareholders in May 2005 and the Company's 2006 Directors Stock Plan was adopted by the Board of the Company on March 23, 2006 and approved by the shareholders in May 2006.

(2) Directors Stock Option and Restricted Stock Plan.

The Company's Directors Stock Option and Restricted Stock Plan was adopted by the Board, and became effective, on April 22, 1999, prior to the listing of the Company's common stock on the Nasdaq National Market System. The plan provides for grants of non-qualified stock options and restricted stock awards to directors of the Company and its subsidiaries. Participants in the plan may be granted non-qualified stock options or restricted stock. All stock option grants have an exercise price per share of no less than the fair market value per share of common stock on the grant date and may have a term of no longer than 10 years after the grant date.

The additional information required by this item is incorporated by reference from the Company's Proxy Statement for its 2007 Annual Meeting of Shareholders under the caption "Stock Ownership of Management and Principal Shareholders."

Item 13. Certain Relationships and Related Transactions, and Director Independence.

This information required by this item is incorporated by reference from the Company's Proxy Statement for its 2007 Annual Meeting of Shareholders under the caption "Certain Transactions With Management."

Item 14. Principal Accountant Fees and Services.

The information regarding principal accounting fees and services and the Company's pre-approval policies and procedures for audit and non-audit services provided by the Company's independent accountants is incorporated by reference to the Company's Proxy Statement for its 2007 Annual Meeting of Shareholders under the caption "Principal Accountant Fees and Services."

PART IV

Item 15. Exhibits and Financial Statement Schedules.

(a) Financial Statements and Financial Statement Schedules

The following documents are filed as part of this report:

1. Financial Statements of 1st Constitution Bancorp.

Consolidated Balance Sheet - December 31, 2006 and 2005.

Consolidated Statements of Income - For the Years Ended December 31, 2006, 2005 and 2004.

Consolidated Statements of Changes in Shareholders' Equity - For the Years Ended December 31, 2006, 2005 and 2004.

Consolidated Statements of Cash Flows - For the Years Ended December 31, 2006, 2005, and 2004.

Notes to Consolidated Financial Statements

Report of Independent Registered Public Accounting Firm

These statements are incorporated by reference to the Company's Annual Report to Shareholders for the year ended December 31, 2006.

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2. All schedules are omitted because either they are inapplicable or not required, or because the information required therein is included in the Consolidated Financial Statements and Notes thereto.

3. Exhibits

Exhibit No.		Description
3 (i)		Certificate of Incorporation of the Company (incorporated by reference to Exhibit 3(i) to the Company's Form 10-K filed with the SEC on March 24, 2005).
3 (ii)		Bylaws of the Company (incorporated by reference to Exhibit 3(ii) to the Company's Form 10-QSB filed with the SEC on May 14, 2003)
4.1		Specimen Share of Common Stock (incorporated by reference to the Company's Form 10-KSB filed with the SEC on March 22, 2002)
4.2		Amended and Restated Declaration of Trust of 1st Constitution Capital Trust I dated as of April 10, 2002 among the Registrant, as sponsor, Wilmington Trust Company, as Delaware and institutional trustee, and the Administrators named therein (incorporated by reference to the Company's Form 10-QSB filed with the SEC on May 8, 2002)
4.3		Indenture dated as of April 10, 2002 between the Registrant, as issuer, and Wilmington Trust Company, as trustee, relating to the Floating Rate Junior Subordinated Debt Securities due 2032 (incorporated by reference to the Company's Form 10-QSB filed with the SEC on May 8, 2002)
4.4		Guarantee Agreement dated as of April 10, 2002 between the Registrant and the Wilmington Trust Company, as guarantee trustee (incorporated by reference to the Company's Form 10-QSB filed with the SEC on May 8, 2002)
4.5		Rights Agreement, dated as of March 18, 2004, between 1st Constitution Bancorp and Registrar and Transfer Company, as Rights Agent, including the form of Certificate of Amendment to the Company's Certificate of Incorporation as Exhibit A thereto, the form of Rights Certificates as Exhibit B thereto, and the Summary of Rights as Exhibit C thereto. Pursuant to the Rights Agreement, printed Rights Certificates will not be mailed until after the Distribution Date (as such term is defined in the Rights Agreement) (incorporated by reference to the Company's Form 8-A12G filed with the SEC on March 18, 2004).
10.1	#	1st Constitution Bancorp Supplemental Executive Retirement Plan, dated as of October 1, 2002 (Incorporated by reference to the Company's Form 10-QSB filed with the SEC on November 13, 2002)

10.2	#	Amended and Restated 1st Constitution Bancorp Directors' Insurance Plan, effective as of June 16, 2005 (incorporated by reference to Exhibit No. 10 to the Company's Form 8-K filed with the SEC on March 24, 2006)
10.3	#	1st Constitution Bancorp Form of Executive Life Insurance Agreement (Incorporated by reference to the Company's Form 10-QSB filed with the SEC on November 13, 2002)

Exhibit No.		Description
10.4	#	Amended and Restated 1990 Stock Option Plan for Key Employees, as amended (incorporated by reference to Exhibit No. 10.1 to the Company's Form 10-QSB filed with the SEC on August 9, 2002)
10.5	#	1996 Employee Stock Option Plan, as amended (incorporated by reference to Exhibit No. 10.2 to the Company's Form 10-QSB filed with the SEC on August 9, 2002)
10.6	#	2000 Employee Stock Option and Restricted Stock Plan (incorporated by reference to Exhibit No. 6.3 to the Company's Form 10-SB filed with the SEC on June 15, 2001)
10.7	#	Directors Stock Option and Restricted Stock Plan (incorporated by reference to Exhibit No. 6.4 to the Company's Form 10-SB filed with the SEC on June 15, 2001)
10.8	#	Employment Agreement between the Company and Robert F. Mangano dated April 22, 1999 (incorporated by reference to Exhibit No. 6.5 to the Company's Form 10-SB filed with the SEC on June 15, 2001)
10.9	#	Amendment No. 1 to 1st Constitution Bancorp Supplemental Executive Retirement Plan, effective January 1, 2004 (incorporated by reference to Exhibit 10.12 to the Company's Form 10-Q filed with the SEC on August 11, 2004)
10.10	#	Change of Control Agreement, effective as of April 1, 2004, by and between the Company and Joseph M. Reardon (incorporated by reference to Exhibit 10.13 to the Company's Form 10-Q filed with the SEC on August 11, 2004)
10.11	#	Form of Stock Option Agreement under the 1st Constitution Bancorp Employee Stock Option and Restricted Stock Plan (incorporated by reference to Exhibit 10.14 to the Company's Form 8-K filed with the SEC on December 22, 2004)
10.12	#	Form of Restricted Stock Agreement under the 1st Constitution Bancorp Employee Stock Option and Restricted Stock Plan (incorporated by reference to Exhibit 10.15 to the Company's Form 8-K filed with the SEC on December 22, 2004)
10.13	#	Employment Agreement between the Company and Robert F. Mangano dated February 22, 2005 (incorporated by reference to Exhibit No. 10.16 to the Company's Form 8-K filed with the SEC on February 24, 2005)
10.14	#	

		The 1st Constitution Bancorp 2005 Equity Incentive Plan (incorporated by reference to Appendix A of the Company's proxy statement filed on April 15, 2005).
10.15	#	Form of Restricted Stock Agreement under the 1st Constitution Bancorp 2005 Equity Incentive Plan (incorporated by reference to Exhibit 10.18 to the Company's Form 10-Q filed with the SEC on August 8, 2005).

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Exhibit No.		Description
10.16	#	Form of Nonqualified Stock Option Agreement under the 1st Constitution Bancorp 2005 Equity Incentive Plan (incorporated by reference to Exhibit 10.19 to the Company's Form 10-Q filed with the SEC on August 8, 2005).
10.17	#	Form of Incentive Stock Option Agreement under the 1st Constitution Bancorp 2005 Equity Incentive Plan (incorporated by reference to Exhibit 10.20 to the Company's Form 10-Q filed with the SEC on August 8, 2005).
10.18	#	1st Constitution Bancorp 2006 Directors Stock Plan (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed with the SEC on May 19, 2006)
10.19	#	Form of Nonqualified Stock Option Agreement under the 1st Constitution Bancorp 2006 Directors Stock Plan (incorporated by reference to Exhibit 10.2 to the Company's Form 8-K filed with the SEC on May 19, 2006)
10.20	#	Form of Restricted Stock Agreement under the 1st Constitution Bancorp 2006 Directors Stock Plan (incorporated by reference to Exhibit 10.3 to the Company's Form 8-K filed with the SEC on May 19, 2006)
10.21		Amended and Restated Declaration of Trust of 1st Constitution Capital Trust II, dated as of June 15, 2006, among 1st Constitution Bancorp, as sponsor, the Delaware and institutional trustee named therein, and the administrators named therein (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed with the SEC on June 16, 2006)
10.22		Indenture, dated as of June 15, 2006, between 1st Constitution Bancorp, as issuer, and the trustee named therein, relating to the Floating Rate Junior Subordinated Debt Securities due 2036 (incorporated by reference to Exhibit 10.2 to the Company's Form 8-K filed with the SEC on June 16, 2006)
10.23		Guarantee Agreement, dated as of June 15, 2006, between 1st Constitution Bancorp and the guarantee trustee named therein (incorporated by reference to Exhibit 10.3 to the Company's Form 8-K filed with the SEC on June 16, 2006)
10.24	*#	Amendment No. 2 to 1st Constitution Bancorp Supplemental Executive Retirement Plan, effective January 1, 2005
10.25	#	1st Constitution Bancorp 2005 Supplemental Executive Retirement Plan, effective January 1, 2005 (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed with

		the SEC on December 28, 2006)
10.26		Branch Purchase and Assumption Agreement, dated as of November 6, 2006, by and between 1st Constitution Bank and Sun National Bank (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed with the SEC on November 13, 2006)
14		Code of Business Conduct and Ethics (incorporated by reference to Exhibit 14 to the Company's Form 10-K filed with the SEC on March 25, 2004)
21	*	Subsidiaries of the Company

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Exhibit No.		Description
23.1	*	Consent of Independent Registered Public Accounting Firm
31.1	*	Certification of Robert F. Mangano, Chief Executive Officer of the Company, pursuant to Securities Exchange Act Rule 13a-14(a).
31.2	*	Certification of Joseph M. Reardon, Chief Financial Officer of the Company, pursuant to Securities Exchange Act Rule 13a-14(a).
32	*	Certifications pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of The Sarbanes-Oxley Act of 2002, signed by Robert F. Mangano, Chief Executive Officer of the Company, and Joseph M. Reardon, Chief Financial Officer of the Company.

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* Filed herewith.

Management contract or compensatory plan or arrangement.

(b) **Exhibits**.

Exhibits required by Section 601 of Regulation S-K (see (a) above)

(c) **Financial Statement Schedules**

See the notes to the Consolidated Financial Statements included in this report.

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1ST CONSTITUTION BANCORP

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

1ST CONSTITUTION BANCORP

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Shareholders
1st Constitution Bancorp:

We have audited the accompanying consolidated balance sheet of 1st Constitution Bancorp and subsidiaries as of December 31, 2006 and 2005 and the related consolidated statements of income, changes in shareholders' equity and cash flows for each of the three years in the period ended December 31, 2006. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of 1st Constitution Bancorp and subsidiaries as of December 31, 2006 and 2005 and the consolidated results of their operations and their consolidated cash flows for each of the three years in the period ended December 31, 2006, in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 1 to the consolidated financial statements, the Company has adopted Financial Accounting Standards Board Statement No. 123(R), *Share-Based Payments (SFAS No. 123(R))* in 2006. Also, as discussed in Note 1 to the consolidated financial statements, the Company has adopted Financial Accounting Standards Board No. 158, *Employer's Accounting For Defined Benefit Pension and Other Postretirement Plans, An Amendment of FASB Statements No. 87, 88, 106 and 132(R)* at December 31, 2006.

/s/ GRANT THORNTON LLP

Philadelphia, Pennsylvania
March 30, 2007

1ST CONSTITUTION BANCORP
CONSOLIDATED BALANCE SHEETS
December 31, 2006 and 2005

ASSETS		**2006**		**2005**
CASH AND DUE FROM BANKS	$	10,336,334	$	9,394,929
FEDERAL FUNDS SOLD / SHORT TERM INVESTMENTS		25,478		2,742,821
Total cash and cash equivalents		10,361,812		12,137,750
INVESTMENT SECURITIES				
Available for sale, at fair value		70,421,328		69,236,658
Held to maturity (fair value of $19,164,679 and $21,521,026 in 2006 and 2005, respectively)		19,254,476		21,758,370
Total securities		89,675,804		90,995,028
LOANS HELD FOR SALE		13,608,942		16,757,734
LOANS		265,142,313		240,014,349
Less- Allowance for loan losses		(3,228,360)		(2,361,375)
Net loans		261,913,953		237,652,974
PREMISES AND EQUIPMENT, net		3,033,618		2,596,852
ACCRUED INTEREST RECEIVABLE		2,235,671		1,905,662
BANK-OWNED LIFE INSURANCE		9,179,408		8,828,932
OTHER ASSETS		2,668,338		1,620,534
Total assets	$	392,677,546	$	372,495,466
LIABILITIES AND SHAREHOLDERS' EQUITY				
LIABILITIES:				
Deposits				
Non-interest bearing	$	64,305,445	$	62,686,802
Interest bearing		248,418,977		243,122,665
Total deposits		312,724,422		305,809,467
BORROWINGS		17,200,000		28,500,000
REDEEMABLE SUBORDINATED DEBENTURES		23,712,000		5,155,000
ACCRUED INTEREST PAYABLE		1,957,574		1,288,040
ACCRUED EXPENSES AND OTHER LIABILITIES		1,886,980		1,946,092
Total liabilities		357,480,976		342,698,599
COMMITMENTS AND CONTINGENCIES				
SHAREHOLDERS' EQUITY				
Common stock, no par value; 30,000,000 shares authorized; 3,742,860 and 3,700,254 shares issued and 3,742,662 and 3,643,501 shares outstanding as of December 31, 2006 and 2005, respectively		28,886,105		25,589,320

Retained earnings		7,290,916		5,981,803
Treasury Stock, at cost, 198 shares and 56,753 shares at December 31, 2006 and 2005, respectively		(3,545)		(1,008,998)
Accumulated other comprehensive loss		(976,906)		(765,258)
Total shareholders’ equity		35,196,570		29,796,867
Total liabilities and shareholders’ equity	$	392,677,546	$	372,495,466

The accompanying notes are an integral part of these financial statements

1ST CONSTITUTION BANCORP
CONSOLIDATED STATEMENTS OF INCOME

For the Years Ended December 31, 2006, 2005 and 2004

	2006	2005	2004
INTEREST INCOME:			
Loans, including fees	$ 23,166,544	$ 17,622,128	$ 13,422,067
Securities:			
Taxable	3,448,780	3,017,885	3,196,936
Tax-exempt	604,846	660,878	386,088
Federal funds sold and short-term investments	85,012	27,181	10,977
Total interest income	27,305,182	21,328,072	17,016,068
INTEREST EXPENSE:			
Deposits	6,688,080	4,313,849	3,300,523
Securities sold under agreements to repurchase and other borrowed funds	1,687,749	1,363,507	981,689
Redeemable subordinated debentures	1,141,668	350,823	263,083
Total interest expense	9,517,497	6,028,179	4,545,295
Net interest income	17,787,685	15,299,893	12,470,773
PROVISION FOR LOAN LOSSES	893,500	405,000	240,000
Net interest income after provision for loan losses	16,894,185	14,894,893	12,230,773
NON-INTEREST INCOME:			
Service charges on deposit accounts	668,071	690,104	514,494
Gain on sales of loans	1,072,731	1,444,521	1,373,660
(Losses) gains on sales of investment securities, net	(99,714)	(271,871)	27,545
Income on Bank-owned life insurance	350,476	235,430	312,496
Other income	599,445	548,677	329,047
Total other income	2,591,009	2,646,861	2,557,242
NON-INTEREST EXPENSES:			
Salaries and employee benefits	6,799,619	5,894,200	4,955,587
Occupancy expense	1,434,728	1,365,930	1,071,463
Other operating expenses	3,803,509	3,627,095	2,962,911
Total other expenses	12,037,856	10,887,225	8,989,961
Income before income taxes	7,447,338	6,654,529	5,798,054
INCOME TAXES	2,114,494	2,094,402	1,960,340
Net income	$ 5,332,844	$ 4,560,127	$ 3,837,714

NET INCOME PER SHARE						
Basic	$	1.45	$	1.25	$	1.05
Diluted	$	1.41	$	1.20	$	1.02
WEIGHTED AVERAGE SHARES OUTSTANDING						
Basic		3,674,432		3,659,456		3,655,461
Diluted		3,772,182		3,803,871		3,799,270

The accompanying notes are an integral part of these financial statements

1ST CONSTITUTION BANCORP
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

For the Years Ended December 31, 2006, 2005 and 2004

	Common Stock	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive (Loss) Income	Total Shareholders' Equity
BALANCE, January 1, 2004	$ 19,694,828	$ 3,745,784	($5,517)	$ 150,161	$ 23,585,256
Exercise of stock options, net and issuance of vested shares under employee benefit programs	(290,277)		468,176		177,899
Treasury Stock, 16,661 shares at cost			(549,555)		(549,555)
5% stock dividend declared December 2004, including fractional share cash payments	2,850,851	(2,858,241)			(7,390)
Comprehensive Income:					
Net income - 2004		3,837,714			3,837,714
Unrealized losses on securities available for sale, net of tax benefit of ($151,962)				(253,540)	(253,540)
Comprehensive Income					3,584,174
BALANCE, December 31, 2004	$ 22,255,402	$ 4,725,257	($86,896)	($103,379)	$ 26,790,384
Exercise of stock options, net and issuance of vested shares under employee benefit programs	30,336		338,837		369,173
Treasury Stock, 66,699 shares at cost			(1,260,939)		(1,260,939)
5% stock dividend declared December 2005, including fractional share cash payments	3,303,582	(3,303,582)			-
Comprehensive Income:					
Net income - 2005		4,560,127			4,560,127
Unrealized losses on securities available for sale net of tax benefit of $503,290				(662,631)	(662,631)

Comprehensive Income					3,897,496
BALANCE, December 31, 2005	$ 25,589,320	$ 5,981,802	($1,008,998)	($765,258)	$ 29,796,867
Exercise of stock options, net and issuance of vested shares under employee benefit programs	(822,175)		1,418,000		595,825
Treasury Stock, 21,749 shares at cost			(412,547)		(412,547)
FAS 123R share-based compensation	95,230				95,230
6% stock dividend declared December 2006, including fractional share cash payments	4,023,730	(4,023,730)			-
Adjustment to initially apply FASB Statement No. 158 (net of tax benefit of $257,160)				(499,194)	(499,194)
Comprehensive Income:					
Net income - 2006		5,332,844			5,332,844
Unrealized gains on securities available for sale net of tax benefit of $241,421				287,546	287,546
Comprehensive Income					5,620,390
BALANCE, December 31, 2006	$ 28,886,105	$ 7,290,916	($3,545)	($976,906)	$ 35,196,570

The accompanying notes are an integral part of these financial statements

1ST CONSTITUTION BANCORP
CONSOLIDATED STATEMENTS OF CASH FLOWS
For the Years Ended December 31, 2006, 2005 and 2004

	2006	2005	2004
OPERATING ACTIVITIES:			
Net income	$ 5,332,844	$ 4,560,127	$ 3,837,714
Adjustments to reconcile net income			
to net cash provided by operating activities-			
Provision for loan losses	893,500	405,000	240,000
Depreciation and amortization	627,833	523,441	385,106
Net amortization of premiums on securities	41,405	139,507	350,168
Gains on sales of loans	(1,072,731)	(1,444,521)	(1,373,660)
Losses (gains) on sale of investment securities, net	99,714	271,871	(27,545)
Originations of loans held for sale	(58,696,245)	(73,491,347)	(75,514,197)
Income on Bank-owned life insurance	(350,476)	(235,430)	(312,496)
Proceeds from sales of loans held for sale	62,917,768	68,106,015	82,365,958
Deferred tax benefit	(471,367)	(233,589)	(149,400)
Increase in accrued interest receivable	(330,009)	(461,169)	(275,478)
(Increase) decrease in other assets	(1,370,830)	216,727	289,628
Increase (decrease) increase in accrued interest payable	669,534	306,020	75,444
Decrease (increase) increase in accrued			
expenses and other liabilities	64,073	1,130,089	(245,600)
Net cash provided by (used in) operating activities	8,355,013	(207,259)	9,645,642
INVESTING ACTIVITIES:			
Purchases of securities -			
Available for sale	(17,386,472)	(15,511,405)	(34,116,716)
Held to maturity	-	(9,969,659)	(6,883,726)
Proceeds from maturities and prepayments			
of securities -			
Available for sale	13,736,214	17,074,576	29,011,317
Held to maturity	2,483,768	360,173	894,985
Proceeds from sales of securities available for sale	2,899,385	13,292,413	3,801,399
Purchase of Bank owned life insurance	-	(1,950,000)	-
Net increase in loans	(25,154,480)	(29,410,092)	(46,724,208)

Capital expenditures		(1,064,599)		(796,074)		(1,347,808)
Net cash used in investing activities		(24,486,184)		(26,910,068)		(55,364,757)
FINANCING ACTIVITIES:						
Issuance of common stock, net		595,825		369,173		177,899
Purchase of Treasury Stock		(412,547)		(1,260,939)		(549,555)
Net increase in demand, savings and time deposits		6,914,955		28,922,434		31,533,309
Net decrease in securities sold under agreements to repurchase		-		-		(1,921,015)
Net advances (repayments) in short-term borrowings		(11,300,000)		3,300,000		9,700,000
Proceeds from issuance of trust preferred securities		18,557,000		-		-
Net cash provided by financing activities		14,355,233		31,330,668		38,940,638
(Decrease) increase in cash and						
(Decrease) increase in cash and cash equivalents		(1,775,938)		4,213,341		(6,778,477)
CASH AND CASH EQUIVALENTS						
AT BEGINNING OF YEAR		12,137,750		7,924,409		14,702,886
CASH AND CASH EQUIVALENTS						
AT END OF YEAR	$	10,361,812	$	12,137,750	$	7,924,409
SUPPLEMENTAL DISCLOSURES						
OF CASH FLOW INFORMATION:						
Cash paid during the year for -						
Interest	$	8,847,963	$	5,722,159	$	4,469,851
Income taxes		3,563,872		2,040,016		2,429,565

The accompanying notes are an integral part of these financial statements

1ST CONSTITUTION BANCORP
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2006, 2005 and 2004

1. Summary of Significant Accounting Policies

1ST Constitution Bancorp (the "Company") is a bank holding company registered under the Bank Holding Company Act of 1956, as amended, and was organized under the laws of the State of New Jersey. The Company is parent to 1st Constitution Bank (the "Bank"), a state chartered commercial bank. The Bank provides community banking services to a broad range of customers, including corporations, individuals, partnerships and other community organizations in the central New Jersey area. The Bank conducts its operations through its main office located in Cranbury, New Jersey, and operates nine additional branch offices in downtown Cranbury, Fort Lee, Hamilton Square, Jamesburg, Montgomery, Perth Amboy, Plainsboro, West Windsor, and Princeton, New Jersey.

Basis of Presentation

The accounting and reporting policies of the Company conform to accounting principals generally accepted in the United States of America and to the accepted practices within the banking industry. The following is a description of the more significant of these policies and practices.

Principles Of Consolidation

The accompanying consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, 1ST Constitution Capital Trust I, 1ST Constitution Capital Trust II (the "Trusts") (for periods prior to December 31, 2003) and the Bank and the Bank's wholly-owned subsidiaries, 1ST Constitution Investment Company of Delaware, Inc., FCB Assets Holdings, Inc and 1ST Constitution Title Agency, LLC. All significant inter-company accounts and transactions have been eliminated. In accordance with the Company's adoption of Financial Accounting Interpretation No. 46, Consolidation of Variable Interest Entities, as revised December 2003, the Company de-consolidated the accounts and related activity of 1st Constitution Capital Trust I as of December 31, 2003.

Use of Estimates in the Preparation of Financial Statements

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

Investment Securities

Investment Securities which the Bank has the intent and ability to hold until maturity are classified as held to maturity and are recorded at cost, adjusted for amortization of premiums and accretion of discounts using the interest method.

Investment Securities which are held for indefinite periods of time, which management intends to use as part of its asset/liability management strategy, or that may be sold in response to changes in interest rates, changes in prepayment risk, increased capital requirements or other similar factors, are classified as available for sale and are carried at estimated market value, except for Federal Home Loan Bank stock, which is carried at cost. Unrealized gains and losses on such securities are recorded as a separate component of shareholders' equity. Realized gains and losses, which are computed using the specific identification method, are recognized on a trade date basis.

In November 2005, the FASB issued FASB Staff Position (FSP) FAS 115-1 and FAS 124-1, "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments." This FSP provides guidance on

determining if an investment is considered to be impaired, if the impairment is other-than-temporary and the measurement of an impairment loss. It also includes accounting considerations subsequent to the recognition of an other-than-temporary impairment and requires certain disclosures about unrealized losses that have not been recognized as other-than-temporary impairments. This FSP was effective for reporting periods beginning after December 15, 2005. Adoption of this FSP did not have a material impact on the Company's results of operations or financial position.

Bank-Owned Life Insurance

The Company invests in bank-owned life insurance (BOLI). BOLI involves the purchasing of life insurance by the Company on a chosen group of employees. The Company is the owner and beneficiary of the policies. This pool of insurance, due to the advantages of the Bank, is profitable to the Company. This profitability is used to offset a portion of future benefit cost increases. The Bank's deposits fund BOLI and the earnings from BOLI are recognized as non-interest income.

Loans And Loans Held For Sale

Loans that management intended to hold to maturity are stated at the principal amount outstanding, net of unearned income. Unearned income is recognized over the lives of the respective loans, principally using the effective interest method. Income from direct financing leases is recorded over the life of the lease under the financing method of accounting. The investment includes the sum of aggregate rentals receivable and the estimated residual value of leased equipment, less deferred income. Interest income is generally not accrued on loans, including impaired loans, where interest or principal is 90 days or more past due, unless the loans are adequately secured and in the process of collection, or on loans where management has determined that the borrowers may be unable to meet contractual principal and/or interest obligations. When it is probable that, based upon current information, the Bank will not collect all amounts due under the contractual terms of the loan, the loan is reported as impaired. Smaller balance homogenous type loans, such as residential loans and loans to individuals, which are collectively evaluated, are excluded from consideration for impairment. Loan impairment is measured based upon the present value of the expected future cash flows discounted at the loan’s effective interest rate or the underlying value of collateral for collateral dependent loans. When a loan, including an impaired loan, is placed on non-accrual, interest accruals cease and uncollected accrued interest is reversed and charged against current income. Non-accrual loans are generally not returned to accruing status until principal and interest payments have been brought current and full collectibility is reasonably assured. Cash receipts on non-accrual and impaired loans are applied to principal, unless the loan is deemed fully collectible. Loans held for sale are carried at the aggregate lower of cost or market value. Realized gains and losses on loans held for sale are recognized at settlement date and are determined based on the cost, including deferred net loan origination fees and the costs of the specific loans sold.

The Bank accounts for its transfers and servicing financial assets in accordance with SFAS No. 140, “Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities.” The Bank originates mortgages under a definitive plan to sell or securitize those loans and service the loans owned by the investor. Upon the transfer of the mortgage loans in a sale or a securitization, the Bank records the servicing assets retained in accordance with SFAS No. 140. The Bank records mortgage servicing rights and the loans based on relative fair values at the date of origination.

Mortgage loans originated and intended for sale in the secondary market are carried at the lower aggregate cost or estimated fair value. Gains and losses on sales are also accounted for in accordance with SFAS No. 134, “Accounting for Mortgage Securities Retained after the Securitization of Mortgage Loans Held for Sale by a Mortgage Banking Enterprise”. This statement requires that an entity engage in mortgage banking activities classify the retained mortgage-backed security or other interest, which resulted from the securitizations of a mortgage loan held for sale, based upon its ability and intent to sell or hold these investments.

The Bank enteres into commitments to originate loans whereby the interest rate on the loan is determined prior to funding (rate lock commitments). Rate lock commitments on mortgage loans that are intended to be sold are considered to be derivatives. Time elapsing between the issuance of a loan commitment and closing and sale of the loan generally ranges from 30 to 120 days. The Bank protects itself from changes in interest rates through the use of best efforts forward delivery contracts, whereby the Bank commits to sell a loan at the time the borrower commits to an interest rate with the intent that the buyer has assumed interest rate risk on the loan. As a result, the Bank is not exposed to losses nor will it realize significant gains related to its rate lock commitments due to changes in interest rates.

The market value of rate lock commitments and best efforts contracts is not readily ascertainable with precision because rate lock commitments and best efforts contracts are not actively traded in stand-alone markets. The Bank determines the fair value of rate lock commitments and best efforts contracts by measuring the change in the value of the underlying asset while taking into consideration the probability that the rate lock commitments will close. Due to high correlation between rate lock commitments and best efforts contracts, no gain or loss occurs on the rate lock commitments.

The Bank adopted FASB Interpretation No. 45, “Guarantor’s Accounting and Disclosure Requirements for Guarantees, including Indirect Guarantees of Indebtedness of Others” (FIN 45), on January 1, 2003. FIN 45 requires a guarantor entity, at the inception of a guarantee covered by the measurement provisions of the interpretation, to record a liability for the fair value of the obligation undertaken in issuing the guarantee.

Allowance for Loan Losses

The allowance for loan losses is a valuation reserve available for losses or expected on extensions of credit. Management maintains the allowance for loan losses at a level that is considered adequate to absorb losses on existing loans that may become uncollectible based upon an evaluation of known and inherent risks in the portfolio. Additions to the allowance are made by charges to the provision for loan losses. The evaluation considers a complete review of the following specific factors: historical losses by loan category, non-accrual loans, problem loans as identified through internal classifications, collateral values, and the growth and size of the portfolio. Additionally, current economic conditions and local real estate market conditions are considered.

The methodology includes the segregation of the loan portfolio into loan types with a further segregation into risk rating categories, such as special mention, substandard, doubtful, and loss. This allows for an allocation of the allowance for loan losses by loan type; however, the allowance is available to absorb any loan loss without restriction. Larger balance, non-homogeneous loans representing significant individual credit exposures are evaluated individually through the internal loan review process. It is this process that produces the watch list. The borrower's overall financial condition, repayment sources, guarantors and value of collateral, if appropriate, are evaluated. Based on these reviews, an estimate of probable losses for the individual larger-balance loans are determined, whenever possible, and used to establish loan loss reserves. In general, for non-homogeneous loans not individually assessed, and for homogeneous groups, such as residential mortgages and consumer credits, the loans are collectively evaluated based delinquency status, loan type, and industry historical losses. These loan groups are then internally risk rated.

The watch list includes loans that are assigned a rating of special mention, substandard, doubtful and loss. Loans criticized special mention have potential weaknesses that deserve management's close attention. If uncorrected, the potential weaknesses may result in deterioration of the repayment prospects. Loans classified substandard have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They include loans that are inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. Loans classified doubtful have all the weaknesses inherent in loans classified substandard with the added characteristic that collection or liquidation in full, on the basis of current conditions and facts, is highly improbable. Loans rated as doubtful in whole, or in part, are placed in nonaccrual status. Loans classified as a loss are considered uncollectible and are charged to the allowance for loan losses.

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

Loans are placed in a nonaccrual status when the ultimate collectibility of principal or interest in whole, or part, is in doubt. Past-due loans contractually past-due 90 days or more for either principal or interest are also placed in nonaccrual status unless they are both well secured and in the process of collection. Impaired loans, in accordance with SFAS 114, are evaluated individually.

All, or part, of the principal balance of commercial and commercial real estate loans, and construction loans are charged off to the allowance as soon as it is determined that the repayment of all, or part, of the principal balance is highly unlikely. Consumer loans are generally charged off no later than 120 days past due on a contractual basis, earlier in the event of bankruptcy, or if there is an amount deemed uncollectible.

Premises and Equipment

Premises and equipment are stated at cost less accumulated depreciation and amortization. Depreciation is computed primarily on the straight-line method over the estimated useful lives of the assets. Building, furniture and fixtures, equipment and leasehold improvements are depreciated or amortized over the estimated useful lives of the assets or lease terms, as applicable. Estimated useful lives of building is forty years, furniture and fixtures and equipment are three to fifteen years, and three to ten years for leasehold improvements. Maintenance and repairs are charged to expense as incurred.

The Bank accounts for impairment of long lived assets in accordance with SFAS No. 144 *Accounting for the Impairment of Disposal of Long-Lived Assets*. The standard requires recognition and measurement for the impairment of long lived assets to be held and used or to be disposed of by sale. The Bank had no impaired long lived assets at December 31, 2006 and 2005.

Income Taxes

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carry forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

Other Real Estate

Other real estate is carried at the lower of fair value of the related property, as determined by current appraisals less estimated costs to sell, or the recorded investment in the property. Write-downs on these properties, which occur after the initial transfer from the loan portfolio, are recorded as operating expenses. Costs of holding such properties are charged to expense in the current period. Gains, to the extent allowable, and losses on the disposition of these properties are reflected in current operations.

Share-Based Compensation

The Company maintains the 2006 Directors Stock Plan and the 2005 Equity Incentive Plan. The 2006 Plan allows the Company to grant participants stock options or shares of restricted stock up to an aggregate of 53,000 shares of common stock to non-employee directors of the Company or directors of any of the Company’s subsidiaries. The exercise price of each option is the market price of the Company’s stock on the date of grant. Under this Plan, options may be granted in such amounts and at such times and upon such terms as deemed prudent and reasonable and such grants need not be uniform as to all participants.

The 2005 Equity Incentive Plan allows the Company to grant stock options or restricted stock up to an aggregate of 333,900 shares of the Company’s common stock. The options have a term of up to ten years when they are issued and vest over a four-year period. The exercise price of each option is the market price of the Company’s stock on the date of grant.

Effective January 1, 2006, the Company has adopted FASB Statement No. 123 (R), “Share-Based Payment”. Statement 123 (R) requires that compensation cost relating to share-based payment transactions be recognized in financial statements. The cost is measured based on the fair value of the equity or liability instruments issued.

Statement 123 (R) covers a wide range of share-based compensation arrangements including share options, restricted share plans, performance-based awards, share appreciation rights, and employee share purchase plans.

In addition to the accounting standard that sets forth the financial reporting objectives and related accounting principles, Statement 123 (R) includes an appendix of implementation guidance that provides expanded guidance on measuring the fair value of share-based payment awards.

Statement 123 (R) replaces FASB Statement No. 123, “Accounting for Stock-Based Compensation” and supersedes APB Opinion No. 25, “Accounting For Stock Issued to Employees”. Statement 123, as originally issued in 1995, established as preferable a fair-value-based method of accounting for share-based payment transactions with employees. However, that Statement permitted entities the option of continuing to apply the guidance in Opinion 25, as long as the footnotes to financial statements disclosed what net income would have been had the preferable fair-value-based method been used.

Because the Company adopted Statement 123 (R) using the modified prospective transition method, prior periods have not been restated. Under this method, the Company is required to record compensation expense for all awards granted after the date of adoption and for the unvested portion of previously granted awards that remain outstanding as of the beginning of the period of adoption. The Company measures share-based compensation cost using the Black-Scholes option pricing model for stock option grants. The assumptions used in the option-pricing model in 2006 were: dividend yield of 0%; expected volatility of 26.6%; risk-free interest rate of 4.53% and expected term of 7 years. Although the initial fair value of stock options is not adjusted after the grant date, changes in the Company’s assumptions may change the value of, and therefore the expense related to, future stock option grants. Forfeitures did not affect the calculated expense based upon historical activities of option grantees.

Prior to 2006, stock-based compensation was accounted for under the intrinsic value based method as prescribed by Accounting Principles Board Opinion No. 25, “Accounting for Stock Issued to Employees.” Included in the table below are the pro forma disclosures required by SFAS No. 123, “Accounting for Stock-Based Compensation,” as amended by SFAS No. 148, “Accounting for Stock-Based Compensation - Transaction and Disclosure,” which assumes the fair value based method of accounting had been adopted.

	2005	2004
Net income -		
As reported	$ 4,560,127	$ 3,837,714
Deduct: Stock-based employee compensation determined under fair value based method for stock options, net of related tax effects	40,277	25,538
Pro forma	$ 4,519,850	$ 3,812,175
Net income per share -		
As reported -		
Basic	$ 1.25	$ 1.05
Diluted	$ 1.20	$ 1.02
Pro forma -		
Basic	$ 1.24	$ 1.04
Diluted	$ 1.19	$ 1.01

The fair value of each option grant was estimated on the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions used for grants in 2005 and 2004; dividend yield of 0%; expected volatility of 35% in 2005 and 2004; risk-free interest rates of 4.39%, and 3.60%, respectively; and expected lives of 5 years.

Share-based compensation of $95,230 was recognized for the year ended December 31, 2006, which related to the unvested portion of options to acquire shares of Company common stock granted prior to January 1, 2006. Reported net income, adjusting for share-based compensation that would have been recognized in the adoption of Statement 123 (R) did not change the way that the Company has accounted for stock awards in prior periods and therefore no such change is reflected in the pro forma table above. The Company expenses the fair value of stock awards determined at the grant date on a straight-line basis over the vesting period of the award.

Benefit Plans

The Company provides certain retirement benefits to employees under a 401(k) plan. The Company's contributions to the 401(k) plan are expensed as incurred.

The Company also provides retirement benefits to certain employees under a supplemental executive retirement plan. The plan is unfunded and the Company accrues actuarial determined benefit costs over the estimated service period of the employees in the plan. The Company follows SFAS No. 132, as revised in December 2003, "Employers' Disclosures about Pensions and Other Post-retirement Benefits" and SFAS No. 158, "Employers Accounting for Defined Benefit Pension and Other Post-retirement Plans-an amendment of FASB Statements No. 87, 88, 106 and 132(R). SFAS No. 132 revised employers' disclosures about pension and other post-retirement benefit plans. It requires additional information about changes in the benefit obligation and the fair values of plan assets. It also standardized the requirements for pensions and other postretirement benefit plans to the extent possible, and illustrates combined formats for the presentation of pension plan and other post-retirement benefit plan disclosures. SFAS 158 requires an employer to recognize the over funded or under funded status of a defined benefit postretirement plan (other than a multiemployer plan) as an asset or liability in its statement of financial position and to recognize changes in that funded status in the year in which the changes occur through comprehensive income.

The incremental effect of apply SFAS No. 158 on individual line items in the Consolidated Balance Sheets is as follows (In Thousands):

	Before Application of Statement 158	Adjustments	After Application of Statement 158
Deferred income taxes	$ 1,905	$ 257	$ 2,162
Total Assets	392,421	257	392,678
Other liabilities	1,131	756	1,887
Total liabilities	356,725	756	357,481
Accumulated other comprehensive loss	(478)	(499)	(977)
Total shareholders' equity	$ 35,696	($499)	$ 35,197

Cash And Cash Equivalents

Cash and cash equivalents includes cash on hand, interest and non-interest bearing amounts due from banks, Federal funds sold and short-term investments. Generally, Federal funds are sold and short-term investments are made for a one or two-day period.

Reclassifications

Certain reclassifications have been made to the prior period amounts to conform with the current period presentation.

Earnings Per Share

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

Diluted net income per common share is calculated by dividing net income by the weighted average number of shares outstanding, as adjusted for the assumed exercise of potential common stock options, using the treasury stock method. All share information has been restated for the effect of a 6% stock dividend declared on December 21, 2006 and paid on January 31, 2007 to shareholders of record on January 23, 2007.

The following tables illustrate the reconciliation of the numerators and denominators of the basic and diluted earnings per share (EPS) calculations.

	Year Ended December 31, 2006		
	Income	Weighted-average shares	Per share Amount
Basic EPS			
Net income available to common shareholders	$ 5,332,844	3,674,432	$ 1.45
Effect of dilutive securities			
Options and Grants	-	103,750	(0.04)
Diluted EPS			
Net income available to common shareholders plus assumed conversion	$ 5,332,844	3,772,182	$ 1.41

All options have been included in the computation of diluted earnings per share.

	Year Ended December 31, 2005		
	Income	Weighted-average shares	Per share Amount
Basic EPS			
Net income available to common stockholders	$ 4,560,127	3,659,456	$ 1.25
Effect of dilutive securities			
Options and Grants	-	144,415	(0.05)
Diluted EPS			
Net income available to common stockholders plus assumed conversion	$ 4,560,127	3,803,871	$ 1.20

All options have been included in the computation of diluted earnings per share.

	Year Ended December 31, 2004		
	Income	Weighted-average shares	Per share Amount
Basic EPS			

Net income available to common stockholders	$	3,837,714	3,655,461	$	1.05
Effect of dilutive securities					
Options and Grants		-	143,809		(0.03)
Diluted EPS					
Net income available to common stockholders plus assumed conversion	$	3,837,714	3,799,270	$	1.02

All options have been included in the computation of diluted earnings per share.

Comprehensive Income

SFAS No. 130, "Reporting Comprehensive Income" requires the reporting of comprehensive income, which includes net income as well as certain other items, which results in a charge in equity during the period.

The income tax effects allocated to comprehensive income (loss) are as follows :

	December 31, 2006			December 31, 2005			December 31, 2004		
	Before Tax Amount	Tax Benefit (Expense)	Net of Tax Amount	Before Tax Amount	Tax Benefit (Expense)	Net of Tax Amount	Before Tax Amount	Tax Benefit (Expense)	Net of Tax Amount
Unrealized (losses) gains during the period	$455,076	(233,341)	$221,735	($1,375,153)	$549,399	($825,754)	($377,957)	$141,696	($236,261)
Reclassification Adjustment	(99,714)	33,903	(65,811)	(271,871)	108,748	(163,123)	27,545	(10,266)	17,279
Other Comprehensive Income (loss)	$554,790	($267,244)	$287,546	($1,103,282)	$440,651	($662,631)	($405,502)	$152,962	($253,540)

Variable Interest Entities

Management has determined that the 1ST Constitution Capital Trust I and 1ST Constitution Capital Trust II (together the "Trusts") qualify as variable interest entities under FASB Interpretation 46 ("FIN 46"). The Trusts issued mandatorily redeemable preferred stock to investors and loaned the proceeds to the Company. Each of the Trusts holds, as its sole asset, subordinated debentures issued by the Company. Subsequent to the issuance of FIN 46 and the establishment of Trust I, the FASB issued a revised interpretation, FIN 46(R), the provisions of which were required to be applied to certain variable interest entities, including Trust I, by March 31, 2004, at which time Trust I was deconsolidated.

In March 2005, the Federal Reserve Board adopted a final rule that would continue to allow the inclusion of trust preferred securities in Tier 1 capital, but with stricter quantitative limits. Under the final rule, after a five-year transition period, the aggregate amount of trust preferred securities and certain other capital elements would be limited to 25% of Tier 1 capital elements, net of goodwill. The amount of trust preferred securities and certain other elements in excess of the limit could be included in Tier 2 capital, subject to restrictions. Based on the final rule, the Company included all of its $23.7 million in trust preferred securities in Tier 1 capital at December 31, 2006.

Segment Information

SFAS No. 131, *Segment Reporting*, establishes standards for public business enterprises to report information about operating segments in their annual financial statements and requires that those enterprises report selected information about operating segments in subsequent interim financial reports issued to shareholders. It also established standards for related disclosure about products and services, geographic areas, and major customers. Operating segments are components of an enterprise, which are evaluated regularly by the chief operating decision-maker in deciding how to allocate and assess resources and performance. The Company's chief operating decision-maker is the President and Chief Executive Officer. The Company has applied the aggregation criteria set forth in SFAS No. 131 for its operating segments to create one reportable segment, "Community Banking."

The Company's Community Banking segment consists of construction, commercial, retail and mortgage banking. The Community Banking segment is managed as a single strategic unit, which generates revenue from a variety of

products and services provided by the Company. For example, construction and commercial lending is dependent upon the ability of the Company to fund itself with retail deposits and other borrowings and to manage interest rate and credit risk. This situation is also similar for consumer and residential real estate lending.

Recent Accounting Pronouncements

In February, 2006, the FASB issued SFAS No. 155, “Accounting for Certain Hybrid Financial Instruments - an amendment of FASB Statements No. 133 and 140: (“SFAS 155”), to simplify and make more consistent the accounting for certain financial instruments. SFAF 155 amends SFAS No. 133, “Accounting for Derivative Instruments and Hedging Activities” (“SFAS 133”) and permits fair value re-measurement for any hybrid financial instrument with an embedded derivative that otherwise would require bifurcation, provided that the whole instrument is accounted for on a fair value basis. Prior to fair value measurement, interests in securitized financial assets must be evaluated to identify interests containing embedded derivatives requiring bifurcation. The amendments to SFAS 133 also clarify which interest-only and principal-only strips are not subject to the requirements of SFAS 133, and that concentration of credit risk in the form of subordination are not embedded derivatives. SFAS 155 amends SFAS 140 to allow a qualifying special-purpose entity to hold a derivative financial instrument that pertains to a beneficial interest other than another derivative financial instrument. SFAS 155 applies to all financial instruments acquired or issued after the beginning of an entity’s first fiscal year that begins after September 15, 2006, with earlier application allowed. SFAS 155 is not expected to have a material impact on the Company’s results of operations or financial condition.

In March 2006, the Financial Accounting Standards Board (FASB) issued Statement No. 156 (SFAS 156), Amending "Accounting for separately Recognized Assets and Servicing Liabilities". SFAS 156 amends SFAS No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities." SFAS 156 permits, but does not require, an entity to choose either the amortization method or the fair value measurement method for measuring each class of separately recognized servicing assets and servicing liabilities. SFAS 156 is effective for fiscal years beginning after September 15, 2006 and is not expected to have a material impact on the Company's consolidated financial statements.

In July 2006, FASB issued FASB Interpretation (FIN) 48, "Accounting for Uncertainty in Income Taxes: an interpretation of FASB Statement No. 109, "Accounting for Income Taxes." FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an entity's financial statements in accordance with Statement of SFAS No. 109. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 is effective for fiscal years beginning after December 15**,** 2006 and is currently under evaluation by the Company to determine the impact on the Company's consolidated financial statements.

In September 2006, FASB Issued Statement No. 157 (SFAS 157), **"**Fair Value Measurements" which is effective for fiscal years beginning after November 15, 2007 and for interim periods within those years. This statement defines fair value, establishes a framework for measuring fair value and expands the related disclosure requirements. The Company is currently evaluating the impact the adoption of SFAS No. 157 will have on its consolidated financial statements.

In September 2006, FASB Issued Statement No. 158 (SFAS 158),**"**Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans—an amendment of FASB Statements No. 87, 88, 106, and 132(R)". SFAS 158 requires an employer to recognize the overfunded or underfunded status of a defined benefit postretirement plan (other than a multiemployer plan) as an asset or liability in its statement of financial position and to recognize changes in that funded status in the year in which the changes occur through comprehensive income. This Statement also improves financial reporting by requiring an employer to measure the funded status of a plan as of the date of its year-end statement of financial position, with limited exceptions. An employer with publicly traded equity securities is required to initially recognize the funded status of a defined benefit postretirement plan and to provide the required disclosures as of the end of the fiscal year ending after December 15, 2006. See the table on Page F-11 for the effect the adoption of SFAS No. 158 had on the consolidated financial statements.

In September 2006, the SEC staff issued Staff Accounting Bulletin No. 108 "Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements." SAB 108 was issued to provide consistency among registrants in the quantification of financial statement misstatements. SAB 108 established an approach that requires quantification of financial statement misstatements based on the effects of the misstatement on each of the company's financial statements and the related disclosures. SAB 108 allows registrants to initially apply the approach either by (1) retroactively adjusting prior financial statements as if the approach had always been used or (2) recording the cumulative effect of initially applying the approach as adjustments to the carrying values of assets and liabilities as of January 1, 2006 with the related offset recorded to the opening balance of retained earnings. Use of the "cumulative effect" transition requires full disclosure as to the nature and amount of each individual error being corrected. The Company adopted SAB No. 108 as of December 31, 2006. The adoption of SAB No. 108 by the Company did not have a material effect on the Company's consolidated financial statements.

At its September 2006 meeting, the Emerging Issues Task Force ("EITF") reached a final consensus on Issue 06-04, "*Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements."* In accordance with the EITF consensus, an agreement by an employer to share a portion of the proceeds of a life insurance policy with an employee during the postretirement period is a postretirement benefit arrangement required to be accounted for under SFAS No. 106 and, therefore, a liability for the postretirement

obligation must be recognized under SFAS No. 106 if the benefit is offered under an arrangement that constitutes a plan or under APB No. 12 if it is not part of a plan. The provisions of Issue 06-04 are to be applied through either a cumulative -effect adjustment to retained earnings as of the beginning of the year of adoption or retrospective application. Issue 06-04 is effective for annual or interim reporting periods beginning after December 15, 2007. The application of Issue 06-04 is not expected to have a material effect on the Company’s financial position or results of operations.

At its September 2006 meeting, the EITF reached a final consensus on Issue 06-05, "*Accounting for Purchases of Life Insurance -Determining the Amount That Could be Realized in Accordance with FASB Technical Bulletin No. 85-4.*" Issue 06-05 concludes that in determining the amount that could be realized under an insurance contract accounted fro under FASB Technical Bulletin No. 85-4, "*Accounting for Purchases of Life Insurance,*" the policyholder should (1) consider any additional amounts included in the contractual terms of the policy; (2) assume the surrender value on an individual life-by individual-life policy basis; and (3) not discount the cash surrender value component of the amount that could be realized when contractual restrictions on the ability to surrender a policy exist. Issue 06-05 should be adopted through either (1) a change in accounting principle through a cumulative-effect adjustment to retained earnings as of the beginning of the year of adoption or (2) a change in accounting principle through retrospective application to all prior periods. Issue 06-05 is effective for fiscal years beginning after December 15, 2006. The application of Issue 06-05 is not expected to have a material effect on the Company's financial position or results of operations.

2. Investment Securities

2006	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale-				
U. S. Treasury securities and obligations of U.S. Government sponsored corporations and agencies	$ 35,625,182	$ 124,144	($694,261)	$ 35,055,065
Mortgage backed securities	28,305,557	113,353	(216,111)	28,202,799
Obligations of State and Political subdivisions	3,655,197	15,902	(31,749)	3,639,350
FHLB stock and other securities	3,554,759	304	(30,949)	3,524,114
	$ 71,140,695	$ 253,703	($973,070)	$ 70,421,328
Held to maturity-				
Mortgage backed securities	$ 5,540,670	$ 2,015	($175,826)	$ 5,366,859
Obligations of State and Political subdivisions	13,713,806	131,955	(47,941)	13,797,820
	$ 19,254,476	$ 133,970	($223,767)	$ 19,164,679

2005	Gross Amortized Cost	Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale-				
U. S. Treasury securities and obligations of U.S. Government sponsored corporations and agencies	$ 34,032,814	$ 7,198	($977,560)	$ 33,062,452
Mortgage backed securities	29,250,341	90,286	(302,193)	29,038,434

Obligations of State and							
Political subdivisions		3,855,987		1,333	(65,063)		3,792,257
FHLB stock and other							
securities		3,371,673		-	(28,158)		3,343,515
	$	70,510,815	$	98,817	($1,372,974)	$	69,236,658
Held to maturity-							
Mortgage backed securities	$	5,807,730	$	7,233	($206,275)	$	5,608,688
Obligations of State and							
Political subdivisions		15,950,640		108,525	(146,827)		15,912,338
	$	21,758,370	$	115,758	($353,102)	$	21,521,026

The amortized cost, estimated fair value and weighted average yield of investment securities at December 31, 2006, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. Federal Home Loan Bank stock is included in “Held to maturity - Due in one year or less.”

	Amortized Cost	Fair Value	Weighted Average Yield*
Available for sale-			
Due in one year or less	$ 1,301,989	$ 1,301,354	5.27%
Due after one year through five years	17,420,177	17,352,325	4.67%
Due after five years through ten years	15,836,536	15,698,842	4.22%
Due after ten years	36,581,993	36,068,807	4.73%
Total	$ 71,140,695	$ 70,421,328	5.01%
Held to maturity-			
Due in one year or less	$ 2,363,612	$ 2,351,783	3.47%
Due after one year through five years	2,839,631	2,838,985	5.38%
Due after five years through ten years	3,615,640	3,625,656	5.52%
Due after ten years	10,435,593	10,348,255	5.59%
Total	$ 19,254,476	$ 19,164,679	5.41%

* computed on a tax equivalent basis.

Gross unrealized losses on securities and the estimated market value of the related securities aggregated by security category and length of time that individual securities have been in a continuous unrealized loss position at December 31, 2006 and December 31, 2005 are as follows:

2006	Less than 12 months		12 months or longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. Treasury securities and obligations of U.S. Government sponsored corporations and agencies	$ 83,506	($22)	$ 22,760,194	($694,238)	$ 22,843,700	($694,261)
Mortgage backed securities	6,274,180	(26,241)	13,608,019	(365,697)	19,882,199	(391,937)
Obligations of State and Political Subdivisions	2,395,099	(12,271)	7,274,761	(67,419)	9,669,860	(79,690)
FHLB stock and other securities	967,328	(13,411)	967,960	(17,538)	1,935,288	(30,949)
Total temporarily impaired securities	$ 9,720,113	($51,945)	$ 44,610,934	($1,144,892)	$ 54,331,047	($1,196,837)

2005	Less than 12 months	12 months or longer	Total

	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. Treasury securities and obligations of U.S. Government sponsored corporations and agencies	$ 16,355,981	($335,803)	$ 13,395,221	($641,757)	$ 29,751,202	($977,560)
Mortgage backed securities	25,099,031	(333,369)	3,905,417	(175,099)	29,004,448	(508,468)
Obligations of State and Political Subdivisions	9,849,588	(88,838)	4,597,019	(123,052)	14,446,607	(211,890)
FHLB stock and other securities	0	0	1,435,715	(28,158)	1,435,715	(28,158)
Total temporarily impaired securities	$ 51,304,600	($758,010)	$ 23,333,372	($968,066)	$ 74,637,972	($1,726,076)

U.S. Treasury obligations and direct obligations of U.S. Government agencies: The unrealized losses on investments in these securities were caused by interest rate increases. The contractual terms of these investments do not permit the issuer to settle the securities at a price less than the amortized cost of the investment. Because the Company has the ability and intent to hold these investments until a market price recovery or maturity, these investments are not considered other-than temporarily impaired.

Mortgage-backed securities: The unrealized losses on investments in mortgage-backed securities were caused by interest rate increases. The contractual cash flows of these securities are guaranteed by the issuer, primarily government or government sponsored agencies. It is expected that the securities would not be settled at a price less than the amortized cost of the investment. Because the decline in fair value is attributable to changes in interest rates and not credit quality, and because the Company has the ability and intent to hold these investments until a market price recovery or maturity, these investments are not considered other-than-temporarily impaired.

FHLB stock and other securities: The investments in these securities with unrealized losses are comprised of corporate trust preferred securities that mature in 2027. The unrealized losses on these securities were caused by interest rate increases. The contractual terms of the bonds do not allow the issuer to settle the securities at a price less than the face value of the bonds, which is greater than the amortized cost of the bonds. Because the decline in fair value is attributable to changes in interest rates and not credit quality, and because the Company has the intent and ability to hold these investments until a market price recovery or maturity, these investments are not considered other-than-temporarily impaired.

The Company recorded gross losses on sales of securities available for sale of $99,714 in 2006 and $271,871 in 2005 and gross gains on sales of $27,545 in 2004.

As of December 31, 2006 and 2005, securities having a book value of $28,824,981 and $32,388,166, respectively, were pledged to secure public deposits, other borrowings and for other purposes required by law.

3. Loans and Loans Held for Sale

Loans are as follows:

	2006	2005
Construction loans	$ 125,268,871	$ 109,862,614
Residential real estate loans	7,670,370	8,602,975
Commercial and commercial real estate	114,897,040	104,448,196
Loans to individuals	16,728,025	16,441,994
Lease financing	-	21,073
Deferred loan fees	404,074	466,678
All other	173,933	170,819
	$ 265,142,313	$ 240,014,349

The Bank's business is concentrated in New Jersey, particularly Middlesex, Mercer and Somerset counties. A significant portion of the total loan portfolio is secured by real estate or other collateral located in these areas.

The Bank had residential mortgage loans held for sale of $13,608,942 at December 31, 2006 and $16,757,734 at December 31, 2005. The Bank sells residential mortgage loans in the secondary market on a non-recourse basis. The related loan servicing rights are generally released to the purchaser. Loans held for sale at December 31, 2006 and 2005 are residential mortgage loans that the Bank intends to sell under forward contracts providing for delivery to purchasers generally within a two month period. Changes in fair value of the forward sales contracts, and the related loan origination commitments and closed loans, were not significant at December 31, 2006, 2005, and 2004.

4. Allowance for Loan Losses

A summary of the allowance for loan losses is as follows:

	2006	2005	2004

Balance, beginning of year	$ 2,361,375	$ 2,005,169	$ 1,786,632
Provision charged to operations	893,500	405,000	240,000
Loans charged off	(29,468)	(52,803)	(22,273)
Recoveries of loans charged off	2,953	4,009	810
Balance, end of year	$ 3,228,360	$ 2,361,375	$ 2,005,169

The amount of loans which were not accruing interest amounted to $4,193,209 and $833,150 at December 31, 2006 and 2005, respectively. Impaired loans totaled $4,193,209 and $833,150 at December 31, 2006 and 2005, respectively. There was a valuation allowance of $553,748 on impaired loans at December 31, 2006. There was no valuation allowance on impaired loans at December 31, 2005. Loans 90 days or more past due and still accruing totaled zero at December 31, 2006, $209 at December 31, 2005 and $63,130 at December 31, 2004.

Additional income before taxes amounting to $348,344, $111,340 and $80,698 would have been recognized in 2006, 2005 and 2004, respectively, if interest on all loans had been recorded based upon original contract terms. No interest was recognized on non-accrual loans in 2006, 2005 or 2004. The average recorded investment in impaired loans for the years ended December 31, 2006, 2005 and 2004, was approximately $2,513,180, $941,280, and $690,097, respectively.

5. Loans to Related Parties

Activity related to loans to directors, executive officers and their affiliated interests during 2006 is as follows:

		2006		2005
Balance, beginning of year	$	2,632,162	$	4,491,192
Loans granted		3,154,202		1,201,426
Repayments of loans		(662,304)		(3,060,456)
Balance, end of year	$	5,124,060	$	2,632,162

All such loans were made under customary terms and conditions and were current as to principal and interest payments as of December 31, 2006 and 2005.

6. Premises And Equipment

Premises and equipment consist of the following:

	Estimated Useful Lives		2006		2005
Land		$	241,784	$	241,784
Building	40 Years		735,579		735,579
Leasehold improvements	10 Years		2,011,056		1,379,023
Furniture and equipment	3 - 15 Years		2,364,917		2,845,959
			5,353,336		5,202,345
Less Accumulated depreciation			(2,319,718)		(2,605,493)
		$	3,033,618	$	2,596,852

7. Deposits

Deposits consist of the following:

		2006		2005
Demand				
Non-interest bearing	$	64,305,445	$	62,686,802
Interest bearing		82,113,165		102,479,894
Savings		53,630,726		49,547,438
Time		112,675,086		91,095,333

	$ 312,724,422	$ 305,809,467

Individual time deposits $100,000 or greater amounted to $48,074,279 and $3,385,000 at December 31, 2006 and 2005, respectively. As of December 31, 2006, time certificates of deposit in amounts of $100,000 or more have remaining maturity time as follows:

Maturity Range	Amount
Three months or less	$ 15,367,321
Over three months through six months	15,526,982
Over six months through twelve months	11,850,558
Over twelve months	5,329,418
	$ 48,074,279

8. Borrowings

The balance of borrowings was $17,200,000 at December 31, 2006, consisting of long-term FHLB borrowings of $15,500,000 and overnight funds purchased of $1,700,000. The balance of borrowings at December 31, 2005 consisted of FHLB borrowings of $23,500,000 and overnight funds purchased of $5,000,000.

At December 31, 2006, the Bank maintained an Overnight Line of Credit at the FHLB in the amount of $16,176,500 and a One Month Overnight Repricing Line of Credit of $10,176,500. Advances issued under these programs are subject to FHLB stock level and collateral requirements. Pricing of these advances may fluctuate based on existing market conditions. The Bank also maintains an unsecured federal funds line of $13,500,000 with a correspondent bank.

The Bank purchased four ten-year fixed rate convertible advances from the FHLB that total $15,500,000 in the aggregate. These advances, in the amounts of $3,000,000, $2,500,000, $5,000,000, and $5,000,000 bear interest at the rates of 5.50%, 5.34%, and 5.06%, respectively. These advances are convertible quarterly at the option of the FHLB. These advances are fully secured by marketable securities.

The FHLB advances mature as follows:

	2006
2007	-
2008	-
2009	$ 3,000,000
2010	12,500,000
2011	-
Thereafter	-
	$ 15,500,000

These callable advances have original maturity dates of ten years and call dates of one year to five years. After the original call period expires, the borrowings are callable quarterly. Due to the call provisions, expected maturities could differ from contractual maturities.

Securities sold under agreements to repurchase are summarized as follows:

	2006	2005	2004
Balance outstanding at year end	-	-	-
Weighted average interest rate at year end	-	-	1.27%
Average daily balance outstanding during year	-	-	$ 1,674,172
Weighted average interest rate during year	-	-	1.28%
Highest month-end outstanding balance	-	-	$ 1,941,042

9. Redeemable Subordinated Debentures

On April 10, 2002, 1ST Constitution Capital Trust I ("Trust I"), a statutory business trust and a wholly owned subsidiary of the Company, issued $5.0 million of variable rate Trust Preferred Securities in a pooled institutional placement transaction maturing April 22, 2032. These Subordinated Debentures constitute the sole assets of Trust I. These Subordinated Debentures are redeemable in whole or part prior to maturity after April 22, 2007. Trust I is obligated to distribute all proceeds of a redemption of these Subordinated Debentures, whether voluntary or upon maturity, to holders of the Trust Preferred Securities. The Company's obligation with respect to the Trust Preferred Securities and the Subordinated Debentures, when taken together, provides a full and unconditional guarantee on a subordinated basis by the Company of the obligations of Trust I to pay amounts when due on the Trust Preferred Securities. On February 23, 2007, the Company notified Wilmington Trust Company, as Indenture Trustee, of the Company's intention to redeem on April 22, 2007 the debt securities issued by the Company to Trust I.

On May 30, 2006, 1ST Constitution Bancorp established 1ST Constitution Capital Trust II, a Delaware business trust subsidiary ("Trust II"), for the sole purpose of issuing $18 million of trust preferred securities (the "Capital Securities"). The Capital Securities were issued in connection with a pooled offering involving approximately 50 other financial institution holding companies. All of the Capital Securities were sold to a single pooling vehicle. The proceeds from the sale of the Capital Securities were loaned to the Company under 30-year floating rate junior subordinated debentures issued to Trust II by the Company. The debentures are the only asset of Trust II. Interest payments on the debentures flow through Trust II to the pooling vehicle. Payments of distributions by Trust II to the pooling vehicle are guaranteed by the Company.

Management has determined that the Trust I and Trust II (together the "Trusts") qualify as variable interest entities under FASB Interpretation 46 ("FIN 46"). The Trusts issued mandatorily redeemable preferred stock to investors and loaned the proceeds to the Company. Each of the Trusts holds, as its sole asset, subordinated debentures issued by the Company. Subsequent to the issuance of FIN 46 and the establishment of Trust I, the FASB issued a revised interpretation, FIN 46(R), the provisions of which were required to be applied to certain variable interest entities, including Trust I, by March 31, 2004, at which time Trust I was deconsolidated.

In March 2005, the Federal Reserve Board adopted a final rule that would continue to allow the inclusion of trust preferred securities in Tier 1 capital, but with stricter quantitative limits. Under the final rule, after a five-year transition period, the aggregate amount of trust preferred securities and certain other capital elements would be limited to 25% of Tier 1 capital elements, net of goodwill. The amount of trust preferred securities and certain other elements in excess of the limit could be included in Tier 2 capital, subject to restrictions. Based on the final rule, the Company included all of its $23.7 million in trust preferred securities in Tier 1 capital at December 31, 2006.

10. Income Taxes

The components of income tax expense (benefit) are summarized as follows:

		2006		2005		2004
Federal-						
Current	$	2,109,541	$	1,955,941	$	1,836,439)
Deferred		(401,229)		(198,849)		(127,181)
		1,708,312		1,757,092		1,709,258
State-						
Current		476,320		372,050		273,301
Deferred		(70,138)		(34,740)		(22,219)
		406,182		337,310		251,082
	$	2,114,494	$	2,094,402	$	1,960,340

A comparison of income tax expense at the Federal statutory rate in 2006, 2005 and 2004 to the Company's provision for income taxes is as follows:

		2006		2005		2004
Federal income tax	$	2,532,095	$	2,262,540	$	1,971,338
Add (deduct) effect of:						
State income taxes net of federal income tax effect		268,080		213,276		165,714
Tax-exempt interest income		(205,648)		(224,699)		(131,270)
Bank-owned life insurance		(119,162)		(80,046)		(106,249)

Other items, net		(360,871)		(76,669)		60,807
Provision for income taxes	$	2,114,494	$	2,094,402	$	1,960,340

The tax effects of existing temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities are as follows:

	2006	2005
Deferred tax assets-		
Allowance for loan losses	$ 1,138,234	$ 943,133
Employee Benefits	541,133	327,718
Unrealized loss on securities available for sale	241,655	508,899
Unfunded SERP Liability	257,160	-
Other	41,117	8,221
Total deferred tax assets	2,219,299	1,787,971
Deferred tax liabilities-		
Other	57,016	86,971
Total deferred tax liabilities	57,016	86,971
Net deferred tax asset	$ 2,162,283	$ 1,701,000

Based upon the current facts, management has determined that it is more likely than not that there will be sufficient taxable income in future years to realize the deferred tax assets. However, there can be no assurances about the level of future earnings.

11. Benefit Plans

Retirement Savings Plan

The Bank has a 401(K) plan which covers substantially all employees with six months or more of service. The plan permits all eligible employees to make basic contributions to the plan up to 12% of base compensation. Under the plan, the Bank provided a matching contribution of 50% in 2006, 2005 and 2004 up to 6% of base compensation. Employer contributions to the plan amounted to $85,899 in 2006, $78,899 in 2005, and $67,864 in 2004.

Benefit Plans

The Company also provides retirement benefits to certain employees under a supplemental executive retirement plan. The plan is unfunded and the Company accrues actuarial determined benefit costs over the estimated service period of the employees in the plan. The present value of the benefits accrued under these plans as of December 31, 2006 and 2005 is approximately $1,249,934 and $825,943, respectively, and is included in other liabilities in the accompanying consolidated balance sheet. Compensation expense of $423,991, $339,516 and $420,921 is included in the accompanying consolidated statement of income for the years ended December 31, 2006, 2005 and 2004, respectively.

In connection with the benefit plans, the Bank purchased $6.0 million in life insurance policies on the lives of its executives, directors and divisional officers. During 2005, the Bank purchased an additional $2.0 million. The Bank is the owner and beneficiary of the policies. The cash surrender values of the policies are approximately $9.2 million and $8.8 million as of December 31, 2006 and 2005, respectively.

The following table sets forth the changes in benefit obligations and plan assets of the Company's supplemental executive retirement plan.

	2006	2005
Change in Benefit Obligation		
Benefit obligation, beginning	$ 1,536,624	$ 486,427
Service cost	210,773	164,871
Interest cost	101,633	85,147
Actuarial (gain) loss	-	115,315
Benefits paid	-	-
Plan amendments	157,258	648,864
Benefit obligation, ending	$ 2,006,288	