1ST CONSTITUTION BANCORP
Form 10-Q
November 13, 2009

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2009

or

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

For the transition period from _____ to _____

Commission file Number: 000-32891

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

New Jersey (State of Other Jurisdiction of Incorporation or Organization)	22-3665653 (I.R.S. Employer Identification No.)
2650 Route 130, P.O. Box 634, Cranbury, NJ (Address of Principal Executive Offices)	08512 (Zip Code)

(609) 655-4500
(Issuer's Telephone Number, Including Area Code)

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

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities 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 ý No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T

(§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ¨ No ¨

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

Large accelerated filer	¨	Accelerated filer	¨
Non-accelerated filer (Do not check if a smaller reporting company)	¨	Smaller reporting company	ý

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

As of November 6, 2009, there were 4,267,421 shares of the registrant's common stock, no par value, outstanding.

1ST CONSTITUTION BANCORP

FORM 10-Q

INDEX

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements.

1st Constitution Bancorp and Subsidiaries
Consolidated Balance Sheets
(unaudited)

	September 30, 2009	December 31, 2008
ASSETS		
CASH AND DUE FROM BANKS	$ 87,327,270	$ 14,321,777
FEDERAL FUNDS SOLD / SHORT-TERM INVESTMENTS	11,380	11,342
Total cash and cash equivalents	87,338,650	14,333,119
INVESTMENT SECURITIES:		
Available for sale, at fair value	133,257,485	93,477,023
Held to maturity (fair value of $36,125,840 and $36,140,379 at September 30, 2009 and December 31, 2008, respectively)	36,139,266	36,550,577
Total investment securities	169,396,751	130,027,600
LOANS HELD FOR SALE	16,786,717	5,702,082
LOANS	375,723,296	377,348,416
Less- Allowance for loan losses	(4,111,914)	(3,684,764)
Net loans	371,611,382	373,663,652
PREMISES AND EQUIPMENT, net	2,096,904	2,302,489
ACCRUED INTEREST RECEIVABLE	2,123,538	2,192,601
BANK-OWNED LIFE INSURANCE	10,221,417	9,929,204
OTHER REAL ESTATE OWNED	2,711,043	4,296,536
OTHER ASSETS	5,354,431	3,839,246
Total assets	$ 667,640,833	$ 546,286,529
LIABILITIES AND SHAREHOLDERS' EQUITY		
LIABILITIES:		
Deposits		
Non-interest bearing	$ 75,400,282	$ 71,772,486
Interest bearing	480,772,299	342,912,245
Total deposits	556,172,581	414,684,731
BORROWINGS	27,500,000	51,500,000
REDEEMABLE SUBORDINATED DEBENTURES	18,557,000	18,557,000
ACCRUED INTEREST PAYABLE	1,861,907	1,984,102
ACCRUED EXPENSES AND OTHER LIABILITIES	5,646,385	3,941,044

Total liabilities	609,737,873	490,666,877
COMMITMENTS AND CONTINGENCIES		
SHAREHOLDERS' EQUITY:		
Preferred Stock, no par value; 5,000,000 shares authorized, of which 12,000 shares of Series B, $1,000 liquidation preference, 5% cumulative increasing to 9% cumulative on February 15, 2014, were issued and outstanding at September 30, 2009 and December 31, 2008	11,446,279	11,387,828
Common stock, no par value; 30,000,000 shares authorized; 4,276,764 and 4,204,202 shares issued and 4,267,421 and 4,198,871 shares outstanding at September 30, 2009 and December 31, 2008, respectively	35,540,270	35,180,433
Retained earnings	10,743,839	9,653,923
Treasury Stock, at cost, 9,343 and 5,331 shares at September 30, 2009 and December 31, 2008, respectively	(65,504)	(53,331)
Accumulated other comprehensive income (loss)	238,076	(549,201)
Total shareholders' equity	57,902,960	55,619,652
Total liabilities and shareholders' equity	$ 667,640,833	$ 546,286,529

See accompanying notes to consolidated financial statements.

1

1st Constitution Bancorp and Subsidiaries

Consolidated Statements of Income
(unaudited)

	Three months ended September 30, 2009	Three months ended September 30, 2008	Nine months ended September 30, 2009	Nine months ended September 30, 2008
INTEREST INCOME				
Loans, including fees	$ 6,094,031	$ 6,199,531	$ 18,395,282	$ 18,335,949
Securities				
Taxable	1,211,220	992,777	3,630,530	2,884,520
Tax-exempt	120,790	140,322	373,308	425,399
Federal funds sold and short-term investments	41,134	56,623	73,799	102,571
Total interest income	7,467,175	7,389,253	22,472,919	21,748,439
INTEREST EXPENSE				
Deposits	2,511,377	2,563,263	7,539,760	7,595,593
Securities sold under agreement to repurchase and other borrowed funds	335,789	372,555	1,060,986	1,151,511
Redeemable subordinated debentures	270,480	265,745	803,455	799,742
Total interest expense	3,117,646	3,201,563	9,404,201	9,546,846
Net interest income	4,349,529	4,187,690	13,068,718	12,201,593
Provision for loan losses	505,000	175,000	1,293,000	535,000
Net interest income after provision for loan losses	3,844,529	4,012,690	11,775,718	11,666,593
NON-INTEREST INCOME				
Service charges on deposit accounts	225,772	257,977	680,526	641,421
Gain on sale of loans	596,991	298,342	1,210,177	893,945
Income on bank-owned life insurance	98,886	97,901	292,213	282,546
Other income	311,548	302,554	840,134	730,143
Total non-interest income	1,233,197	956,774	3,023,050	2,548,055
NON-INTEREST EXPENSE				
Salaries and employee benefits	2,595,934	2,177,318	7,117,329	6,228,445
Occupancy expense	464,799	459,958	1,360,471	1,324,396
Data Processing expenses	281,177	230,618	817,057	660,210
FDIC insurance expenses	183,386	58,941	987,169	130,602
Other operating expenses	824,810	981,991	2,880,259	2,596,665
Total non-interest expenses	4,350,106	3,908,826	13,162,285	10,940,318
Income before income taxes	727,620	1,060,638	1,636,483	3,274,330
INCOME TAXES	106,386	278,244	3,949	971,893
Net income	621,234	782,394	1,632,534	2,302,437
Dividends and accretion on preferred stock	176,983	-	542,618	-
Net income available to common shareholders	$ 444,251	$ 782,394	$ 1,089,916	$ 2,302,437
NET INCOME PER COMMON SHARE				

Basic	$ 0.10	$ 0.19	$ 0.26	$ 0.55
Diluted	$ 0.10	$ 0.18	$ 0.26	$ 0.54

See accompanying notes to consolidated financial statements.

1st Constitution Bancorp and Subsidiaries
Consolidated Statements of Changes in Shareholders' Equity
For the Nine Months Ended September 30, 2009 and 2008
(unaudited)

	Preferred Stock	Common Stock	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income (loss)	Sha
BALANCE, January 1, 2008	$-	$32,514,936	$9,009,955	$(18,388)	$(533,186)	$40
Adjustment to initially apply EITF 06-4			(329,706)			(3
Exercise of stock options, net of issuance of vested shares under benefit programs		146,711		35,584		18
Share-based compensation		92,182				92
Treasury stock, shares acquired at cost				(46,417)		(4
Comprehensive Income:						
Net Income for the nine months ended September 30, 2008			2,302,437			2,
Unrealized loss on securities available for sale, net of tax benefit					(19,319)	(1
Unrealized loss on interest rate swap contract net of tax benefit					(158,355)	(1
Minimum pension liability net of tax benefit					72,538	72
Comprehensive Income						2,
Balance, September 30, 2008	$-	$32,753,829	$10,982,686	$(29,221)	$(638,322)	$43
Balance, January 1, 2009	$11,387,828	$35,180,433	$9,653,923	$(53,331)	$(549,201)	$55
Share-based compensation		64,517				64
Treasury stock, shares acquired at cost				(70,478)		(7
Exercise of stock options, net and issuance of vested shares under benefit programs		295,320		58,305		35
Dividends on preferred stock			(461,667)			(4
Preferred stock issuance cost	(22,500)					(2
Accretion of discount on preferred stock	80,951		(80,951)			0

Comprehensive Income:						
Net Income for the nine months ended September 30, 2009			1,632,534			1,
Minimum pension liability, net of tax benefit					51,436	51
Unrealized gain on securities for sale net of tax benefit					643,735	64
Unrealized gain on interest rate swap contract net of tax benefit					92,106	92
Comprehensive Income						2,
Balance, September 30, 2009	$11,446,279	$35,540,270	$10,743,839	$(65,504)	$238,076	$57

See accompanying notes to consolidated financial statements.

3

1st Constitution Bancorp and Subsidiaries

Consolidated Statements of Cash Flows
(unaudited)

	Nine Months Ended September 30, 2009	2008
OPERATING ACTIVITIES:		
Net income	$ 1,632,534	$ 2,302,437
Adjustments to reconcile net income to net cash used in operating activities-		
Provision for loan losses	1,293,000	535,000
Depreciation and amortization	480,488	530,000
Net amortization of premiums and discounts on securities	24,780	69,011
Gains on sales of other real estate owned	(27,776)	-
Gain on sales of loans held for sale	(1,210,177)	(893,945)
Originations of loans held for sale	(121,742,676)	(65,535,874)
Proceeds from sales of loans held for sale	111,868,218	63,229,572
Income on Bank – owned life insurance	(292,213)	(282,546)
Share-based compensation expense	176,517	243,827
Decrease in accrued interest receivable	69,063	497,977
(Increase) in other assets	(2,145,550)	(606,656)
Decrease in accrued interest payable	(122,195)	(111,577)
Increase (decrease) in accrued expenses and other liabilities	1,757,356	(1,042,190)
Net cash used in operating activities	(8,238,631)	(1,064,964)
INVESTING ACTIVITIES:		
Purchases of securities -		
Available for sale	(78,656,269)	(33,765,333)
Held to maturity	(1,619,834)	-
Proceeds from maturities and prepayments of securities -		
Available for sale	40,082,916	21,813,162
Held to maturity	1,950,349	7,363,599
Net increase in loans	(1,069,417)	(68,194,698)
Additional investment in other real estate owned	(400,991)	(1,706,937)
Proceeds from sales of other real estate owned	3,842,947	1,049,582
Capital expenditures	(247,369)	(163,611)
Net cash used in investing activities	(36,117,668)	(73,604,236)
FINANCING ACTIVITIES:		
Exercise of stock options and issuance of Treasury Stock	353,625	182,295
Purchase of Treasury Stock	(70,478)	(46,417)
Dividend paid on preferred stock	(386,667)	-
Preferred stock issuance costs paid	(22,500)	-
Net increase in demand, savings and time deposits	141,487,850	61,244,848
Net (decrease) increase in borrowings	(24,000,000)	21,600,000
Net cash provided by financing activities	117,361,830	82,980,726
Increase in cash and cash equivalents	73,005,531	8,311,526

CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	14,333,119	7,548,102
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ 87,338,650	$ 15,859,628
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Cash paid during the period for -		
Interest	$ 9,526,396	$ 9,658,423
Income taxes	329,160	2,380,200
Non-cash investing activities		
Real estate acquired in full satisfaction of loans in foreclosure	1,828,687	1,389,181

See accompanying notes to consolidated financial statements.

4

1st Constitution Bancorp and Subsidiaries
Notes To Consolidated Financial Statements
September 30, 2009 (Unaudited)

(1) Summary of Significant Accounting Policies

The accompanying unaudited Consolidated Financial Statements include 1st Constitution Bancorp (the "Company"), its wholly-owned subsidiary, 1st Constitution Bank (the "Bank"), and the Bank's wholly-owned subsidiaries, 1st Constitution Investment Company of Delaware, Inc., 1st Constitution Investment Company of New Jersey, Inc., FCB Assets Holdings, Inc. and 1st Constitution Title Agency, LLC. 1st Constitution Capital Trust II, a subsidiary of the Company, is not included in the Company's consolidated financial statements, as it is a variable interest entity and the Company is not the primary beneficiary. All significant intercompany accounts and transactions have been eliminated in consolidation and certain prior period amounts have been reclassified to conform to current year presentation. The accounting and reporting policies of the Company and its subsidiaries conform to accounting principles generally accepted in the United States of America and pursuant to the rules and regulations of the Securities and Exchange Commission (the "SEC") including the instructions to Form 10-Q and Article 8 of Regulation S-X. Certain information and footnote disclosures normally included in financial statements have been condensed or omitted pursuant to such rules and regulations. These Consolidated Financial Statements should be read in conjunction with the audited consolidated financial statements and the notes thereto included in the Company's Form 10-K for the year ended December 31, 2008, filed with the SEC on March 27, 2009.

In the opinion of the Company, all adjustments (consisting only of normal recurring accruals) which are necessary for a fair presentation of the operating results for the interim periods have been included. The results of operations for periods of less than a year are not necessarily indicative of results for the full year.

The Company has evaluated events and transactions occurring subsequent to the balance sheet date of September 30, 2009 for items that should potentially be recognized or disclosed in these financial statements. The evaluation was conducted through November 13, 2009, the date these financial statements were issued.

(2) Net Income Per Common Share

Basic net income per common share is calculated by dividing net income less dividends and discount accretion on preferred stock by the weighted average number of common shares outstanding during each period.

Diluted net income per common share is calculated by dividing net income less dividends and discount accretion on preferred stock by the weighted average number of common shares outstanding, as adjusted for the assumed exercise of stock options and the vesting of unvested Stock Awards (as defined below), using the treasury stock method. All 2008 per common share information has been adjusted for the effect of a 5% stock dividend declared December 18, 2008 and paid on February 2, 2009 to shareholders of record on January 20, 2009.

The following tables illustrate the reconciliation of the numerators and denominators of the basic and diluted earnings per common share (EPS) calculations. Dilutive securities in the tables below exclude common stock options and warrants with exercise prices that exceed the average market price of the Company's common stock during the periods presented. Inclusion of these common stock options and warrants would be anti-dilutive to the diluted earnings per common share calculation.

	Three Months Ended September 30, 2009		
	Income	Weighted-average shares	Per share amount
Basic Earnings Per Common Share			
Net income	$621,234		
Preferred stock dividends and accretion	(176,983)		
Income available to common shareholders	444,251	4,267,614	$0.10
Effect of dilutive securities			
Stock options and unvested stock awards		21,077	
Diluted Earnings Per Common Share			
Income available to common shareholders plus assumed conversion	$444,251	4,288,691	$0.10

	Three Months Ended September 30, 2008		
	Income	Weighted-average shares	Per share Amount
Basic Earnings Per Common Share			
Net income	$782,394		
Preferred stock dividends and accretion	0		
Income available to common shareholders	782,394	4,197,078	$0.19
Effect of dilutive securities			
Stock options and unvested stock awards		37,476	
Diluted Earnings Per Common Share			
Net income available to common shareholders plus assumed conversion	$782,394	4,234,553	$0.18

	Nine Months Ended September 30, 2009		
	Income	Weighted-average shares	Per share Amount
Basic Earnings Per Common Share			
Net income	$1,632,534		
Preferred stock dividends and accretion	(542,618)		
Income available to common shareholders	1,089,916	4,246,960	$0.26
Effect of dilutive securities			
Stock options and unvested stock awards		11,540	
Diluted Earnings Per Common Share			
Income available to common shareholders	$1,089,916	4,258,500	$0.26

plus assumed conversion

6

	Nine Months Ended September 30, 2008		
	Income	Weighted-average shares	Per share Amount
Basic Earnings Per Common Share			
Net income	$2,302,437		
Preferred stock dividends and accretion	-		
Income available to common shareholders	2,302,437	4,191,844	$0.55
Effect of dilutive securities			
Stock options and unvested stock awards		44,503	
Diluted Earnings Per Common Share			
Net income available to common shareholders plus assumed conversion	$2,302,437	4,236,347	$0.54

(3) Investment Securities

Amortized cost, gross unrealized gains and losses, and the estimated fair value by security type are as follows:

September 30, 2009	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	$ 74,172,919	$ 361,104	$ (28,565)	$ 74,505,458
Residential collateralized mortgage obligations	5,538,737	65,426	(106,870)	5,497,293
Residential mortgage backed securities	44,116,647	2,674,046	-	46,790,693
Obligations of State and Political subdivisions	3,180,401	60,207	(87,058)	3,153,550
Trust preferred debt securities	2,456,622	-	(861,031)	1,595,591
Restricted stock	1,689,900	-	-	1,689,900
Mutual fund	25,000	-	-	25,000
	$ 131,180,226	$ 3,160,783	$ (1,083,524)	$ 133,257,485
Held to maturity-				
U. S. Treasury securities and				

obligations of U.S. Government sponsored corporations and agencies	$	10,000,000	$	25,000	$	0		$	10,025,000
Residential collateralized mortgage obligations		5,915,485		196,353		-			6,111,838
Residential mortgage backed securities		6,401,723		96,450		(17,302	)		6,480,871
Obligations of State and Political subdivisions		8,940,998		320,507		-			9,261,505
Trust preferred debt securities		992,905		-		(756,051	)		236,854
Corporate bonds		3,888,155		121,617		-			4,009,772
	$	36,139,266	$	759,927	$	(773,353	)	$	36,125,840

7

Restricted stock at September 30, 2009 consists of $1,674,900 of Federal Home Loan Bank of New York stock and $15,000 of Atlantic Central Bankers Bank stock.

The amortized cost and estimated fair value of investment securities at September 30, 2009, 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 "Available for sale - Due in one year or less."

	Amortized Cost	Fair Value
Available for sale-		
Due in one year or less	$ 3,468,637	$ 3,485,646
Due after one year through five years	53,615,661	53,962,705
Due after five years through ten years	28,711,108	29,137,695
Due after ten years	45,384,820	46,671,439
Total	$ 131,180,226	$ 133,257,485
Held to maturity-		
Due in one year or less	$ 12,837,245	$ 12,914,790
Due after one year through five years	4,492,703	4,659,975
Due after five years through ten years	5,562,003	5,761,873
Due after ten years	13,247,315	12,789,202
Total	$ 36,139,266	$ 36,125,840

Gross unrealized losses on securities and the estimated fair 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 September 30, 2009 are as follows:

September 30, 2009		Less than 12 months		12 months or longer		T
	Number of Securities	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value
U.S. Treasury securities and obligations of U.S. Government sponsored corporations and agencies	6	$8,721,435	$(28,565)	$-	$-	$8,721,435
Residential mortgage backed securities	1	2,914,489	(17,302)	-	-	2,914,489
Residential collateralized mortgage obligations	3	583,825	(848)	466,163	(106,022)	1,049,988
Obligations of State and Political Subdivisions	1	929,225	(87,058)	-	-	929,225
Trust preferred securities	5	0	0	1,832,445	(1,617,082)	1,832,445
Total temporarily impaired securities	16	$13,148,974	$(133,773)	$2,298,608	$(1,723,104)	$15,447,58

U.S. Treasury securities and obligations of U.S. Government sponsored corporations and 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 does not intend to sell these investments and it is not more likely than not that the Company will be required to sell these investments before a market price recovery or maturity, these investments are not considered other-than temporarily impaired.

Collateralized mortgage obligations and mortgaged-backed securities: The unrealized losses on investments in collateral mortgage obligations and 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 does not intend to sell these investments and it is not more likely than not that the Company will be required to sell these investments before a market price recovery or maturity, these investments are not considered other-than-temporarily impaired.

Obligations of State and Political Subdivisions: The unrealized losses or investments in these securities were caused by interest rate increases. 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 does not intend to sell these investments and it is not more likely than not that the Company will be required to sell these investments before a market price recovery or maturity, these investments are not considered other-than-temporarily impaired.

Trust preferred securities: The investments in these securities with unrealized losses are comprised of corporate trust preferred securities that mature in 2027, all but one of which were single-issuer securities. The contractual terms of the trust preferred securities do not allow the issuer to settle the securities at a price less than the face value of the trust preferred securities, which is greater than the amortized cost of the trust preferred securities. None of the corporate issuers have defaulted on interest payments. Because the decline in fair value is attributable to changes in interest rates and the lack of an active trading market for these securities and to a lesser degree market concerns on the issuers' credit quality, and because the Company does not intend to sell these investments and it is not more likely than not that the Company will be required to sell these investments before a market price recovery or maturity, these investments are not considered other-than-temporarily impaired.

(4) Share-Based Compensation

The Company establishes fair value for its equity awards to determine its cost and recognizes the related expense for stock options over the vesting period using the straight-line method. The grant date fair value for stock options is calculated using the Black-Scholes option valuation model.

The Company's stock plans authorize the issuance of an aggregate of 1,119,022 shares of common stock pursuant to awards that may be granted in the form of stock options to purchase common stock ("Options") and awards of shares of common stock ("Stock Awards"). The purpose of the Company's stock-based incentive plans is to attract and retain personnel for positions of substantial responsibility and to provide additional incentive to certain officers, directors, employees and other persons to promote the success of the Company. Under the Company's stock plans, Options expire ten years after the date of grant. Options are granted at the then fair market value of the Company's common stock. As of September 30, 2009, there were 255,956 shares of common stock (as adjusted for the 5% stock dividend declared December 18, 2008 and paid February 2, 2009 to shareholders of record on January 20, 2009) available for Options or Stock Awards under the Company's stock plans.

Stock-based compensation expense related to Options was $64,517 and $92,182 for the nine months ended September 30, 2009 and 2008, respectively.

Option transactions under the Company's stock plans during the nine months ended September 30, 2009 are summarized as follows:

Stock Options	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (years)	Aggregate Intrinsic Value
Outstanding at January 1, 2009	164,041	$9.92		
Options Granted	36,520	9.08		
Options Exercised	(53,218)	4.70		
Options Forfeited	-	-		
Options Expired	-	-		
Outstanding at September 30, 2009	147,343	$11.60	6.4	$34,367
Exercisable at September 30, 2009	96,041	$11.63	5.2	$34,367

The total intrinsic value (market value on date of exercise less grant price) of Options exercised during the nine month period ended September 30, 2009 was $83,322.

Significant assumptions used to calculate the fair value of the Options granted for the nine month period ended September 30, 2009 are as follows:

	January 2009	August 2009
Fair value of Options granted	$ 3.26	$ 2.89
Risk-free rate of return	1.60 %	2.57 %
Expected Option life in years	7	7
Expected volatility	27.58 %	27.58 %
Expected dividends (1)	-	-

(1) To date, the Company has not paid cash dividends on its common stock.

As of September 30, 2009, there was approximately $181,816 of unrecognized compensation costs related to non-vested Option-based compensation arrangements granted under the Company's stock plans. That cost is expected to be recognized over the next four years.

Stock Awards generally vest over a four-year service period on the anniversary of the grant date, except in the case of the Company's highest compensated employee (currently its chief executive officer) for Stock Awards granted on or after June 15, 2009 which related to long term restricted stock awards. Such long-term restricted Stock Awards granted to the highest compensated employee vest 50% immediately following the second anniversary of the Award and 25% immediately following each of the next two anniversaries. In that instance, transferability of the stock received pursuant to a Stock Award is generally tied to repayment of funds received by the Company from the United States Department of the Treasury (the "Treasury") in exchange for preferred stock of the Company and warrants to acquire common stock of the Company. Also, such Stock Awards granted to the Company's highest compensated employee which are long term are subject to forfeiture unless such person performs substantial services for the Company for two years after the date of grant of the Stock Award, except in certain circumstances and even if vested, the Stock Award is not transferable until the Company has repaid the Treasury the funds received with respect to the preferred stock and warrants sold to the Treasury. The release of the transferability restriction is 25% of the Stock Award for each repayment of 25% of the funds originally received by the Company from the Treasury, with an exception from the transferability restriction for the number of shares sufficient to pay taxes arising from the vesting of the Stock Award. Once vested, Stock Awards are irrevocable, except that such Stock Awards are subject to clawback in certain circumstances pursuant to Section 304 of the Sarbanes-Oxley Act of 2002 and pursuant to Section 111 of the Emergency Economic Stabilization Act of 2008 as amended by the American Recovery and Reinvestment Act of 2009. The product of the number of shares granted and the grant date market price of the Company's common stock determine the fair value of shares covered by the Stock Award under the Company's stock plans. Management recognizes compensation expense for the fair value of the shares covered by the Stock Award on a straight-line basis over the requisite service period. Stock-based compensation expense related to Stock Awards was $112,000 and $151,645 for the nine months ended September 30, 2009 and 2008, respectively.

The following table summarizes the non-vested portion of Stock Awards outstanding at September 30, 2009:

Stock Awards	Number of Shares	Average Grant Date Fair Value
Non-vested stock awards at January 1, 2009	30,470	$ 14.80
Shares granted	56,760	8.94
Shares vested	(11,070)	(14.19)
Shares forfeited	-	-
Non-vested stock awards at September 30, 2009	76,160	$ 10.24

As of September 30, 2009, there was approximately $655,691 of unrecognized compensation cost related to non-vested share-based compensation arrangements granted under the Company's stock plans. That cost is expected to be recognized over the next four years.

(5) 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 recognizes the over funded or under funded status of a defined benefit post-retirement 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 components of net periodic expense for the Company's supplemental executive retirement plan for the nine months ended September 30, 2009 and 2008 are as follows:

	Three months ended September 30,		Nine months ended September 30,	
	2009	2008	2009	2008
Service cost	$ 79,544	$ 57,637	$ 220,182	$ 172,911
Interest cost	45,630	39,830	136,890	119,490
Actuarial loss recognized	21,744	15,375	65,232	46,125
Prior service cost recognized	24,750	24,858	74,358	74,574
	$ 171,668	$ 137,700	$ 496,662	$ 413,100

In September 2006, the Financial Accounting Standards Board ("FASB") Emerging Issues Task Force finalized guidance on Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-dollar Life Insurance Arrangements which requires that a liability be recorded during the service period when a split-dollar life insurance agreement continues after participants' employment or retirement. The required accrued liability is based on either the post-employment benefit cost for the continuing life insurance or based on the future death benefit depending on the contractual terms of the underlying agreement. The Company adopted this guidance on January 1, 2008, and recorded a cumulative effect adjustment of $329,706 as a reduction of retained earnings effective January 1, 2008.

(6) Comprehensive Income and Accumulated Other Comprehensive Income (Loss)

The components of accumulated other comprehensive income (loss) and their related income tax effects are as follows:

	September 30, 2009	December 31, 2008
Unrealized holding gains on securities available for sale	$ 2,077,259	$ 926,166
Related income tax effect	(829,997)	(322,639)
	1,247,262	603,527
Unrealized loss on interest rate swap contract	(1,005,799)	(1,159,156)
Related income tax effect	402,497	463,748
	(603,302)	(695,408)
Pension liability	(675,781)	(761,439)
Related income tax effect	269,897	304,119
	(405,884)	(457,320)
Accumulated other comprehensive income (loss)	$ 238,076	$ (549,201)

The components of other comprehensive income (loss) and their related income tax effects for the three and nine month periods ended September 30, 2009 and 2008 are as follows:

	Three Months Ended		Nine Months Ended	
	September 30, 2009	September 30, 2008	September 30, 2009	September 30, 2008
Unrealized holding gain (loss) on securities available for sale	$1,049,862	$767,537	$1,151,093	$(33,041)
Related income tax effect	(473,218)	(258,475)	(507,358)	13,722
	576,644	509,062	643,735	(19,319)
Unrealized gain (loss) on interest rate swap contract	22,877	(151,326)	153,357	(262,763)
Related income tax effect	2,776	60,441	(61,251)	104,408
	25,653	(90,885)	92,106	(158,355)
Pension liability amortization	28,553	40,300	85,658	120,767
Related income tax effect	(13,088)	(16,101)	(34,222)	(48,229)
	15,465	24,199	51,436	72,538
Other comprehensive income (loss)	$617,762	$442,376	$787,277	$(105,136)

(7) Recent Accounting Pronouncements

In April 2009, the Financial Accounting Standards Board ("FASB") issued guidance in regard to determining fair value when the volume and level of activity for an asset or liability have significantly decreased and identifying transactions that are not orderly. This guidance defined fair value as the price that would be received to sell the asset or transfer the liability in an orderly transaction (that is, not a forced liquidation or distressed sale) between market participants at the measurement date under current market conditions and provided additional guidance on determining when the volume and level of activity for the asset or liability has significantly decreased and on identifying circumstances when a transaction may not be considered orderly. The guidance included a list of factors that a reporting entity should evaluate to determine whether there has been a significant decrease in the volume and level of activity for the asset or liability in relation to normal market activity for the asset or liability. When the Company concludes there has been a significant decrease in the volume and level of activity for the asset or liability, further analysis of the information from that market is required and significant adjustments to the related prices may be necessary to estimate fair value. This guidance also clarifies that when there has been a significant decrease in the volume and level of activity for the asset or liability, some transactions may not be orderly. In those situations, the Company must evaluate the weight of the evidence to determine whether the transaction is orderly. The guidance provides a list of circumstances that may indicate that a transaction is not orderly. A transaction price that is not associated with an orderly transaction is given little, if any, weight when estimating fair value. The adoption of this guidance, as required, effective June 30, 2009, did not have a material impact on the Company's consolidated financial statements, although additional disclosure is now required.

In April 2009, the FASB issued guidance on the recognition and presentation of other-than-temporary impairment which clarifies the interaction of the factors that should be considered when determining whether a debt security is other-than-temporarily impaired. For debt securities, management must assess whether (a) it has the intent to sell the security and (b) it is more likely than not that it will be required to sell the security prior to its anticipated recovery. These steps are done before assessing whether the entity will recover the cost basis of the investment. Previously, this assessment required management to assert it has both the intent and the ability to hold a security for a period of time sufficient to allow for an anticipated recovery in fair value to avoid recognizing other-than-temporary impairment. This change does not affect the need to forecast recovery of the value of the security through either cash flows or market price. In instances when a determination is made that an other-than-temporary impairment exists but the investor does not intend to sell the debt security and it is not more likely than not that it will be required to sell the debt security prior to its anticipated recovery, this guidance changes the presentation and amount of the other-than-temporary impairment recognized in the income statement. The other-than-temporary impairment is separated into (a) the amount of the total other-than-temporary impairment related to a decrease in cash flows expected to be collected from the debt security (the credit loss) and (b) the amount of the total other-than-temporary impairment related to all other factors. The amount of the total other-than-temporary impairment related to the credit loss is recognized in earnings. The amount of the total other-than-temporary impairment related to all other factors is recognized in other comprehensive income. The adoption of this guidance, as required, effective June 30, 2009, did not have a material impact on the Company’s consolidated financial statements, although additional disclosure is now required.

In April 2009, the FASB issued guidance on interim disclosures about the fair value of financial instruments which required disclosures about fair value of financial instruments for interim reporting periods of publicly traded companies in addition to the existing annual requirements. The adoption of this guidance, as required, effective June 30, 2009, did not have a material impact on the Company’s consolidated financial statements, although additional disclosure is now required.

In March 2008, the FASB issued guidance on disclosures about derivative instruments and hedging activities that amended earlier guidance to require entities that utilize derivative instruments to provide qualitative disclosures about the objectives and strategies for using derivatives, quantitative data about the fair value of, and gains and losses on, derivative contracts, and details of credit-risk-related contingent features in their hedged positions. Entities are also required to disclose additional information about the amounts and location of derivatives located within the financial statements, how the provisions of the guidance have been applied, and the impact that hedges have on an entity’s financial position, financial performance, and cash flows. This guidance was effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008. The adoption of this guidance did not have a material impact on the Company’s financial statements.

In May 2009, the FASB issued guidance establishing general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued or are available to be issued, setting forth (1) the period after the balance sheet date during which management of a reporting entity should evaluate events or transactions that may occur for potential recognition or disclosure in the financial statements, (2) the circumstances under which an entity should recognize events or transactions occurring after the balance sheet date in its financial statements and (3) the disclosures that an entity should make about events or transactions that occurred after the balance sheet date. This guidance is effective for interim or annual financial periods ending after June 15, 2009.

In June 2009, the FASB issued guidance regarding the accounting for transfers of financial assets that prescribes the information that a reporting entity must provide in its financial reports about a transfer of financial assets; the effects of a transfer on its financial position, financial performance and cash flows; and a transferor’s continuing involvement in transferred financial assets. This guidance specifically removes the concept of a qualifying special-purpose entity and the exception from applying otherwise applicable consolidation requirements to variable interest entities that are qualifying special-purpose entities. It also modifies the financial-components approach used in accounting for transfers. This guidance will be effective for fiscal years beginning after November 15, 2009. We have not determined the effect that the adoption of this guidance will have on our consolidated financial position or results of operations.

In June 2009, the FASB issued amended guidance to require that an enterprise determine whether it's variable interest or interests give it a controlling financial interest in a variable interest entity. The primary beneficiary of a variable interest entity is the enterprise that has both (1) the power to direct the activities of a variable interest entity that most significantly impact the entity's economic performance and (2) the obligation to absorb losses of the entity that could potentially be significant to the variable interest entity or the right to receive benefits from the entity that could potentially be significant to the variable interest entity. This guidance requires ongoing reassessments of whether an enterprise is the primary beneficiary of a variable interest entity and is effective for fiscal years beginning after November 15, 2009. We have not determined the effect that the adoption of this guidance will have on our consolidated financial position or results of operations.

In June 2009, the FASB issued guidance establishing the FASB Accounting Standards Codification (the "Codification") as the source of authoritative accounting principles recognized by the FASB to be applied by nongovernmental entities in preparation of financial statements in conformity with generally accepted accounting principles in the United States for interim and annual periods ending after September 15, 2009. This change did not have an impact on our consolidated financial position or results of operations.

In August 2009, the FASB issued guidance regarding fair value measurements and disclosures to clarify that in circumstances in which a quoted price in an active market for the identical liability is not available, a reporting entity is required to measure fair value using one or more of the following techniques: (1) The quoted price of the identical liability when traded as an asset; (2) Quoted prices for similar liabilities or similar liabilities when traded as assets; or (3) Another valuation technique that is consistent with the principles of Codification Topic 820. Two examples of these techniques would be an income approach, such as a present value technique, or a market approach, such as a technique that is based on the amount at the measurement date that the reporting entity would pay to transfer the identical liability or would receive to enter into the identical liability. When estimating the fair value of a liability, a reporting entity is not required to include a separate input or adjustment to other inputs relating to the existence of a restriction that prevents the transfer of the liability. Both a quoted price in an active market for the identical liability at the measurement date and the quoted price for the identical liability when traded as an asset in an active market when no adjustments to the quoted price of the asset are required are Level 1 fair value measurements. This guidance is effective for the first reporting period (including interim periods) beginning after issuance. This guidance did not have an impact on our consolidated financial position or results of operations.

(8) Fair Value Disclosures

GAAP utilizes a fair value hierarchy that prioritizes the inputs to valuation methods used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are as follows:

Level 1: Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities.

Level 2: Quoted prices in markets that are not active, or inputs that are observable either directly or indirectly, for substantially the full term of the asset or liability.

Level 3: Prices or valuation techniques that require inputs that are both significant to the fair value measurement and unobservable (i.e., supported with little or no market activity).

An asset's or liability's level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement.

A description of the valuation methodologies used for instruments measured at fair value, as well as the general classification of such instruments pursuant to the valuation hierarchy, is set forth below. These valuation methodologies were applied to all of the Company's financial assets and financial liabilities carried at fair value effective January 1, 2008.

In general, fair value is based upon quoted market prices, where available. If such quoted market prices are not available, fair value is based upon internally developed models that primarily use, as inputs, observable market-based parameters. Valuation adjustments may be made to ensure that financial instruments are recorded at fair value. These adjustments may include amounts to reflect counterparty credit quality and counterparty creditworthiness, among other things, as well as unobservable parameters. Any such valuation adjustments are applied consistently over time. The Company's valuation methodologies may produce a fair value calculation that may not be indicative of net realizable value or reflective value or reflective of future values. While management believes the Company's valuation methodologies are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date.

Securities Available for Sale. Securities classified as available for sale are reported at fair value utilizing Level 2 Inputs. For these securities, the Company obtains fair value measurements from an independent pricing service. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the Treasury yield curve, live trading levels, trade execution data, market consensus prepayments speeds, credit information and the security's terms and conditions, among other things.

Impaired loans. Loans included in the following table are those classified as impaired for which the Company has measured impairment generally based on the fair value of the loan's collateral. Fair value is generally determined based upon independent third party appraisals of the properties, or discounted cash flows based on the expected proceeds. These assets are included as Level 3 fair values, based upon the lowest level of input that is significant to the fair value measurements. The fair value consists of the loan balances less specific valuation allowances.

Derivatives. Derivatives are reported at fair value utilizing Level 2 Inputs. The Company obtains dealer quotations to value its interest rate swap.

The following table summarizes financial assets and financial liabilities measured at fair value on a recurring basis, segregated by the level of the valuation inputs within the fair value hierarchy utilized to measure fair value:

	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total Fair Value
September 30, 2009:				
Securities available for sale	$ -	$ 133,257,485	$ -	$ 133,257,485
Derivative liabilities	-	(1,005,799)	-	(1,005,799)
December 31, 2008:				
Securities available for sale	$ -	$ 93,477,023	$ -	$ 93,477,023
Derivative liabilities	-	(1,159,156)	-	(1,159,156)

Certain financial assets and financial liabilities are measured at fair value on a nonrecurring basis; that is, the instruments are not measured at fair value on an ongoing basis but are subject to fair value adjustments in certain circumstances (for example, when there is evidence of impairment). Financial assets and financial liabilities measured at fair value on a non-recurring basis consist of impaired loans as follows:

	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total Fair Value
September 30, 2009:				

Impaired loans	$	-	$	-	$	2,331,418	$	2,331,418
Other real estate owned		-		-		2,711,043		2,711,043
December 31, 2008:								
Impaired loans	$	-	$	-				