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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405) of this chapter is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or 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  Accelerated filer  Non-accelerated filer

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

The approximate aggregate market value of the voting stock held by non-affiliates of the Registrant, based upon the closing price of the Common Stock on June 30, 2006, was \$144,542,441.

The number of shares of the Registrant's common stock outstanding on March 7, 2007 was 6,089,446.

Portions of the following documents are incorporated into the Parts of this Report on Form 10-K indicated below:

The Registrant's definitive Proxy Statement for the 2007 Annual Meeting to be filed pursuant to Regulation 14A filed on or before April 30, 2007 (Part III).

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**PART I**

**DOCUMENTS INCORPORATED BY REFERENCE**

Portions of the Proxy Statement for the Annual Meeting of Shareholders to be held April 27, 2007, dated March 23, 2007, are incorporated by reference into Part III.

**Item 1. Business**

Bridge Bancorp, Inc. (the “Registrant” or “Company”) is a registered bank holding company and is the holding company for The Bridgehampton National Bank (the “Bank”). The Bank was established in 1910 as a national banking association and is headquartered in Bridgehampton, New York. The Registrant was organized as a New York business corporation and incorporated under the laws of the State of New York in 1988, at the direction of the Board of Directors of the Bank for the purpose of becoming a bank holding company pursuant to a plan of reorganization; under which the former shareholders of the Bank became the shareholders of the Company. Since commencing business in March 1989, after the reorganization, the Registrant has functioned primarily as the holder of all of the Bank’s common stock. In May 1999, the Bank established a real estate investment trust subsidiary, Bridgehampton Community, Inc. (“BCI”). The assets transferred to BCI are viewed by the regulators as part of the Bank’s assets in consolidation. The operations of the Bank also include a financial subsidiary, a 100% ownership in an investment in Bridge Abstract LLC (“Bridge Abstract”). Prior to April 1, 2004, Bridgehampton Abstract Holding LLC, which was 100% owned by the Bank and was dissolved January 1, 2005, had a 51% ownership interest in Bridge Abstract

The Bank operates thirteen branches on eastern Long Island. Federally chartered in 1910, the Bank was founded by local farmers and merchants. For nearly a century, the Bank has maintained its focus on building customer relationships in this market area. The mission of the Company is to grow through the provision of exceptional service to its customers, its employees, and the community. The Company strives to achieve excellence in financial performance and build long term shareholder value. The Bank engages in full service commercial and consumer banking business, including accepting time and demand deposits from the consumers, businesses and local municipalities surrounding its branch offices. These deposits, together with funds generated from operations and borrowings, are invested primarily in (1) commercial real estate loans; (2) home equity loans; (3) construction loans; (4) residential mortgages; (5) secured and unsecured commercial and consumer loans; (6) FHLB, FNMA, and FHLMC mortgage-backed securities; (7) New York State and local municipal obligations; and (8) U.S. Treasury and government agency securities. The Bank also offers the CDARS program, providing up to \$20,000,000 of FDIC insurance to its customers. In addition, the Bank offers merchant credit and debit card processing, automated teller machines, cash management services, online banking services, safe deposit boxes and individual retirement accounts. Through its title insurance abstract subsidiary, the Bank acts as a broker for title insurance services. The Bank’s customer base is comprised principally of small businesses, municipal relationships and consumer relationships.

At present, the Registrant has no paid employees. However, the Company has an equity incentive plan under which it may issue shares of the common stock of the Company and its subsidiaries. The Bank employs 128 people on a full-time and part-time basis. The Bank provides a variety of employment benefits and considers its relationship with its employees to be positive.

All phases of the Bank’s business are highly competitive. The Bank faces direct competition from a significant number of financial institutions operating in its market area, many with a statewide or regional presence, and in some cases, a national presence. There is also competition for banking business from competitors outside of its market areas. Most of these competitors are significantly larger than the Bank, and therefore have greater financial and marketing resources and lending limits than those of the Bank. The fixed cost of regulatory compliance remains high for community banks as compared to their larger competitors that are able to achieve economies of scale. The Bank considers its major competition to be local commercial banks as well as other commercial banks with branches in the

Bank's market area. Other competitors include mortgage brokers and financial services firms other than financial institutions such as investment and insurance companies. Increased competition within the Bank's market areas may limit growth and profitability. Additionally, as the Bank's market area expands westward, competitive pressure in new markets is expected to be strong. The title insurance abstract subsidiary also faces competition from other brokers of title insurance as well as directly from the companies that underwrite title insurance. In New York State, title insurance is obtained on most transfers of real estate and mortgage transactions.

The Bank's market area is located on eastern Long Island. Although the Bank does maintain some customer relationships in Riverhead, Brookhaven and Shelter Island towns at this time, the majority of its customer base and all of its existing branches are located in the towns of Southampton, East Hampton, and Southold. The Bank projects a 2007 opening of its first full-service branch facility in the Town of Riverhead, which will be located in Wading River, NY. In December 2005, the Company opened a branch facility in Westhampton Beach. Geographically this location moves the Bank westward and demonstrates the commitment to traditional growth through branch expansion. In January 2007, the Bank opened a state-of-the-art branch facility in the Village of Southampton. The Bank also opened a new branch facility in Cutchogue, NY, in February 2007. The Bank purchased property to construct new branch facilities in the Village of East Hampton and the Town of Southold. Plans for a new East Hampton branch are in

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the municipal approval process. The Bank continues to add to its menu of products and services that meet the needs of consumers and businesses.

Eastern Long Island is semi-rural. Surrounded by water and including the Hamptons and North Fork, the region is a recreational destination for the New York metropolitan area, and a highly regarded resort locale world-wide. While the local economy flourishes in the summer months as a result of the influx of tourists and second homeowners, in recent years, the year-round population has grown considerably resulting in reducing the seasonal fluctuations in the economy. Industries represented in the marketplace include retail establishments; construction and trades; restaurants and bars; lodging and recreation; professional entities; real estate; health services; passenger transportation and agricultural and related businesses. During the last decade, the Long Island wine industry has matured with an increasing number of new wineries and vineyards locating in the region each year. The vast majority of businesses are considered small businesses employing fewer than ten full-time employees. In recent years, more national chains have opened retail stores within the villages on the north and south forks of the island. Major employers in the region include the municipalities, school districts, hospitals, and financial institutions.

The Company, the Bank and its subsidiaries with the exception of the real estate investment trust, which files its own federal and state tax return, report their income on a consolidated basis using the accrual method of accounting and are subject to federal and state income taxation. In general, banks are subject to federal income tax in the same manner as other corporations. However, gains and losses realized by banks from the sale of available for sale securities are generally treated as ordinary income, rather than capital gains or losses. Additionally, the Company can exclude from its income 100% of dividends received from the Bank as a member of the same affiliated group. The Bank is subject to the New York State Franchise Tax on Banking Corporations based on certain criteria. The taxation of net income is similar to federal taxable income subject to certain modifications.

*REGULATION AND SUPERVISION*

The Bridgehampton National Bank is chartered by and is subject to extensive regulation, examination and supervision by the Office of the Comptroller of the Currency (the "OCC"). The Bank is a member of the Federal Home Loan Bank of New York and its deposit accounts are insured up to applicable limits by the Federal Deposit Insurance Corporation (the "FDIC"). The Bank also is a member of the Federal Reserve System. The Bank must file reports with the OCC concerning its activities and financial condition, in addition to obtaining regulatory approvals prior to entering into certain transactions such as mergers with, or acquisitions of, other financial institutions. There are periodic examinations by the OCC to test the compliance with various regulatory requirements.

The Bank is subject to various statutory requirements and rules and regulations promulgated and enforced primarily by the OCC and to a lesser extent the FDIC. These statutes, rules and regulations relate to insurance of deposits, minimum capital requirements, allowable investments, lending authority, mergers, consolidations, issuance of securities, payment of dividends, establishment of branches and other aspects of our business.

This regulation and supervision establishes a comprehensive framework of activities in which the Bank may engage and is intended primarily for the protection of the insurance fund and depositors. The regulatory structure also gives the regulatory authorities extensive discretion in connection with their supervisory and enforcement activities and examination policies, including policies with respect to the classification of assets and the establishment of adequate loan loss reserves.

Bridge Bancorp, Inc., as a bank holding company controlling the Bank, is subject to the Bank Holding Company Act of 1956, as amended ("BHCA"), and the rules and regulations of the Federal Reserve Board under the BHCA applicable to bank holding companies. The Company is required to file reports with, and otherwise comply with the rules and regulations of the Federal Reserve Board. Such regulation and supervision govern the activities in which a bank and its holding company may engage and are intended primarily for the protection of the insurance fund and depositors. These regulatory authorities have extensive enforcement authority over the institutions that they regulate to prohibit or

correct activities that violate law, regulation or a regulatory agreement or which are deemed to be unsafe or unsound banking practices. Enforcement actions may include the appointment of a conservator or receiver, the issuance of a cease and desist order, the termination of deposit insurance, the imposition of civil money penalties on the institution, its directors, officers, employees and institution-affiliated parties, the issuance of directives to increase capital, the issuance of formal and informal agreements, the removal of or restrictions on directors, officers, employees and institution-affiliated parties, and the enforcement of any such mechanisms through restraining orders or other court actions. Any change in laws and regulations, whether by the OCC, the FDIC, the Federal Reserve Board or through legislation, could have a material adverse impact on the Bank and the Company and their operations and stockholders. Additional information on regulatory requirements is set forth in Note 11 to the Consolidated Financial Statements.

Bridge Bancorp, Inc. had nominal results of operations for 2006, 2005 and 2004 on a parent-only basis. Equity incentive plan grants of stock options and stock awards are recorded directly to the holding company. The Company's sources of funds are dependent on dividends from the Bank, its own earnings, additional capital raised and borrowings. The information in this report reflects principally the financial condition and results of operations of the Bank. The Bank's results of operations are primarily dependent on its net

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interest income. The Bank also generates other income, such as fee income on deposit accounts and merchant credit and debit card processing programs, income from its title insurance abstract subsidiary, and net gains on sales of securities and loans. The level of its other expenses, such as salaries and benefits, occupancy and equipment costs, other general and administrative expenses, expenses from its title insurance abstract subsidiary, and income tax expense, further affects the Bank's net income.

The Company files certain reports with the Securities and Exchange Commission under the federal securities laws. The Company's operations are also subject to extensive regulation by other federal, state and local governmental authorities and it is subject to various laws and judicial and administrative decisions imposing requirements and restrictions on part or all of its operations. Management believes that the Company is in substantial compliance, in all material respects, with applicable federal, state and local laws, rules and regulations. Because the Company's business is highly regulated, the laws, rules and regulations applicable to it are subject to regular modification and change. There can be no assurance that these proposed laws, rules and regulations, or any other laws, rules or regulations, will not be adopted in the future, which could make compliance more difficult or expensive or otherwise adversely affect the Company's business, financial condition or prospects.

**EXECUTIVE OFFICERS**

| <b>Name</b>         | <b>Positions held with the Company</b>                             |
|---------------------|--|
| Thomas J. Tobin     | President and Chief Executive Officer                              |
| Howard H. Nolan     | Senior Executive Vice President and Chief Operating Officer        |
| Janet T. Verneuille | Executive Vice President and Chief Financial Officer and Treasurer |

Biographical information of executive officers of the Company who are not directors is as follows:

Janet T. Verneuille, age 46, was promoted to Executive Vice President of the Company in June 2006 and has served as the Company's Senior Vice President since January 2000 and Chief Financial Officer since January 2001 and as Treasurer of the Company since March 2003. Ms. Verneuille served as Vice President and Controller of the Company from October 1995 to 2001.

**OTHER INFORMATION**

Through a link on the Investor Relations section of the Bank's website of [www.bridgenb.com](http://www.bridgenb.com), copies of the Company's Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q and Current Reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) for 15(d) of the Exchange Act, are made available, free of charge, as soon as reasonably practicable after electronically filing such material with, or furnishing it to, the Securities and Exchange Commission. Copies of such reports and other information also are available at no charge to any person who requests them or at [www.sec.gov](http://www.sec.gov). Such requests may be directed to Bridge Bancorp, Inc., Investor Relations, 2200 Montauk Highway, PO Box 3005, Bridgehampton, NY 11932, (631) 537-1000.

*CORPORATE GOVERNANCE*

The Company has a Code of Ethics, which applies to all directors, officers, and employees. The Code of Ethics is posted on the Bank's website at [www.bridgenb.com](http://www.bridgenb.com).

**Item 1A. Risk Factors**

**Concentration of Loan Portfolio**

The Bank generally invests a greater proportion of our assets in loans secured by commercial and residential real estate properties located in eastern Long Island. A downturn in real estate values and economic conditions on eastern Long Island could have a significant impact on the value of collateral securing the loans as well as the ability for the repayment of loans. See a further discussion in "Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations - Financial Condition - Loans."

**Changes in Interest Rates Could Affect Profitability**

The ability to earn a profit, like most financial institutions, depends on the net interest income, which is the difference between the interest income that the Bank earns on its interest-bearing assets, such as loans and investments, and the interest expense which we pay on our interest-bearing liabilities, such as deposits. Our profitability depends on our ability to manage our assets and liabilities during periods of changing market interest rates.

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A sustained decrease in market interest rates could adversely affect our earnings. When interest rates decline, borrowers tend to refinance higher-rate, fixed-rate loans at lower rates. Under those circumstances, we would not be able to reinvest those prepayments in assets earning interest rates as high as the rates on those prepaid loans or in investment securities. In addition, the majority of our loans are at variable interest rates, which would adjust to lower rates.

In a period of rising interest rates, the interest income earned on our assets may not increase as rapidly as the interest paid on our liabilities. In an increasing interest rate environment, our cost of funds is expected to increase more rapidly than interest earned on our loan and investment portfolio as the primary source of funds is deposits with generally shorter maturities than those on our loans and investments. This makes the balance sheet more liability sensitive in the short term.

### Geographic Location

The Bank's market area is in the eastern end of Long Island and its customer base is mainly located in the towns of East Hampton, Southampton and Southold. Competition in the banking and financial services industry is intense. The profitability of the Bank depends on the continued ability to successfully compete. The Bank competes with commercial banks, savings banks, insurance companies, and brokerage and investment banking firms. Many of our competitors have substantially greater resources and lending limits than the Bank and may offer certain services that the Bank does not provide. In addition competitors recently have been offering loans with lower fixed rates and loans with more attractive terms and less stringent credit structures than the Bank has been willing to offer. Additionally, the high cost of living on the twin forks of eastern Long Island creates staff recruitment and retention challenges.

### The Company's Future Depends on Successful Growth of its Subsidiary

The Company's primary business activity for the foreseeable future will be to act as the holding company of the Bank. Therefore, the Company's future profitability will depend on the success and growth of this subsidiary.

### The Loss of Key Personnel Could Impair our Future Success

Our future success depends in part on the continued service of our executive officers, other key management, as well as our staff, and on our ability to continue to attract, motivate, and retain additional highly qualified employees. The loss of services of one or more of our key personnel or our inability to timely recruit replacements for such personnel, or to otherwise attract, motivate, or retain qualified personnel could have an adverse effect on our business, operating results, and financial condition.

### Highly Regulated Environment

We are subject to extensive regulation, supervision and examination by the OCC, FDIC, the Federal Reserve Board and the Securities and Exchange Commission. Such regulation and supervision govern the activities in which a financial institution and its holding company may engage and are intended primarily for the protection of the consumer. Recently regulators have intensified their focus on the USA PATRIOT Act's anti-money laundering and Bank Secrecy Act compliance requirements. In order to comply with regulations, guidelines and examination procedures in this area as well as other areas of the Bank, we have been required to adopt new policies and procedures and to install new systems. We cannot be certain that the policies, procedures, and systems we have in place are flawless and there is no assurance that in every instance we are in full compliance with these requirements. Regulatory authorities have extensive discretion in connection with their supervisory and enforcement activities, including the imposition of restrictions on the operation of an institution. Any change in such regulation and oversight, whether in the form of regulatory policy, regulations, or legislation, may have a material impact on our operations.

### **Item 1B. Unresolved Staff Comments**

None.

### **Item 2. Properties**

At present, the Registrant does not own or lease any property. The Registrant uses the Bank's space and employees without separate payment. Headquarters are located at 2200 Montauk Highway, Bridgehampton, New York 11932. The Bank's internet address is *www.bridgenb.com*

All of the Bank's properties are located on eastern Long Island in New York. The Bank's Main Office in Bridgehampton is owned. The Bank also owns buildings that house its Montauk Branch located at 1 The Plaza, Montauk; its Southold Branch located at 54790 Main Road, Southold; its Westhampton Beach Office at 194 Mill Road, Westhampton Beach; and its Southampton Village Branch located at 150 Hampton Road, Southampton. The Bank currently leases out a portion of the Montauk building, the Westhampton Beach building and space in the former Southampton Village branch building. The Bank leases seven additional properties on eastern Long Island as branch locations at 32845 Main Road, Cutchogue; 26 Park Place, East Hampton; 218 Front Street, Greenport; 48 East Montauk Highway, Hampton Bays; Mattituck Plaza, Main Road, Mattituck; 2 Bay Street, Sag Harbor; and 425 County Road 39A, Southampton. Additionally, the Bank utilizes space for a branch in the retirement community Peconic Landing at 1500 Brecknock Road, Greenport.

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In 2003, the Bank purchased property in the Village of East Hampton and is currently planning construction of a building on that site. The Bank entered into a contract for the purchase of real estate in the Town of Southold which will also be considered as a site for a future branch facility. In 2006 the Bank entered into a lease agreement in Wading River, NY, with the intentions of opening a new branch in this location during the second half of 2007.

**Item 3. Legal Proceedings**

The Registrant and its subsidiary are subject to certain pending and threatened legal actions that arise out of the normal course of business. In the opinion of management at the present time, the resolution of any pending or threatened litigation will not have a material adverse effect on its financial condition or results of operations.

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

No matters were submitted to a vote of the shareholders during the fourth quarter of the fiscal year covered by this report.

**PART II****Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities****COMMON STOCK INFORMATION**

The Company's common stock is traded on the NASDAQ® over the counter bulletin board market under the symbol, "BDGE." The following table details the quarterly high and low bid prices of the Company's common stock and the dividends declared for such periods.

At December 31, 2006 the Company had approximately 610 shareholders of record, not including the number of persons or entities holding stock in nominee or the street name through various banks and brokers.

**COMMON STOCK INFORMATION**

|                    | Stock Prices |          | Dividends |
|--------------------|--------------|----------|-----------|
|                    | High         | Low      | Declared  |
| By Quarter<br>2006 |              |          |           |
| First              | \$ 26.30     | \$ 24.15 | \$ 0.23   |
| Second             | \$ 26.65     | \$ 24.65 | \$ 0.23   |
| Third              | \$ 26.10     | \$ 24.50 | \$ 0.23   |
| Fourth             | \$ 25.85     | \$ 23.75 | \$ 0.23   |
| By Quarter<br>2005 |              |          |           |
| First              | \$ 32.60     | \$ 30.20 | \$ 0.22   |
| Second             | \$ 31.75     | \$ 26.20 | \$ 0.23   |
| Third              | \$ 29.50     | \$ 26.10 | \$ 0.23   |
| Fourth             | \$ 26.50     | \$ 24.25 | \$ 0.23   |

Stockholders received cash dividends totaling \$5,668,000 in 2006 and \$5,551,000 in 2005. The ratio of dividends per share to net income per share was 68.98% in 2006 compared to 58.88% in 2005.

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Pursuant to the regulations of the SEC, the graph below compares the performance of the Company with that of the total return for the NASDAQ® stock market and for certain bank stocks of financial institutions with an asset size \$500 million to \$1 billion, as reported by SNL Financial L.C. from December 31, 2001 through December 31, 2006. The graph assumes the reinvestment of dividends in additional shares of the same class of equity securities as those listed below.

## Bridge Bancorp, Inc.

| <b>December, 31</b>  | 2001   | 2002   | 2003   | 2004   | 2005   | <b>2006</b>   |
|----------------------|--------|--------|--------|--------|--------|---------------|
| <b>Index</b>         |        |        |        |        |        |               |
| Bridge Bancorp, Inc. | 100.00 | 127.05 | 206.18 | 276.94 | 231.15 | <b>232.99</b> |
| NASDAQ®              | 100.00 | 68.76  | 103.67 | 113.16 | 115.57 | <b>127.58</b> |
| Composite            |        |        |        |        |        |               |
| SNL \$500M-\$1B      | 100.00 | 127.67 | 184.09 | 208.62 | 217.57 | <b>247.44</b> |
| Bank Index           |        |        |        |        |        |               |

**ISSUER PURCHASES OF EQUITY SECURITIES**

| Period        | Total Number of Shares Purchased in Month | Average Price Paid per Share | Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs-2006 <sup>(1)</sup> | Maximum Number (or Approximate Dollar Value) of Shares that May Yet Be Purchased Under the Plans or Programs |
|---------------|---|------------------------------|--|--|
| October 2006  | 10,000                                    | \$25.95                      | 141,959  | 167,041  |
| November 2006 | -   | -                            | 141,959  | 167,041  |
| December 2006 | -   | -                            | 141,959  | 167,041  |

(1) The Board of Directors approved a stock repurchase program on March 27, 2006.

- The Board of Directors approved repurchase of shares up to 309,000 shares.
- There is no expiration date for the stock repurchase plan.
- There is no stock repurchase plan that has expired or that has been terminated during the period ended December 31, 2006.

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(In thousands, except per share data and financial ratios)

Set forth below are selected consolidated financial and other data of the Company. The Company's business is primarily the business of the Bank. This financial data is derived in part from, and should be read in conjunction with, the Consolidated Financial Statements of the Company.

| <b>December 31,</b>                                     | <b>2006</b> | <b>2005</b> | <b>2004<sup>(2)</sup></b> | <b>2003<sup>(2)</sup></b> | <b>2002<sup>(2)</sup></b> |
|---|-------------|-------------|---------------------------|---------------------------|---------------------------|
| <b>Selected Financial Data:</b>                         |             |             |                           |                           |                           |
| Securities available for sale                           | \$ 202,590  | \$ 182,801  | \$ 202,042                | \$ 193,699                | \$ 180,800                |
| Securities, restricted                                  | 878         | 1,377       | 1,979                     | 1,642                     | 1,616                     |
| Securities held to maturity                             | 9,444       | 10,012      | 21,213                    | 14,396                    | 11,023                    |
| Total loans   | 325,997     | 302,264     | 296,134                   | 273,188                   | 248,388                   |
| Total assets  | 573,644     | 533,444     | 547,200                   | 511,613                   | 463,986                   |
| Total deposits  | 504,412     | 468,025     | 469,311                   | 457,159                   | 406,409                   |
| Total stockholders' equity                              | 45,539      | 46,651      | 47,213                    | 42,794                    | 39,971                    |
| <b>Year Ended December 31,</b>                          |             |             |                           |                           |                           |
| <b>Selected Operating Data:</b>                         |             |             |                           |                           |                           |
| Total interest income                                   | \$ 32,030   | \$ 28,713   | \$ 26,923                 | \$ 25,968                 | \$ 26,486                 |
| Total interest expense                                  | 8,337       | 4,319       | 2,351                     | 2,601                     | 4,490                     |
| Net interest income                                     | 23,693      | 24,394      | 24,572                    | 23,367                    | 21,996                    |
| Provision for loan losses                               | 85          | 300         | 300                       | -                         | 220                       |
| Net interest income after provision for loan losses     | 23,608      | 24,094      | 24,272                    | 23,367                    | 21,776                    |
| Total other income                                      | 4,413       | 5,105       | 5,440                     | 4,716                     | 3,405                     |
| Total other expenses                                    | 16,002      | 14,647      | 13,564                    | 12,997                    | 11,942                    |
| Income before income taxes                              | 12,019      | 14,552      | 16,148                    | 15,086                    | 13,239                    |
| Provision for income taxes                              | 3,851       | 4,929       | 5,771                     | 5,488                     | 4,722                     |
| Net income  | \$ 8,168    | \$ 9,623    | \$ 10,377                 | \$ 9,598                  | \$ 8,517                  |
| <b>December 31,</b>                                     |             |             |                           |                           |                           |
| <b>Selected Financial Ratios and Other Data:</b>        |             |             |                           |                           |                           |
| Return on average equity                                | 17.68%      | 20.15%      | 22.82%                    | 22.58%                    | 23.93%                    |
| Return on average assets                                | 1.49%       | 1.76%       | 1.89%                     | 1.91%                     | 1.90%                     |
| Average equity to average assets                        | 8.41%       | 8.71%       | 8.30%                     | 8.46%                     | 7.96%                     |
| Dividend payout ratio <sup>(1)</sup>                    | 68.98%      | 58.88%      | 43.39%                    | 50.98%                    | 29.57%                    |
| Diluted earnings per share                              | \$ 1.33     | \$ 1.53     | \$ 1.64                   | \$ 1.53                   | \$ 1.37                   |
| Basic earnings per share                                | \$ 1.33     | \$ 1.54     | \$ 1.66                   | \$ 1.55                   | \$ 1.38                   |
| Cash dividends declared per common share <sup>(1)</sup> | \$ 0.92     | \$ 0.91     | \$ 0.72                   | \$ 0.78                   | \$ 0.41                   |

(1) On December 15, 2003, the Company declared a special dividend of approximately \$1,660,000, or \$0.27 per share.



(2) Amounts have been restated for a three-for-two stock split, in the form of a stock dividend, effective July 9, 2004.

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**Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations**

*PRIVATE SECURITIES LITIGATION REFORM ACT SAFE HARBOR STATEMENT*

This report may contain statements relating to the future results of the Company (including certain projections and business trends) that are considered “forward-looking statements” as defined in the Private Securities Litigation Reform Act of 1995 (the “PSLRA”). Such forward-looking statements, in addition to historical information, which involve risk and uncertainties, are based on the beliefs, assumptions and expectations of management of the Company. Words such as “expects,” “believes,” “should,” “plans,” “anticipates,” “will,” “potential,” “could,” “intend,” “may,” “outlook,” “predict,” “estimates,” “assumes,” “likely,” and variations of such similar expressions are intended to identify such forward-looking statements. Examples of forward-looking statements include, but are not limited to, possible or assumed estimates with respect to the financial condition, expected or anticipated revenue, and results of operations and business of the Company, including earnings growth; revenue growth in retail banking, lending and other areas; origination volume in the Company’s consumer, commercial and other lending businesses; current and future capital management programs; non-interest income levels, including fees from the abstract subsidiary and banking services as well as product sales; tangible capital generation; market share; expense levels; and other business operations and strategies. For this presentation, the Company claims the protection of the safe harbor for forward-looking statements contained in the PSLRA.

Factors that could cause future results to vary from current management expectations include, but are not limited to, changing economic conditions; legislative and regulatory changes; monetary and fiscal policies of the federal government; changes in tax policies; rates and regulations of federal, state and local tax authorities; changes in interest rates; deposit flows; the cost of funds; demand for loan products; demand for financial services; competition; changes in the quality and composition of the Bank’s loan and investment portfolios; changes in management’s business strategies; changes in accounting principles, policies or guidelines; changes in real estate values and other factors discussed elsewhere in this report, factors set forth under Item 1A., Risk Factors, and in other reports filed by the Company with the Securities and Exchange Commission. The forward-looking statements are made as of the date of this report, and the Company assumes no obligation to update the forward-looking statements or to update the reasons why actual results could differ from those projected in the forward-looking statements.

*OVERVIEW*

*Who We Are and How We Generate Income*

Bridge Bancorp, Inc. (“the Company”), a New York corporation, is a single bank holding company formed in 1989. On a parent-only basis, the Company has had minimal results of operations. In the event the Company subsequently expands its current operations, it will be dependent on dividends from its wholly owned subsidiary, The Bridgehampton National Bank (“the Bank”), its own earnings, additional capital raised, and borrowings as sources of funds. The information in this report reflects principally the financial condition and results of operations of the Bank. The Bank’s results of operations are primarily dependent on its net interest income, which is mainly the difference between interest income on loans and investments and interest expense on deposits and borrowings. The Bank also generates other income, such as fee income on deposit accounts and merchant credit and debit card processing programs, income from its title abstract subsidiary, and net gains on sales of securities and loans. The level of its other expenses, such as salaries and benefits, occupancy and equipment costs, other general and administrative expenses, expenses from its title insurance subsidiary, and income tax expense, further affects the Bank’s net income. Certain reclassifications have been made to prior year amounts and the related discussion and analysis to conform to the current year presentation.

*Year to Date and Quarterly Highlights*

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- Returns on average equity and average assets of 17.68% and 1.49% respectively for 2006;
- Net income of \$8,168,000 or \$1.33 per diluted share for 2006 as compared to net income of \$9,623,000 or \$1.53 per diluted share for 2005;
- Net income of \$2,039,000 or \$0.34 per diluted share for the fourth quarter 2006 as compared with \$2,574,000 or \$0.41 per diluted share for the same period one year ago;
  - A net interest margin of 4.8% for 2006 as compared to 4.9% for 2005;
- Total assets of \$573,644,000 at December 31, 2006, an increase of 7.5% over the same date last year;
- Total loans of \$325,997,000, an increase of 7.9% at December 31, 2006 from December 31, 2005;
  - Continued sound credit quality;

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- Total investments of \$212,912,000 at December 31, 2006, an increase of 9.6% over December 31, 2005;
- Balance sheet and interest rate risk management included a repositioning of a portion of the available for sale investment securities portfolio resulting in a net pretax loss of \$257,000 during the first quarter of 2006;
  - Total deposits of \$504,412,000 at December 31, 2006, growth of 7.8% over December 31, 2005;
- The Company's capital levels remain strong with a Tier 1 Capital to Average Assets ratio of 8.3% and the Company is positioned well for future growth. Stockholders' equity totaled \$45,539,000 at December 31, 2006 as compared \$46,651,000 at December 31, 2005;
  - Declaration of cash dividends totaling \$0.92 for 2006;
- Execution of the Bank's branch expansion plan, including completion of the new Southampton Village and Cutchogue facilities, which opened in January and February 2007 respectively; and
  - Regulatory approval for the Bank's 14th branch office which will be located in Wading River, NY.

*Principal Products and Services and Locations of Operations*

The Bank operates thirteen branches on eastern Long Island. Federally chartered in 1910, the Bank was founded by local farmers and merchants. For nearly a century, the Bank has maintained its focus on building customer relationships on eastern Long Island. The Bank engages in full service commercial and consumer banking business, including accepting time and demand deposits from the consumers, businesses and local municipalities surrounding its branch offices. These deposits, together with funds generated from operations and borrowings, are invested primarily in (1) commercial real estate loans; (2) home equity loans; (3) construction loans; (4) residential mortgages; (5) secured and unsecured commercial and consumer loans; (6) FHLB, FNMA, and FHLMC mortgage-backed securities; (7) New York State and local municipal obligations; and (8) U.S. Treasury and government agency securities. In addition, the Bank offers merchant credit and debit card processing, automated teller machines, cash management services, online banking services, safe deposit boxes and individual retirement accounts. Through its title insurance abstract subsidiary, the Bank acts as a broker for title insurance services. The Bank's customer base is comprised principally of small businesses as well as consumer relationships.

*Opportunities and Challenges*

Growing profits in the current flat or inverted yield curve environment presents significant challenges to the Bank since, as a community bank, its income historically relies heavily on the interest rate spread between short term and long term rates. The ability for the Bank to borrow on a short term basis at a lower cost and invest on a long term basis at a higher yield is diminished. As throughout most of 2006, the pressure on net interest income continued through the fourth quarter as the deposit base shifted to more interest bearing deposits resulting in higher funding costs. The yield curve remained flat or slightly inverted throughout the year, and it remains less than certain that it will revert to the steepness of the past in the near future.

The economic and competitive landscape has changed over the past two years. Recognizing that our market areas are generally affluent, large money center banks increasingly meet their funding needs by aggressively pricing deposits in the Bank's markets. Competition for deposits and loans is intense as various banks in the marketplace, large and small, promise excellent service yet often price their products irrationally. Deposit growth is essential to the Bank's ability to

raise earnings therefore branch expansion and building share in our existing markets remain key strategic goals. Controlling funding costs yet protecting the deposit base along with focusing on profitable growth, presents a unique set of challenges in this operating environment.

The net interest margin was 4.8% for the year ended December 31, 2006 as compared to 4.9% for the year ended December 31, 2005. Net interest income declined \$701,000 in 2006 versus 2005 principally from increased funding costs of rate sensitive municipal and promotional deposit products. Non-interest income also declined, largely the result of a decrease in Bridge Abstract income from the prior year, principally due to a slowdown in real estate closings in our markets.

Non-interest expense increased 9.3% primarily due to increased expenses related to salaries and benefits as well as systems services. Presently resources are in place to support franchise growth. Management recognizes that slowing the growth of non-interest expense relative to revenues will be important to improving the net income trend going into 2007.

Total loans grew 7.9% or \$23.7 million over year end 2005 to \$326.0 million at December 31, 2006.

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The pace of loan originations continued to pick up during the fourth quarter, and the Company is optimistic regarding the continued up tick in loan growth going into 2007. Additionally, during the fourth quarter total investment securities increased to \$212,912,000 at December 31, 2006.

The Bank's loan portfolio remains heavily weighted toward real estate collateralized loans. As such, management carefully monitors the loan portfolio as well as real estate trends on eastern Long Island. During the fourth quarter of 2006, \$85,000 was added to the allowance for loan losses, due primarily to growth in the loan portfolio during the second half of the year. The loan loss reserve remains healthy relative to existing nonperforming assets. By maintaining conservative underwriting criteria, the Company believes it will be better positioned against declining credit quality should there be a weakening of the local real estate market.

Asset growth was funded by an increase in total deposits of 7.8% over 2005, primarily driven by increases in municipal and promotional deposits. Demand deposits at December 31, 2006 totaled \$173.6 million, comprising 34.4% of total deposits at that date. During the third and fourth quarter of 2006, the Bank introduced additional consumer deposit products with the objectives of promoting deposit growth among existing and new customers, as well as supporting customer retention. Core deposits are important relative to funding costs, and the Bank remains committed to growing its deposit base through increased market share in existing markets and continued branch expansion. The Bank's Southampton Village facility opened during January 2007, enhancing the Bank's presence in the market. Opened in February 2007, the Bank's Cutchogue, NY location supports the Bank's position on the North Fork. The Bank anticipates opening a branch in Wading River, NY during the second half of 2007. These branch facilities are expected to strengthen the Bank's franchise value and broaden its footprint.

Corporate objectives for 2007 include: attention to opportunities and processes that enhance the customer experience at the Bank; improving operational efficiencies and slowing growth in non-interest expense relative to revenues; and exploring ways to maximize non-interest revenues through building Bridge Abstract as well as other lines of business. Company planning includes prioritizing the allocation of resources relative to the potential for future revenues. The ability to attract, retain, train and cultivate employees at all levels of the operation remains significant to meeting these objectives.

*CRITICAL ACCOUNTING POLICIES*

Note 1 to our Consolidated Financial Statements for the year ended December 31, 2006 contains a summary of our significant accounting policies. Various elements of our accounting policies, by their nature, are inherently subject to estimation techniques, valuation assumptions and other subjective assessments. Our policy with respect to the methodologies used to determine the allowance for loan losses is our most critical accounting policy. This policy is important to the presentation of our financial condition and results of operations, and it 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. The use of different judgments, assumptions and estimates could result in material differences in our results of operations or financial condition.

The following is a description of our critical accounting policy and an explanation of the methods and assumptions underlying its application.

*ALLOWANCE FOR LOAN LOSSES*

Management considers the accounting policy on loans and the related allowance for loan losses to be the most critical and requires complex management judgment as discussed below. The judgments made regarding the allowance for loan losses can have a material effect on the results of operations of the Company.

The allowance for loan losses is established and maintained through a provision for loan losses based on probable incurred losses inherent in the Bank's loan portfolio. Management evaluates the adequacy of the allowance on a quarterly basis. The allowance is comprised of both individual valuation allowances and loan pool valuation allowances. If the allowance for loan losses is not sufficient to cover actual loan losses, the Company's earnings could decrease.

The Bank monitors its entire loan portfolio on a regular basis, with consideration given to detailed analysis of classified loans, repayment patterns, probable incurred losses, past loss experience, current economic conditions, and various types of concentrations of credit. Additions to the allowance are charged to expense and realized losses, net of recoveries, are charged to the allowance.

Individual valuation allowances are established in connection with specific loan reviews and the asset classification process including the procedures for impairment testing under Statement of Accounting Standard ("SFAS") No. 114, "*Accounting by Creditors for Impairment of a Loan, an Amendment of FASB Statements No. 5 and 15,*" and SFAS No. 118, "*Accounting by Creditors for Impairment of a Loan - Income Recognition and Disclosures, an Amendment of SFAS No. 114.*" Such valuation, which includes a review of loans for which full collectibility in accordance with contractual terms is not reasonably assured, considers the estimated fair value of the underlying collateral less the costs to sell, if any, or the present value of expected future cash flows, or the loan's

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observable market value. Any shortfall that exists from this analysis results in a specific allowance for the loan. Pursuant to our policy, loan losses must be charged-off in the period the loans, or portions thereof, are deemed uncollectible. Assumptions and judgments by management, in conjunction with outside sources, are used to determine whether full collectibility of a loan is not reasonably assured. These assumptions and judgments also are used to determine the estimates of the fair value of the underlying collateral or the present value of expected future cash flows or the loan's observable market value. Individual valuation allowances could differ materially as a result of changes in these assumptions and judgments. Individual loan analyses are periodically performed on specific loans considered impaired. The results of the individual valuation allowances are aggregated and included in the overall allowance for loan losses.

Loan pool valuation allowances represent loss allowances that have been established to recognize the inherent risks associated with our lending activities, but which, unlike individual allowances, have not been allocated to particular problem assets. Pool evaluations are broken down as follows: first, loans with homogenous characteristics are pooled by loan type and include home equity loans, residential mortgages, land loans and consumer loans. Then all remaining loans are segregated into pools based upon the risk rating of each credit. Key factors in determining a credit's risk rating include management's evaluation of: cash flow, collateral, guarantor support, financial disclosures, industry trends and management. The determination of the adequacy of the valuation allowance is a process that takes into consideration a variety of factors. The Bank has developed a range of valuation allowances necessary to adequately provide for probable incurred losses inherent in each pool of loans. We consider our own charge-off history along with the growth in the portfolio as well as the Bank's credit administration and asset management philosophies and procedures when determining the allowances for each pool. In addition, we evaluate and consider the impact that existing and projected economic and market conditions may have on the portfolio as well as known and inherent risks in the portfolio. Finally, we evaluate and consider the allowance ratios and coverage percentages of both peer group and regulatory agency data. These evaluations are inherently subjective because, even though they are based on objective data, it is management's interpretation of that data that determines the amount of the appropriate allowance. If the evaluations prove to be incorrect, the allowance for loan losses may not be sufficient to cover losses inherent in the loan portfolio, resulting in additions to the allowance for loan losses.

The Classification Committee is comprised of both members of management and the Board of Directors. The adequacy of the reserves is analyzed quarterly, with any adjustment to a level deemed appropriate by the Classification Committee, based on its risk assessment of the entire portfolio. Based on the Classification Committee's review of the classified loans and the overall reserve levels as they relate to the entire loan portfolio at December 31, 2006, management believes the allowance for loan losses has been established at levels sufficient to cover the probable incurred losses in the Bank's loan portfolio. Future additions or reductions to the allowance may be necessary based on changes in economic, market or other conditions. Changes in estimates could result in a material change in the allowance. In addition, various regulatory agencies, as an integral part of the examination process, periodically review the Bank's allowance for loan losses. Such agencies may require the Bank to recognize adjustments to the allowance based on their judgments of the information available to them at the time of their examination.

For additional information regarding our allowance for loan losses, see Note 3 to the Consolidated Financial Statements.

*NET INCOME*

Net income for 2006 totaled \$8,168,000 or \$1.33 per diluted share while net income for 2005 totaled \$9,623,000 or \$1.53 per diluted share, as compared to net income of \$10,377,000, or \$1.64 per diluted share for the year ended December 31, 2004. Net income decreased \$1,455,000 or 15.1% as compared to 2005 and net income for 2005 decreased \$754,000 or 7.3% over 2004. Significant trends for 2006 include: (i) a \$701,000 or 2.9% decrease in net interest income; (ii) a \$692,000 or 13.6% decrease in total other income and (iii) a \$1,355,000 or 9.3% increase in total other expenses. The provision for income taxes decreased \$1,078,000 or 21.9%.



*NET INTEREST INCOME*

Net interest income, the primary contributor to earnings, represents the difference between income on interest earning assets and expenses on interest bearing liabilities. Net interest income depends upon the volume of interest earning assets and interest bearing liabilities and the interest rates earned or paid on them.

The following table sets forth certain information relating to the Company's average consolidated statements of financial condition and its consolidated statements of income for the years indicated and reflect the average yield on assets and average cost of liabilities for the years indicated. Such yields and costs are derived by dividing income or expense by the average balance of assets or liabilities, respectively, for the years shown. Average balances are derived from daily average balances and include non-performing accrual loans. The yields and costs include fees, which are considered adjustments to yields. Interest on nonaccrual loans has been included only to the extent reflected in the consolidated statements of income. For purposes of this table, the average balances for investments in debt and equity securities exclude unrealized appreciation/depreciation due to the application of SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities."

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| Year Ended<br>December 31,<br>(Dollars in<br>thousands) | 2006               |                               |                           | 2005               |                               |                           | 2004               |                               |                           |
|---|--------------------|-------------------------------|---------------------------|--------------------|-------------------------------|---------------------------|--------------------|-------------------------------|---------------------------|
|   | Average<br>Balance | Average<br>Yield/<br>Interest | Average<br>Yield/<br>Cost | Average<br>Balance | Average<br>Yield/<br>Interest | Average<br>Yield/<br>Cost | Average<br>Balance | Average<br>Yield/<br>Interest | Average<br>Yield/<br>Cost |
| Interest earning assets:                                |                    |                               |                           |                    |                               |                           |                    |                               |                           |
| Loans, net<br>(including loan fee<br>income)            | \$ 307,394         | \$ 23,345                     | 7.6%                      | \$ 299,950         | \$ 20,724                     | 6.9%                      | \$ 285,058         | \$ 18,850                     | 6.6%                      |
| Mortgage-backed<br>securities                           | 112,463            | 4,989                         | 4.4                       | 102,460            | 4,160                         | 4.0                       | 107,146            | 4,137                         | 3.8                       |
| Tax exempt<br>securities <sup>(1)</sup>                 | 57,948             | 3,060                         | 5.2                       | 60,005             | 2,944                         | 4.8                       | 53,552             | 2,514                         | 4.6                       |
| Taxable securities                                      | 26,258             | 970                           | 3.6                       | 41,485             | 1,520                         | 3.6                       | 57,170             | 2,187                         | 3.8                       |
| Federal funds sold                                      | 10,800             | 560                           | 5.1                       | 7,971              | 265                           | 3.3                       | 7,776              | 98                            | 1.2                       |
| Securities, restricted                                  | 907                | 65                            | 7.2                       | 2,034              | 95                            | 4.7                       | 1,895              | 34                            | 1.8                       |
| Deposits with banks                                     | 348                | 21                            | 6.0                       | 93                 | 2                             | 2.2                       | 176                | 2                             | 1.1                       |
| Total interest<br>earning assets                        | 516,118            | 33,010                        | 6.4                       | 513,998            | 29,710                        | 5.8                       | 512,773            | 27,822                        | 5.4                       |
| Non interest earning assets:                            |                    |                               |                           |                    |                               |                           |                    |                               |                           |
| Cash and due from<br>banks                              | 14,307             |                               |                           | 15,871             |                               |                           | 16,591             |                               |                           |
| Other assets  | 18,963             |                               |                           | 18,186             |                               |                           | 18,671             |                               |                           |
| Total assets  | \$ 549,388         |                               |                           | \$ 548,055         |                               |                           | \$ 548,035         |                               |                           |
| Interest bearing liabilities:                           |                    |                               |                           |                    |                               |                           |                    |                               |                           |
| Savings, N.O.W.<br>and<br>money market<br>deposits      |                    |                               |                           |                    |                               |                           |                    |                               |                           |
|   | \$ 259,747         | \$ 6,322                      | 2.4%                      | \$ 249,382         | \$ 3,022                      | 1.2%                      | \$ 258,100         | \$ 1,331                      | 0.5%                      |
| Certificates of<br>deposit of \$100,000<br>or more      |                    |                               |                           |                    |                               |                           |                    |                               |                           |
|   | 24,293             | 888                           | 3.7                       | 28,777             | 550                           | 1.9                       | 36,249             | 475                           | 1.3                       |
| Other time<br>deposits                                  |                    |                               |                           |                    |                               |                           |                    |                               |                           |
|   | 25,420             | 723                           | 2.8                       | 27,805             | 470                           | 1.7                       | 31,907             | 457                           | 1.4                       |
| Other borrowed<br>money                                 |                    |                               |                           |                    |                               |                           |                    |                               |                           |
|   | 4,205              | 216                           | 5.1                       | 6,688              | 205                           | 3.1                       | 3,131              | 55                            | 1.8                       |
| Federal funds<br>purchased                              |                    |                               |                           |                    |                               |                           |                    |                               |                           |
|   | 3,666              | 188                           | 5.1                       | 1,999              | 72                            | 3.6                       | 2,136              | 33                            | 1.5                       |
| Total interest<br>bearing liabilities                   | 317,331            | 8,337                         | 2.6                       | 314,651            | 4,319                         | 1.4                       | 331,523            | 2,351                         | 0.7                       |
| Non interest bearing<br>liabilities:                    |                    |                               |                           |                    |                               |                           |                    |                               |                           |

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|  |                   |             |            |      |            |      |
|--|-------------------|-------------|------------|------|------------|------|
| Demand deposits  | <b>183,157</b>    |             | 183,260    |      | 167,765    |      |
| Other liabilities  | <b>2,699</b>      |             | 2,386      |      | 3,277      |      |
| Total liabilities  | <b>503,187</b>    |             | 500,297    |      | 502,565    |      |
| Stockholders' equity   | <b>46,201</b>     |             | 47,758     |      | 45,470     |      |
| Total liabilities and stockholders' equity                       | <b>\$ 549,388</b> |             | \$ 548,055 |      | \$ 548,035 |      |
| Net interest income/interest rate spread <sup>(2)</sup>          | <b>24,673</b>     | <b>3.8%</b> | 25,391     | 4.4% | 25,471     | 4.7% |
| Net interest earning assets/net interest margin <sup>(3)</sup>   | <b>\$ 198,787</b> | <b>4.8%</b> | \$ 199,347 | 4.9% | \$ 181,250 | 5.0% |
| Ratio of interest earning assets to interest bearing liabilities | <b>162.6%</b>     |             | 163.4%     |      | 154.7%     |      |
| Less: Tax equivalent adjustment                                  | <b>(980)</b>      |             | (997)      |      | (899)      |      |
| Net interest income  | <b>\$ 23,693</b>  |             | \$ 24,394  |      | \$ 24,572  |      |

(1) The above table is presented on a tax equivalent basis.

(2) Net interest rate spread represents the difference between the yield on interest earning assets and the cost of interest bearing liabilities.

(3) Net interest margin represents net interest income divided by average interest earning assets.

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RATE/VOLUME

Net interest income can be analyzed in terms of the impact of changes in rates and volumes. The following table illustrates the extent to which changes in interest rates and in the volume of average interest earning assets and interest bearing liabilities have affected the Bank's interest income and interest expense during the periods indicated. Information is provided in each category with respect to (i) changes attributable to changes in volume (changes in volume multiplied by prior rate); (ii) changes attributable to changes in rates (changes in rates multiplied by prior volume); and (iii) the net changes. For purposes of this table, changes that are not due solely to volume or rate changes have been allocated to these categories based on the respective percentage changes in average volume and rate. Due to the numerous simultaneous volume and rate changes during the periods analyzed, it is not possible to precisely allocate changes between volume and rates. In addition, average earning assets include nonaccrual loans.

| Year Ended December<br>31,<br>(In thousands)            | 2006 Over 2005<br>Changes Due To |            |               | 2005 Over 2004<br>Changes Due To |          |               |
|---|----------------------------------|------------|---------------|----------------------------------|----------|---------------|
|   | Volume                           | Rate       | Net<br>Change | Volume                           | Rate     | Net<br>Change |
| Interest income on<br>interest earning assets:          |                                  |            |               |                                  |          |               |
| Loans (including loan<br>fee income)                    | \$ 525                           | \$ 2,096   | \$ 2,621      | \$ 1,004                         | \$ 870   | \$ 1,874      |
| Mortgage-backed<br>securities                           | 426                              | 403        | 829           | (186)                            | 209      | 23            |
| Tax exempt securities<br>(1)                            | (101)                            | 217        | 116           | 309                              | 121      | 430           |
| Taxable securities                                      | (562)                            | 12         | (550)         | (584)                            | (83)     | (667)         |
| Federal funds sold                                      | 114                              | 181        | 295           | 3                                | 164      | 167           |
| Securities, restricted                                  | (67)                             | 37         | (30)          | 3                                | 58       | 61            |
| Deposits with banks                                     | 15                               | 4          | 19            | (2)                              | 2        | -             |
| Total interest<br>earning assets                        | 350                              | 2,950      | 3,300         | 547                              | 1,341    | 1,888         |
| Interest expense on<br>interest bearing<br>liabilities: |                                  |            |               |                                  |          |               |
| Savings, N.O.W. and<br>money market deposits            | 131                              | 3,169      | 3,300         | (47)                             | 1,738    | 1,691         |
| Certificates of deposit<br>of \$100,000 or more         | (97)                             | 435        | 338           | (112)                            | 187      | 75            |
| Other time deposits                                     | (43)                             | 296        | 253           | (63)                             | 76       | 13            |
| Other borrowed money                                    | (94)                             | 105        | 11            | 91                               | 59       | 150           |
| Federal funds<br>purchased                              | 77                               | 39         | 116           | (2)                              | 41       | 39            |
| Total interest bearing<br>liabilities                   | (26)                             | 4,044      | 4,018         | (133)                            | 2,101    | 1,968         |
| Net interest income                                     | \$ 376                           | \$ (1,094) | \$ (718)      | \$ 680                           | \$ (760) | \$ (80)       |

(1) The above table is presented on a tax equivalent basis.

The net interest margin compression continued in 2006. Net interest income was \$23,693,000 in 2006 compared to \$24,394,000 in 2005 and \$24,572,000 in 2004. The decrease of 2.9% as compared to 2005 primarily resulted from the effect of the increase in rate for the average total interest bearing liabilities being greater than the effect of the increase in the rate of average total interest earning assets. Yields on interest bearing liabilities increased 126 basis points during 2006 compared to the prior year, which were partly offset by increased yields of 61 basis points on interest earning assets. To protect core balances that were leaving the Bank for higher yields elsewhere, deposit promotions during the year were partially the cause for the increased cost of interest bearing liabilities at 2.6% for 2006 as opposed to a cost of 1.4% during 2005. Part of the increase in the cost of certificates of deposit greater than \$100,000 is driven by the purchase of \$2,000,000 in brokered certificates of deposit. These certificates of deposit, as well as the certificates of deposit generated through the Bank's promotions, provide funding as the Bank encounters seasonal outflows. Because the Company's interest bearing liabilities generally reprice or mature more quickly than its interest earning assets, an increase in short term interest rates would initially result in a decrease in net interest income. Additionally, the large percentages of deposits in money market accounts reprice at short term market rates making the balance sheet more liability sensitive.

Average interest earning assets grew by \$2,120,000 in 2006, an increase of 0.4% compared to 2005. The 0.7% decrease in net interest income of 2005 over 2004 reflects the stabilization of the net interest margin despite the continued flat yield curve. Average interest earning assets grew slightly to \$513,998,000 in 2005 from \$512,773,000 in 2004, representing a 0.2% increase. Average interest bearing liabilities totaled \$314,651,000 in 2005 and \$331,523,000 in 2004. The percentage decrease year over year was 5.1%. The tax adjusted net interest margin was 4.8% in 2006, 4.9% in 2005, and 5.0% in 2004.

Total interest income increased to \$32,030,000 in 2006 from \$28,713,000 in 2005 and from \$26,923,000 in 2004, an increase of 11.6% between 2006 and 2005 and 6.6% increase to 2005 from 2004. The average yield on total interest earning assets for 2006 increased to 6.4% from 5.8 % in 2005 and the average yield for 2005 increased to 5.8% from 5.4% for 2004. The ratio of interest earning assets to interest bearing liabilities decreased to 162.6% in 2006 as compared to 163.4% in 2005 but increased from 154.7% in 2004. Interest income on loans increased \$2,621,000 in 2006 over 2005 and \$1,874,000 in 2005 over 2004 while average loans increased 2.5% to

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\$307,394,000 in 2006 versus 2005 and 5.2% to \$299,950,000 in 2005 from 2004. The yield on average loans for 2006 increased to 7.6% from 6.9% in 2005 and the average yield for 2005 increased to 6.9% from 6.6% for 2004.

Interest income on investment in debt and equity securities increased \$382,000 or 4.9% in 2006 from 2005 and in 2005 decreased \$251,000 or 3.2% from 2004. Amortization of premiums on securities decreased over the three year period from totals of \$1,261,000 to \$786,000 to \$272,000 in years 2004, 2005, and 2006 respectively as the rate environment changed and prepayments substantially slowed on the mortgage backed security portfolio. Average total securities decreased 4.1% to \$197,576,000 in 2006 from 2005 and decreased 6.3% to \$205,984,000 in 2005 from 2004. The tax adjusted average yield on total securities increased to 4.6% in 2006 from 2005 and increased to 4.2% in 2005 from 4.0% in 2004. Average federal funds sold increased \$2,829,000 or 35.5% in 2006 from 2005 and increased \$195,000 or 2.5% in 2005 from 2004.

For the year ended December 31, 2006, average total deposits increased by \$3,393,000 or 0.7% as compared to average total deposits for the year ended December 31, 2005. For the year ended December 31, 2006, components of this change include an increase in average balances in savings, N.O.W. and money market accounts of \$10,365,000 or 4.2% as compared to average balances in savings, N.O.W. and money market accounts for the year ended December 31, 2005. The average balances in demand deposits decreased \$103,000 or 0.1% for the year ended December 31, 2006 compared to the prior year. Average balances in certificates of deposit of \$100,000 or more and other time deposits decreased \$6,870,000 or 12.1% for the year ended December 31, 2006 as compared to average balances in 2005. Average public fund deposits comprised 22.5% of total average deposits during the year ended December 31, 2006 and 15.8% of total average deposits for the year ended December 31, 2005. Average federal funds purchased totaled with average other borrowed money decreased \$816,000 or 9.4% over comparable average balances for the prior year.

Interest expense increased \$4,018,000 to \$8,337,000 in 2006 from 2005 and increased \$1,968,000 to \$4,319,000 in 2005 from \$2,351,000 in 2004. The increase of 93.0% in 2006 and 83.7% in 2005 in interest expense were caused by the upward trend in the cost of average interest bearing liabilities. The cost of average interest bearing liabilities was 2.6% in 2006, 1.4% in 2005 and 0.7% during 2004. Average federal funds purchased and overnight borrowings totaled \$7,871,000 and \$8,687,000 in 2006 and 2005, respectively. While average federal funds purchased increased, the average balance for overnight borrowings decreased.

**Provision for Loan Losses**

The performance of the loan portfolio continued to be strong for the years ended December 31, 2006 and 2005. Nonaccrual loans decreased \$235,000 to \$423,000 in 2006 from 2005. In 2005, nonaccrual loans decreased \$1,037,000 to \$658,000 from 2004. This represents 0.1% and 0.2% of net loans at December 31, 2006 and 2005, respectively. The Company had no foreclosed real estate at December 31, 2006 and 2005.

Net recoveries were \$44,000 for the year ended December 31, 2006 and net charge-offs were \$105,000 and \$256,000 for the years ended December 31, 2005 and 2004, respectively. The ratio of allowance for loan losses to nonaccrual loans was 593.9%, 362.2%, and 129.1% at December 31, 2006, 2005, and 2004, respectively.

Loans of approximately \$4,156,000, \$5,085,000 and \$7,679,000 at December 31, 2006, 2005, and 2004, respectively were classified as potential problem loans. This represents 1.3%, 1.7%, and 2.6% of total loans at December 31, 2006, 2005, and 2004, respectively. These are loans for which management has information that indicates the borrower may not be able to comply with the present repayment terms. These loans are subject to increased management attention and their classification is reviewed on at least a quarterly basis. Due to the structure and nature of the credits, management currently believes that the likelihood of sustaining a material loss on these relationships is remote. As of December 31, 2006 there was one loan considered to be a troubled debt restructuring, as defined by SFAS No. 114, totaling \$118,000. After review of the estimated fair value of the underlying collateral less the costs to sell, management believes it will be able to collect all amounts due without a shortfall according to the modified terms of

the loan agreements. There were no restructured loans as of December 31, 2005.

Based on our continuing review of the overall loan portfolio, the current asset quality of the portfolio, and the net recoveries or charge-offs, a provision for loan losses of \$85,000 was recorded in 2006 and \$300,000 was recorded in 2005 and in 2004. The allowance for loan losses increased to \$2,512,000 at December 31, 2006, and \$2,383,000 at December 31, 2005, as compared to \$2,188,000 at December 31, 2004. As a percentage of total loans, the allowance was 0.77% and 0.79% at December 31, 2006 and 2005, respectively.

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The following table sets forth changes in the allowance for loan losses.

| December 31,<br>(Dollars in thousands)   | 2006            | 2005            | 2004            | 2003            | 2002            |
|--|-----------------|-----------------|-----------------|-----------------|-----------------|
| Allowance for loan losses<br>balance at beginning of<br>period                         | \$ 2,383        | \$ 2,188        | \$ 2,144        | \$ 2,294        | \$ 2,249        |
| <b>Charge-offs:</b>  |                 |                 |                 |                 |                 |
| Real estate mortgage loans   | -               | 7               | 3               | 38              | 4               |
| Real estate construction<br>loans  | -               | -               | -               | -               | -               |
| Commercial, financial and<br>agricultural loans  | 33              | 153             | 302             | 163             | 212             |
| Installment/consumer loans   | 50              | 129             | 65              | 148             | 22              |
| <b>Total</b>   | <b>83</b>       | <b>289</b>      | <b>370</b>      | <b>349</b>      | <b>238</b>      |
| <b>Recoveries:</b>   |                 |                 |                 |                 |                 |
| Real estate mortgage loans   | 6               | 17              | 23              | 13              | 8               |
| Real estate construction<br>loans  | -               | 100             | -               | -               | -               |
| Commercial, financial and<br>agricultural loans  | 59              | 37              | 61              | 90              | 44              |
| Installment/consumer loans   | 62              | 30              | 30              | 96              | 31              |
| <b>Total</b>   | <b>127</b>      | <b>184</b>      | <b>114</b>      | <b>199</b>      | <b>83</b>       |
| <b>Net recoveries (charge-offs)</b>  | <b>44</b>       | <b>(105)</b>    | <b>(256)</b>    | <b>(150)</b>    | <b>(155)</b>    |
| Provision for loan losses<br>charged to operations                                     | 85              | 300             | 300             | -               | 220             |
| Balance before reclass to<br>other liabilities   | 2,512           | 2,383           | 2,188           | 2,144           | 2,314           |
| Net change in other<br>liabilities portion allocated to<br>off balance sheet items     | -               | -               | -               | -               | (20)            |
| <b>Balance at end of period</b>  | <b>\$ 2,512</b> | <b>\$ 2,383</b> | <b>\$ 2,188</b> | <b>\$ 2,144</b> | <b>\$ 2,294</b> |
| Ratio of net recoveries<br>(charge-offs) during period<br>to average loans outstanding | <b>0.01%</b>    | <b>(0.04%)</b>  | <b>(0.09%)</b>  | <b>(0.06%)</b>  | <b>(0.07%)</b>  |

Allocation of Allowance for Loan Losses

The following table sets forth the allocation of the total allowance for loan losses by loan type.

| Year Ended<br>December 31,<br>(Dollars in<br>thousands) | 2006                               | 2005                               | 2004                               | 2003                               | 2002                               |
|---|------------------------------------|------------------------------------|------------------------------------|------------------------------------|------------------------------------|
| <b>Percentage<br/>of<br/>Loans</b>                      | <b>Percentage<br/>of<br/>Loans</b> | <b>Percentage<br/>of<br/>Loans</b> | <b>Percentage<br/>of<br/>Loans</b> | <b>Percentage<br/>of<br/>Loans</b> | <b>Percentage<br/>of<br/>Loans</b> |



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|  | <b>to</b>       |               | <b>to</b>       |               | <b>to</b>       |               | <b>To</b>       |               | <b>to</b>       |               |
|--|-----------------|---------------|-----------------|---------------|-----------------|---------------|-----------------|---------------|-----------------|---------------|
|  | <b>Total</b>    |               | <b>Total</b>    |               | <b>Total</b>    |               | <b>Total</b>    |               | <b>Total</b>    |               |
|  | <b>Amount</b>   | <b>Loans</b>  | Amount          | Loans         | Amount          | Loans         | Amount          | Loans         | Amount          | Loans         |
| Commercial, financial and agricultural loans | \$ 303          | 12.1%         | \$ 273          | 10.5%         | \$ 315          | 11.6%         | \$ 272          | 12.4%         | \$ 591          | 15.6%         |
| Real estate construction loans               | 121             | 4.8           | 183             | 5.9           | 148             | 6.2           | 148             | 7.3           | 227             | 5.0           |
| Real estate mortgage loans                   | 2,009           | 80.0          | 1,817           | 80.4          | 1,659           | 80.0          | 1,663           | 78.1          | 1,160           | 76.2          |
| Installment/consumer loans                   | 79              | 3.1           | 110             | 3.2           | 66              | 2.2           | 61              | 2.2           | 316             | 3.2           |
| <b>Total</b>                                 | <b>\$ 2,512</b> | <b>100.0%</b> | <b>\$ 2,383</b> | <b>100.0%</b> | <b>\$ 2,188</b> | <b>100.0%</b> | <b>\$ 2,144</b> | <b>100.0%</b> | <b>\$ 2,294</b> | <b>100.0%</b> |

**Non Interest Income**

Total other income decreased by \$692,000 or 13.6% in 2006 to \$4,413,000 and decreased \$335,000 or 6.2% to \$5,105,000 in 2005 compared to \$5,440,000 in 2004. The decline in total other income during 2006 compared to 2005 was due to net losses on sales of securities during the year, a decrease of \$251,000 in title fee income from Bridge Abstract, a decline in fees from other customer services of \$62,000 and lower service charges on deposit accounts of \$35,000, partly offset by an increase in other operating income of \$61,000. Excluding net securities losses and gains, total other income decreased \$287,000 or 5.8% for the year ended December 31, 2006.

A net loss on securities of \$289,000 was recognized in 2006 while net gains on securities of \$116,000 and \$734,000 were recognized in 2005 and 2004, respectively. The net loss on securities in 2006 was due to repositioning of the available for sale investment portfolio.

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Bridge Abstract, the Bank's title insurance abstract subsidiary, generated title fee income of \$1,042,000, \$1,293,000, and \$866,000 in 2006, 2005, and 2004, respectively. The decrease of \$251,000 or 19.4% in 2006 was due to a slowdown in the volume of transactions processed by the subsidiary.

Fees from other customer services declined \$62,000 or 4.2% from 2005. This decline was primarily due to revenues from merchant processing decreasing \$54,000 or 7.7% from 2005. Fees from other customer services increased \$143,000 or 10.7% in 2005 compared to 2004. Service charges on deposit accounts for the year ended December 31, 2006 totaled \$2,069,000, a decrease of \$35,000 as compared to 2005. For the year ended December 31, 2005, service charges were \$2,104,000, a decrease of \$224,000 from 2004. The Company believes that the decline is attributable to the change in customer behavior to avoid paying fees for overdrafts and uncollected account balances, which partially stems from changes in our fee policies.

Other operating income for the year ended December 31, 2006 totaled \$169,000, an increase of \$61,000 or 56.5% from the prior year. Other operating income for 2005 totaled \$108,000, a decrease of \$63,000 or 36.8% over 2004.

**Non Interest Expense**

Other expenses increased by \$1,355,000 or 9.2% in 2006 to \$16,002,000 from \$14,647,000 in 2005 and other expenses in 2005 increased \$1,083,000 or 8.0% from \$13,564,000 in 2004. The primary component of this change was an increase in salaries and employee benefits of \$840,000 or 10.1% in 2006 and \$891,000 or 12.0% in 2005. Salaries and benefits increases reflect base salary increases, filling vacant positions, hiring additional staff to support the Company's expanding infrastructure and branch network, growth in business lines such as the title insurance abstract subsidiary in 2005, and an increase in employee benefit costs, particularly medical insurance expense and pension costs. During 2005 there were unfilled management positions that were subsequently filled. In addition, due to the unanticipated departure of the Chief Operating Officer in the fourth quarter of 2005, an accrual for related severance was recorded at that time.

Other operating expenses for the year ended December 31, 2006 totaled \$3,800,000, an increase of \$251,000 or 7.1% compared to 2005, and 2005 totaled \$3,549,000, an increase of \$239,000 or 7.2% over 2004. Higher other operating expenses were due to increases in information systems costs and other operational costs related to expanding the Company's infrastructure including online services and the opening and preparing for new branch offices. The increase in 2005 resulted from increased professional fees primarily from costs associated with the review of the executive compensation policies which are reviewed every three years.

Net occupancy expense increased \$180,000 or 14.6% in 2006 to \$1,414,000 from \$1,234,000 in 2005 and decreased \$49,000 or 3.8% from \$1,283,000 in 2004. Higher net occupancy expense during 2006 was due to increases in depreciation expense and rent expense related to the opening of new branch offices.

**Provision for Income Taxes**

The provision for income taxes for December 31, 2006, 2005, and 2004 was \$3,851,000, \$4,929,000, and \$5,771,000, respectively. The decrease in 2006 was due to the reduction in income before provision for income taxes and a lower effective rate. The reduction in tax rate primarily resulted from a greater percentage of interest income from tax exempt securities in 2006. The decrease in 2005 was due to income before income taxes declining to \$14,552,000 from \$16,148,000 in 2004. This reduction also is partially attributed to a reduction in the New York State tax. The effective tax rate was 32.0%, 33.9% and 35.7% for the years ended December 31, 2006, 2005, and 2004, respectively.

*FINANCIAL CONDITION*

The assets of the Company totaled \$573,644,000 at December 31, 2006, an increase of \$40,200,000 or 7.5% from the previous year-end. This increase mainly resulted from growth in total loans of \$23,733,000 or 7.9%, an increase in total securities of \$18,722,000 or 8.8% and an increase in banking premises and equipment of \$2,365,000 or 15.1%

partly offset by a decrease in total cash and cash equivalents of \$2,412,000 or 15.4% and a decline in other assets of \$2,147,000 or 39.5%.

Total stockholders' equity was \$45,539,000 at December 31, 2006, a decrease of \$1,112,000 or 2.4% from December 31, 2005 primarily due to declaration of dividends totaling \$5,634,000, the repurchases of treasury stock of \$4,039,000, and the adoption of SFAS 158 of \$648,000, partially offset by net income of \$8,168,000 and a decrease in net unrealized loss on securities of \$851,000.

In December 2006, the Company declared a quarterly dividend of \$0.23 per share. The Company continues its long term trend of uninterrupted dividends.

### **Loans**

During 2006, the Company continued to experience growth trends in real estate lending. The concentration of loans in our primary market areas may increase risk. Unlike larger banks that are more geographically diversified, the Bank's loan portfolio consists primarily of real estate loans secured by commercial and residential real estate properties located in the Bank's principal lending area

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on eastern Long Island. The markets in which the Company operates have experienced substantial growth in construction and land development activity over the past several years, which has been a factor in overall loan growth. The local economic conditions on eastern Long Island have a significant impact on the volume of loan originations and the quality of our loans, the ability of borrowers to repay these loans, and the value of collateral securing these loans. A considerable decline in the general economic conditions caused by inflation, recession, unemployment or other factors beyond the Company's control would impact these local economic conditions and could negatively affect the financial results of the Company's operations. Additionally, while the Company has a significant amount of commercial real estate loans, the majority of which are owner-occupied, decreases in tenant occupancy may also have a negative effect on the ability of borrowers to make timely repayments of their loans, which would have an adverse impact on the Company's earnings.

The interest rates charged by the Bank on loans are affected primarily by the demand for such loans, the supply of money available for lending purposes, the rates offered by its competitors, the Bank's relationship with the customer, and the related credit risks of the transaction. These factors are affected by general and economic conditions including, but not limited to, monetary policies of the federal government, including the Federal Reserve Board, legislative policies and governmental budgetary matters.

The Bank targets its business lending and marketing initiatives towards promotion of loans that primarily meet the needs of small to medium-sized businesses. These small- to medium-sized businesses generally have fewer financial resources in terms of capital or borrowing capacity than larger entities. If general economic conditions negatively impact these businesses, the results of operations and financial condition may be adversely affected.

With respect to the underwriting of loans, there are certain risks, including the risk of non-payment that is associated with each type of loan that the Bank markets. Approximately 46.7% of the Bank's loan portfolio at December 31, 2006 is comprised of commercial real estate loans. Home equity lines of credit comprise approximately 18.7%, construction mortgage loans comprise approximately 10.2%, residential mortgages comprise approximately 10.1%, and land loans comprise approximately 1.0%. Risks associated with a concentration in real estate loans include potential losses from fluctuating values of land and improved properties. Largest loan concentrations by industry are loans granted to lessors of commercial property both owner occupied and nonowner occupied. The Bank uses conservative underwriting criteria to better insulate itself from a downturn in real estate values and economic conditions on eastern Long Island that could have a significant impact on the value of collateral securing the loans as well as the ability of customers to repay loans.

The remainder of the loan portfolio is comprised of commercial and consumer loans, which comprises approximately 13.3% of the Bank's loan portfolio. The primary risks associated with commercial loans are the cash flow of the business, the experience and quality of the borrowers' management, the business climate, and the impact of economic factors. The primary risks associated with consumer loans relate to the borrower, such as the risk of a borrower's unemployment as a result of deteriorating economic conditions or the amount and nature of a borrower's other existing indebtedness, and the value of the collateral securing the loans if the Bank must take possession of the collateral. Consumer loans also have risks associated with concentrations of loans in a single type of loan.

The Company's policy for charging off loans is a multi-step process. A loan is considered a potential charge-off when it is in default of either principal or interest for a period of 90, 120 or 180 days, depending upon the loan type, as of the end of the prior month. In addition to date criteria, other triggering events may include, but are not limited to, notice of bankruptcy by the borrower or guarantor, death of the borrower, and deficiency balance from the sale of collateral. These loans identified are presented for evaluation at the regular meeting of the Classification Committee. The recovery of charged-off balances is actively pursued until the potential for recovery has been exhausted, or until the expense of collection does not justify the recovery efforts.

Total loans grew \$23,733,000 or 7.9% during 2006 and \$6,130,000 or 2.1% during 2005. Average net loans grew \$7,444,000 or 2.5% during 2006 over 2005 and \$14,892,000 or 5.2% during 2005 when compared to the prior year. Real estate mortgage loans were the largest contributor of the growth for both 2006 and 2005 and increased \$22,896,000 or 9.4% and \$6,116,000 or 2.6%, respectively. Growth in real estate loans is primarily attributed to an increase in commercial and residential mortgages and increases in the home equity loan portfolio. Within the residential mortgage portfolio the Bank offers interest only mortgages. Commercial, financial and agricultural loans increased \$4,854,000 or 15.3% in 2006 from 2005 and decreased \$2,698,000 or 7.9% in 2005 from 2004. Real estate construction loans decreased \$3,193,000 or 17.8% in 2006 and decreased \$492,000 or 2.7% in 2005. Installment/consumer loans declined \$979,000 or 10.0% during 2006 and increased \$3,142,000 or 47% during 2005. Fixed rate loans represented 16.7%, 13.8%, and 14.9% of total loans at December 31, 2006, 2005, and 2004, respectively. The rate of loan growth for 2006 improved compared to loan growth of 2.1% in 2005 but is still lower than historical growth reflecting increased competition for quality credits within our market area.

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The following table sets forth the major classifications of loans:

| December 31,<br>(In thousands)                   | 2006       | 2005       | 2004       | 2003       | 2002       |
|--|------------|------------|------------|------------|------------|
| Real estate mortgage loans                       | \$ 265,824 | \$ 242,928 | \$ 236,812 | \$ 213,256 | \$ 189,226 |
| Commercial, financial, and<br>agricultural loans | 36,498     | 31,644     | 34,342     | 33,810     | 38,692     |
| Installment/consumer loans                       | 8,848      | 9,827      | 6,685      | 6,105      | 8,011      |
| Real estate construction loans                   | 14,767     | 17,960     | 18,452     | 20,037     | 12,520     |
| Total loans                                      | 325,937    | 302,359    | 296,291    | 273,208    | 248,449    |
| Unamortized cost/(Unearned<br>income)            | 60         | (95)       | (157)      | (20)       | (61)       |
|  | 325,997    | 302,264    | 296,134    | 273,188    | 248,388    |
| Allowance for loan losses                        | (2,512)    | (2,383)    | (2,188)    | (2,144)    | (2,294)    |
| Net loans  | \$ 323,485 | \$ 299,881 | \$ 293,946 | \$ 271,044 | \$ 246,094 |

Selected Loan Maturity Information

The following table sets forth the approximate maturities and sensitivity to changes in interest rates of certain loans, exclusive of real estate mortgages and consumer loans to individuals as of December 31, 2006:

| (In thousands)                          | Within One<br>Year | After One<br>But Within<br>Five Years | After<br>Five Years | Total     |
|---|--------------------|---------------------------------------|---------------------|-----------|
| Commercial loans                        | \$ 13,015          | \$ 17,007                             | \$ 6,476            | \$ 36,498 |
| Construction loans <sup>(1)</sup>       | 35                 | 5,036                                 | 9,696               | 14,767    |
| Total                                   | \$ 13,050          | \$ 22,043                             | \$ 16,172           | \$ 51,265 |
| Rate provisions:                        |                    |                                       |                     |           |
| Amounts with fixed interest<br>rates    | \$ 487             | \$ 8,663                              | \$ 3,062            | \$ 12,212 |
| Amounts with variable interest<br>rates | 12,563             | 13,380                                | 13,110              | 39,053    |
| Total                                   | \$ 13,050          | \$ 22,043                             | \$ 16,172           | \$ 51,265 |

- (1) Included in the "After Five Years" column, are one-step construction loans that contain a preliminary construction period (interest only) that automatically convert to amortization at the end of the the construction phase.

Past Due, Nonaccrual and Restructured Loans

The following table sets forth selected information about past due, nonaccrual and restructured loans.

| December 31,<br>(In thousands)                       | 2006 | 2005 | 2004  | 2003 | 2002 |
|--|------|------|-------|------|------|
| Loans 90 days or more past due<br>and still accruing | \$ - | \$ - | \$ -  | \$ - | \$ - |
| Nonaccrual loans                                     | 305  | 658  | 1,695 | 152  | 200  |

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|                              |               |               |                 |               |            |
|------------------------------|---------------|---------------|-----------------|---------------|------------|
| Restructured loans           | <b>118</b>    | -             | -               | -             | -          |
| Other real estate owned, net | -             | -             | -               | -             | -          |
| <b>Total</b>                 | <b>\$ 423</b> | <b>\$ 658</b> | <b>\$ 1,695</b> | <b>\$ 152</b> | <b>200</b> |

|                                |             |      |      |      |      |
|--------------------------------|-------------|------|------|------|------|
| <b>Year Ended December 31,</b> | <b>2006</b> | 2005 | 2004 | 2003 | 2002 |
| (In thousands)                 |             |      |      |      |      |

Gross interest income that has not been paid or recorded during the year under original terms:

|                    |             |       |       |      |    |
|--------------------|-------------|-------|-------|------|----|
| Nonaccrual loans   | <b>\$ 9</b> | \$ 38 | \$ 16 | \$ 9 | 13 |
| Restructured loans | <b>\$ 1</b> | -     | -     | -    | -  |

Gross interest income recorded during the year:

|                    |              |       |       |      |   |
|--------------------|--------------|-------|-------|------|---|
| Nonaccrual loans   | <b>\$ 12</b> | \$ 17 | \$ 12 | \$ 6 | 4 |
| Restructured loans | <b>\$ 9</b>  | -     | -     | -    | - |

Commitments for additional funds

|   |   |   |   |   |   |
|---|---|---|---|---|---|
| - | - | - | - | - | - |
|---|---|---|---|---|---|

Table of Contents**Securities**

Total securities increased to \$212,034,000 at December 31, 2006 from \$192,813,000 at December 31, 2005. The available for sale portfolio increased 10.8% to \$202,590,000 and the securities held to maturity declined 5.7% to \$9,444,000. Securities held as available for sale may be sold in response to, or in anticipation of, changes in interest rates and resulting prepayment risk, or other factors. U.S. Treasury and government agency securities decreased to \$33,777,000 at December 31, 2006 from \$37,662,000 at December 31, 2005 and state and municipal obligations declined by \$2,377,000, while mortgage-backed securities increased by \$26,051,000. Fixed rate securities represent 92.1% of total securities at December 31, 2006. The Bank continued to maintain its levels of mortgage-backed securities, which represented approximately 59.2% of the available for sale balance at December 31, 2006 as compared to 51.4% at the prior year-end. A change in market rates was the primary reason for the net increase in unrealized depreciation in securities available for sale, which increased other comprehensive income.

A summary of the amortized cost, gross unrealized gains, gross unrealized losses and estimated fair value of securities is as follows:

| December 31,<br>(In thousands)                             | 2006              |                              |                               |                            |                   |                              | 2005                          |                            |                   |                              |                               |                            |
|--|-------------------|------------------------------|-------------------------------|----------------------------|-------------------|------------------------------|-------------------------------|----------------------------|-------------------|------------------------------|-------------------------------|----------------------------|
|  | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Estimated<br>Fair<br>Value | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Estimated<br>Fair<br>Value | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Estimated<br>Fair<br>Value |
| Available for sale:  |                   |                              |                               |                            |                   |                              |                               |                            |                   |                              |                               |                            |
| U.S.<br>Treasury and<br>government<br>agency<br>securities | \$ 34,123         | \$ -                         | \$ (346)                      | \$ 33,777                  | \$ 38,443         | \$ 7                         | \$ (788)                      | \$ 37,662                  | \$ 53,736         | \$ 519                       | \$ (216)                      | \$ 54,000                  |
| State and<br>municipal<br>obligations                      | 49,008            | 316                          | (481)                         | 48,843                     | 51,392            | 387                          | (559)                         | 51,220                     | 40,027            | 1,098                        | (81)                          | 41,344                     |
| Mortgage-backed<br>securities                              | 122,009           | 364                          | (2,403)                       | 119,970                    | 96,938            | 27                           | (3,046)                       | 93,919                     | 107,609           | 483                          | (1,133)                       | 106,959                    |
| Total available<br>for sale                                | 205,140           | 680                          | (3,230)                       | 202,590                    | 186,773           | 421                          | (4,393)                       | 182,801                    | 201,372           | 2,100                        | (1,430)                       | 202,303                    |
| Held to maturity:  |                   |                              |                               |                            |                   |                              |                               |                            |                   |                              |                               |                            |
| State and<br>municipal<br>obligations                      | 9,444             | -                            | (2)                           | 9,442                      | 10,012            | -                            | (23)                          | 9,989                      | 21,213            | -                            | (82)                          | 21,131                     |
| Total held to<br>maturity                                  | 9,444             | -                            | (2)                           | 9,442                      | 10,012            | -                            | (23)                          | 9,989                      | 21,213            | -                            | (82)                          | 21,131                     |
| Total debt and<br>equity securities                        | \$ 214,584        | \$ 680                       | \$ (3,232)                    | \$ 212,032                 | \$ 196,785        | \$ 421                       | \$ (4,416)                    | \$ 192,790                 | \$ 222,585        | \$ 2,100                     | \$ (1,512)                    | \$ 223,434                 |

**Deposits and Borrowings**

Overnight borrowings increased \$4,100,000 to \$18,600,000 from the prior year-end. Total deposits increased \$36,387,000 or 7.8% as compared to 2005. The growth in deposits is attributable to increased public funds deposits, the opening of the new branch in Westhampton and the offering of promotional deposit products. Demand deposits decreased \$16,798,000 or 8.8%. Savings, N.O.W. and money market deposits increased \$36,238,000 or 15.5%. Certificates of deposit of \$100,000 or more grew \$11,497,000 or 60.4% from December 31, 2005 and other time deposits increased \$5,450,000 or 21.9% as compared to the prior year.



## *LIQUIDITY*

The objective of liquidity management is to ensure the sufficiency of funds available to respond to the needs of depositors and borrowers, and to take advantage of unanticipated earnings enhancement opportunities for Company growth. Liquidity management addresses the ability of the Company to meet financial obligations that arise in the normal course of business. Liquidity is primarily needed to meet customer borrowing commitments, deposit withdrawals either on demand or contractual maturity, to repay other borrowings as they mature, to fund current and planned expenditures and to make new loans and investments as opportunities arise.

The Company's principal source of liquidity is dividends from the Bank. Due to regulatory restrictions (see Note 1(l) to the Consolidated Financial Statements), dividends from the Bank to the Company at December 31, 2006 were limited to \$7,156,000, which represents the Bank's 2006 retained net income and the net retained undivided profits from the previous two years. The dividends received from the Bank are used primarily for dividends to the shareholders and stock repurchases. In the event that the Company subsequently expands its current operations, in addition to dividends from the Bank, it will need to rely on its own earnings, additional capital raised and other borrowings to meet liquidity needs.

The Bank's most liquid assets are cash and cash equivalents, securities available for sale and securities held to maturity due within one year. The levels of these assets are dependent upon the Bank's operating, financing, lending and investing activities during any given period. Other sources of liquidity include loan and investment securities principal repayments and maturities, lines of credit with other financial institutions including the Federal Home Loan Bank, growth in core deposits and sources of wholesale funding such as brokered certificates of deposit. While scheduled loan amortization, maturing securities and short-term investments are a relatively predictable source of funds, deposit flows and loan and mortgage-backed securities prepayments are greatly influenced by general interest rates, economic conditions and competition. The Bank adjusts its liquidity levels as appropriate to meet funding needs such as seasonal deposit outflows, loans, and asset and liability management objectives. Historically, the Bank has relied on its deposit base, drawn through its full-service branches that serve its market area and local municipal deposits, as its principal source of funding. The Bank seeks to retain existing deposits and loans and maintain customer relationships by offering quality service and competitive interest rates to its customers, while managing the overall cost of funds needed to finance its strategies. However, during 2006 the Bank relied more heavily on funding from municipal accounts which are more rate sensitive and therefore volatile as individual,

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partnership and corporate account balances declined. The Bank's Asset/Liability and Funds Management Policy allows for wholesale borrowings of up to 25% of total assets. At December 31, 2006, the Bank had aggregate lines of credit of \$52,000,000 with unaffiliated correspondent banks to provide short-term credit for liquidity requirements. Of these aggregate lines of credit, \$32,000,000 is available on an unsecured basis. The Bank also has the ability, as a member of the Federal Home Loan Bank ("FHLB") system, to borrow against unencumbered residential mortgages owned by the Bank. The Bank also has a master repurchase agreement with the FHLB, which increases its borrowing capacity. As of December 31, 2006, the amount of overnight borrowings under these lines was \$18,600,000. In addition, the Bank has an approved broker relationship for the purpose of issuing brokered certificates of deposit. As of December 31, 2006 the Bank had issued \$2,000,000 of brokered certificates of deposit.

Management continually monitors the liquidity position and believes that sufficient liquidity exists to meet all of our operating requirements. Based on the objectives determined by the Asset and Liability Committee, the Bank's liquidity levels may be affected by the use of short-term and wholesale borrowings, and the amount of public funds in the deposit mix. The Asset and Liability Committee is comprised of members of senior management and the Board. Excess short-term liquidity is invested in overnight federal funds sold.

**CONTRACTUAL OBLIGATIONS**

In the ordinary course of operations, the Company enters into certain contractual obligations. The following table summarizes the Company's significant and determinable obligations by payment date at December 31, 2006.

The following represents contractual obligations outstanding at December 31, 2006:

|   | Total<br>Amounts<br>Committed | Less than<br>One Year | One to<br>Three Years | Four to Five<br>Years | Over Five<br>Years |
|---|-------------------------------|-----------------------|-----------------------|-----------------------|--------------------|
| (In thousands)                                  |                               |                       |                       |                       |                    |
| Operating leases                                | \$ 3,980                      | \$ 693                | \$ 1,246              | \$ 742                | \$ 1,299           |
| Purchase obligation                             | 250                           | 250                   | -                     | -                     | -                  |
| Time deposits                                   | 60,818                        | 56,137                | 4,013                 | 668                   | -                  |
| Total contractual<br>obligations<br>outstanding | \$ 65,048                     | \$ 57,080             | \$ 5,259              | \$ 1,410              | \$ 1,299           |

**COMMITMENTS, CONTINGENT LIABILITIES, and OFF-BALANCE SHEET ARRANGEMENTS**

Some financial instruments, such as loan commitments, credit lines, letters of credit, and overdraft protection, are issued to meet customer financing needs. These are agreements to provide credit or to support the credit of others, as long as conditions established in the contract are met, and usually have expiration dates. Commitments may expire without being used. Off-balance-sheet risk to credit loss exists up to the face amount of these instruments, although material losses are not anticipated. The same credit policies are used to make such commitments as are used for loans, often including obtaining collateral at exercise of the commitment. At December 31, 2006 the Company had \$16,718,000 in outstanding loan commitments and \$98,960,000 in outstanding commitments for various lines of credit including unused overdraft lines. The Company also has \$2,736,000 of standby letters of credit as of December 31, 2006. See Note 9 of the Notes to the Consolidated Financial Statements for additional information on loan commitments and standby letters of credit.

**CAPITAL RESOURCES**

Stockholders' equity decreased to \$45,539,000 at December 31, 2006 from \$46,651,000 at December 31, 2005 as a result of undistributed net income; plus the change in net unrealized appreciation in securities available for sale, net of tax; less the transition to adopt SFAS 158; and less the repurchase of treasury shares net of the issuance of shares of common stock pursuant to the equity incentive plan. SFAS 158 is a statement the FASB issued in September 2006. The statement is described in the notes to the consolidated financial statements on page 32. The ratio of average stockholders' equity to average total assets increased to 8.41% at year end 2006 from 8.71% at year end 2005.

The Company's capital strength is paralleled by the solid capital position of the Bank, as reflected in the excess of its regulatory capital ratios over the minimum risk-based capital adequacy ratio levels required for classification as a "well capitalized" institution by the FDIC (see Note 11 to the Consolidated Financial Statements). Management believes that the current capital levels along with future retained earnings will allow the Bank to maintain a position exceeding required capital levels and which is sufficient to support Company growth. Additionally, the Company has the ability to issue additional common stock and/or trust preferred securities should the need arise. The Company had returns on average equity of 17.68%, 20.15%, and 22.82% and returns on average assets of 1.49%, 1.76%, and 1.89% for the years ended December 31, 2006, 2005, and 2004, respectively.

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The Company utilizes cash dividends and stock repurchases to manage capital levels. Cash paid for dividends totaled \$5,668,000 in 2006 as compared to dividends paid in 2005 of \$5,561,000. The dividend payout ratio for 2006 was 68.98%. The Company continues its trend of uninterrupted dividends.

On March 27, 2006, the Company approved its stock repurchase plan allowing the repurchase of up to 5% of its current outstanding shares, 309,000 shares. There is no expiration date for the share repurchase plan. The Company considers opportunities for stock repurchases carefully. During 2006, 157,334 shares were repurchased at a total cost of approximately \$4,039,000 or an average price per share of \$25.67.

On June 21, 2004, the Company declared a three-for-two stock split. The stock split was payable in the form of a stock dividend to shareholders of record as of July 9, 2004. The stock split increased outstanding common shares from 4,257,597 to 6,386,306.

*IMPACT OF INFLATION AND CHANGING PRICES*

The Consolidated Financial Statements and notes thereto presented herein have been prepared in accordance with U.S. generally accepted accounting principles, which require the measurement of financial position and operating results in terms of historical dollars without considering changes in the relative purchasing power of money over time due to inflation. The primary effect of inflation on the operations of the Company is reflected in increased operating costs. Unlike most industrial companies, virtually all of the assets and liabilities of a financial institution are monetary in nature. As a result, changes in interest rates have a more significant effect on the performance of a financial institution than do the effects of changes in the general rate of inflation and changes in prices. Changes in interest rates could adversely affect our results of operations and financial condition. Interest rates do not necessarily move in the same direction, or in the same magnitude, as the prices of goods and services. Interest rates are highly sensitive to many factors, which are beyond the control of the Company, including the influence of domestic and foreign economic conditions and the monetary and fiscal policies of the United States government and federal agencies, particularly the Federal Reserve Bank.

*IMPACT OF PROSPECTIVE ACCOUNTING STANDARDS*

For discussion regarding the impact of new accounting standards, refer to Note 1(r) of Notes to Consolidated Financial Statements.

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Table of Contents**Item 7A. Quantitative and Qualitative Disclosures About Market Risk**

Management considers interest rate risk to be the most significant market risk for the Company. Market risk is the risk of loss from adverse changes in market prices and rates. Interest rate risk is the exposure to adverse changes in the net income of the Company as a result of changes in interest rates.

The Company's primary earnings source is net interest income, which is affected by changes in the level of interest rates, the relationship between rates, the impact of interest rate fluctuations on asset prepayments, the level and composition of deposits and liabilities, and the credit quality of earning assets. The Company's objectives in its asset and liability management are to maintain a strong, stable net interest margin, to utilize its capital effectively without taking undue risks, to maintain adequate liquidity, and to reduce vulnerability of its operations to changes in interest rates.

The Company's Asset and Liability Committee evaluates periodically, but at least four times a year, the impact of changes in market interest rates on assets and liabilities, net interest margin, capital and liquidity. Risk assessments are governed by policies and limits established by senior management, which are reviewed and approved by the full Board of Directors at least annually. The economic environment continually presents uncertainties as to future interest rate trends. The Asset and Liability Committee regularly utilizes a model that projects net interest income based on increasing or decreasing interest rates, in order to be better able to respond to changes in interest rates.

At December 31, 2006, \$196,172,000 or 92.1% of the Company's securities had fixed interest rates. Changes in interest rates affect the value of the Company's interest earning assets and in particular its securities portfolio. Generally, the value of securities fluctuates inversely with changes in interest rates. Decreases in the fair value of securities available for sale, therefore, could have an adverse effect on stockholder's equity. Increases in interest rates could result in decreases in the market value of interest earning assets, which could adversely affect the Company's results of operations if sold. The Company is also subject to reinvestment risk associated with changes in interest rates. Increases in market interest rates also could affect the type (fixed-rate or adjustable-rate) and amount of loans originated by the Company and the average life of loans and securities, which can impact the yields earned on the Company's loans and securities. Changes in interest rates may affect the average life of loans and mortgage related securities. In periods of decreasing interest rates, the average life of loans and securities held by the Company may be shortened to the extent increased prepayment activity occurs during such periods which, in turn, may result in the investment of funds from such prepayments in lower yielding assets. Under these circumstances the Company is subject to reinvestment risk to the extent that it is unable to reinvest the cash received from such prepayments at rates that are comparable to the rates on existing loans and securities. Additionally, increases in interest rates may result in decreasing loan prepayments with respect to fixed rate loans, and therefore an increase in the average life of such loans, may result in a decrease in loan demand, and make it more difficult for borrowers to repay adjustable rate loans.

The Company utilizes the results of a detailed and dynamic simulation model to quantify the estimated exposure to net interest income to sustained interest rate changes. Management routinely monitors simulated net interest income sensitivity over a rolling two-year horizon. The simulation model captures the impact of changing interest rates on the interest income received and the interest expense paid on all assets and liabilities reflected on the Company's Statement of Condition. This sensitivity analysis is compared to the asset and liability policy limits that specify a maximum tolerance level for net interest income exposure over a one-year horizon given both a 200 basis point upward and downward shift in interest rates. A parallel and pro rata shift in rates over a twelve-month period is assumed. The following reflects the Company's net interest income sensitivity analysis at December 31, 2006:

|                    | 2006             |
|--------------------|------------------|
| Change in Interest | Potential Change |

| Rates in Basis<br>Points<br>(RATE<br>SHOCK)<br>(Dollars in<br>thousands) |            | in Net<br>Interest Income | %       |
|--|------------|---------------------------|---------|
|  | \$ Change  |                           | Change  |
| 200  | \$ (1,501) |                           | (5.87)% |
| Static   | -          |                           | -       |
| (200)  | \$ (27)    |                           | (0.11)% |

The preceding sensitivity analysis does not represent a Company forecast and should not be relied upon as being indicative of expected operating results. These hypothetical estimates are based upon numerous assumptions including, but not limited to, the nature and timing of interest rate levels and yield curve shapes, prepayments on loans and securities, deposit decay rates, pricing decisions on loans and deposits, and reinvestment and replacement of asset and liability cash flows. While assumptions are developed based upon perceived current economic and local market conditions, the Company cannot make any assurances as to the predictive nature of these assumptions including how customer preferences or competitor influences may change.

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Also, as market conditions vary from those assumed in the sensitivity analysis, actual results will also differ due to prepayment and refinancing levels likely deviating from those assumed, the varying impact of interest rate change caps or floors on adjustable rate assets, the potential effect of changing debt service levels on customers with adjustable rate loans, depositor early withdrawals, prepayment penalties and product preference changes and other internal and external variables. Furthermore, the sensitivity analysis does not reflect actions that management might take in responding to, or anticipating changes in interest rates and market conditions.

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Table of Contents**Item 8. Financial Statements and Supplementary Data****CONSOLIDATED STATEMENTS OF CONDITION**

(In thousands, except share and per share amounts)

|  | December 31,<br>2006 | December 31,<br>2005 |
|--|----------------------|----------------------|
| <b>ASSETS</b>  |                      |                      |
| Cash and due from banks  | \$ 13,231            | \$ 15,649            |
| Interest earning deposits with banks   | 32                   | 26                   |
| Total cash and cash equivalents  | 13,263               | 15,675               |
| Securities available for sale, at fair value   | 202,590              | 182,801              |
| Securities held to maturity (fair value of \$9,442 and \$9,989, respectively)                        | 9,444                | 10,012               |
| Total securities, net  | 212,034              | 192,813              |
| Securities, restricted   | 878                  | 1,377                |
| Loans  | 325,997              | 302,264              |
| Less:  |                      |                      |
| Allowance for loan losses  | (2,512)              | (2,383)              |
| Loans, net   | 323,485              | 299,881              |
| Banking premises and equipment, net  | 18,005               | 15,640               |
| Accrued interest receivable  | 2,692                | 2,624                |
| Other assets   | 3,287                | 5,434                |
| <b>Total Assets</b>  | <b>\$ 573,644</b>    | <b>\$ 533,444</b>    |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>  |                      |                      |
| Demand deposits  | \$ 173,628           | \$ 190,426           |
| Savings, N.O.W. and money market deposits  | 269,966              | 233,728              |
| Certificates of deposit of \$100,000 or more   | 30,518               | 19,021               |
| Other time deposits  | 30,300               | 24,850               |
| Total deposits   | 504,412              | 468,025              |
| Overnight borrowings   | 18,600               | 14,500               |
| Accrued interest payable   | 855                  | 328                  |
| Other liabilities and accrued expenses   | 4,238                | 3,940                |
| <b>Total Liabilities</b>   | <b>528,105</b>       | <b>486,793</b>       |
| <b>Stockholders' equity:</b>   |                      |                      |
| Common stock, par value \$0.01 per share:  |                      |                      |
| Authorized: 20,000,000 shares; 6,386,306 issued; 6,078,565 and 6,206,539 shares,                     |                      |                      |
| outstanding at December 31, 2006 and 2005, respectively  | 64                   | 64                   |
| Surplus  | 21,565               | 21,631               |
| Undivided profits  | 34,347               | 31,813               |
| Less: Treasury stock at cost, 307,741 and 179,767 shares at December 31, 2006 and 2005, respectively | (8,176)              | (4,285)              |
| Unearned stock awards  | -                    | (108)                |



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|  |                   |                   |
|--|-------------------|-------------------|
|  | <b>47,800</b>     | 49,115            |
| Accumulated other comprehensive loss:  |                   |                   |
| Net unrealized loss on securities, net of taxes of \$1,025 and \$1,596 at December 31, 2006 and 2005, respectively | <b>(1,525)</b>    | (2,376)           |
| Net minimum pension liability, net of taxes of \$59 at December 31, 2005   | -                 | (88)              |
| Transition due to the adoption of SFAS 158, net of taxes of \$490  | <b>(736)</b>      | -                 |
| <b>Total Stockholders' Equity</b>  | <b>45,539</b>     | 46,651            |
| <b>Total Liabilities and Stockholders' Equity</b>  | <b>\$ 573,644</b> | <b>\$ 533,444</b> |

*See accompanying notes to Consolidated Financial Statements.*

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Table of Contents**CONSOLIDATED STATEMENTS OF INCOME**

(In thousands, except per share amounts)

| Year Ended December 31,                             | 2006      | 2005      | 2004      |
|---|-----------|-----------|-----------|
| Interest income:                                    |           |           |           |
| Loans (including fee income)                        | \$ 23,345 | \$ 20,724 | \$ 18,850 |
| Mortgage-backed securities                          | 4,989     | 4,160     | 4,137     |
| Tax exempt interest income:                         |           |           |           |
| State and municipal obligations                     | 2,080     | 1,947     | 1,615     |
| Taxable interest income:                            |           |           |           |
| U.S. Treasury and government agency securities      | 970       | 1,520     | 2,187     |
| Federal funds sold                                  | 560       | 265       | 98        |
| Other securities                                    | 65        | 95        | 34        |
| Deposits with banks                                 | 21        | 2         | 2         |
| Total interest income                               | 32,030    | 28,713    | 26,923    |
| Interest expense:                                   |           |           |           |
| Savings, N.O.W. and money market deposits           | 6,322     | 3,022     | 1,331     |
| Certificates of deposit of \$100,000 or more        | 888       | 550       | 475       |
| Other time deposits                                 | 723       | 470       | 457       |
| Other borrowed money                                | 216       | 205       | 55        |
| Federal funds purchased                             | 188       | 72        | 33        |
| Total interest expense                              | 8,337     | 4,319     | 2,351     |
| Net interest income                                 | 23,693    | 24,394    | 24,572    |
| Provision for loan losses                           | 85        | 300       | 300       |
| Net interest income after provision for loan losses | 23,608    | 24,094    | 24,272    |
| Other income:                                       |           |           |           |
| Service charges on deposit accounts                 | 2,069     | 2,104     | 2,328     |
| Fees for other customer services                    | 1,422     | 1,484     | 1,341     |
| Title fee income                                    | 1,042     | 1,293     | 866       |
| Net securities (losses) gains                       | (289)     | 116       | 734       |
| Other operating income                              | 169       | 108       | 171       |
| Total other income                                  | 4,413     | 5,105     | 5,440     |
| Other expenses:                                     |           |           |           |
| Salaries and employee benefits                      | 9,187     | 8,347     | 7,456     |
| Net occupancy expense                               | 1,414     | 1,234     | 1,283     |
| Furniture and fixture expense                       | 742       | 719       | 785       |
| Data/Item processing                                | 445       | 397       | 374       |
| Advertising   | 414       | 401       | 356       |
| Other operating expenses                            | 3,800     | 3,549     | 3,310     |
| Total other expenses                                | 16,002    | 14,647    | 13,564    |
| Income before provision for income taxes            | 12,019    | 14,552    | 16,148    |
| Provision for income taxes                          | 3,851     | 4,929     | 5,771     |
| Net income  | \$ 8,168  | \$ 9,623  | \$ 10,377 |
| Basic earnings per share                            | \$ 1.33   | \$ 1.54   | \$ 1.66   |

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|                            |    |              |    |       |    |       |
|----------------------------|----|--------------|----|-------|----|-------|
| Diluted earnings per share | \$ | <b>1.33</b>  | \$ | 1.53  | \$ | 1.64  |
| Comprehensive Income       | \$ | <b>9,019</b> | \$ | 6,877 | \$ | 9,094 |

*See accompanying notes to Consolidated Financial Statements.*

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Table of Contents**CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY**

(In thousands, except share and per share amounts)

|  | Common Stock<br>Shares<br>Outstanding | Common Stock<br>Amount | Comprehensive<br>Surplus | Comprehensive<br>Income <sup>(1)</sup> | Undivided<br>Profits | Treasury<br>Stock | Unearned<br>Stock<br>Awards | Accumulated<br>Other<br>Comprehensive<br>Income<br>(Loss) | Total     |
|--|---------------------------------------|------------------------|--------------------------|--|----------------------|-------------------|-----------------------------|---|-----------|
| Balance at   |                                       |                        |                          |  |                      |                   |                             |   |           |
| December 31, 2003                                      | 4,155,595                             | \$ 43                  | \$ 21,194                |  | \$ 21,982            | \$ (1,909)        | \$ (81)                     | \$ 1,565  | \$ 42,794 |
| Net income   |                                       |                        |                          | 10,377                                 | 10,377               |                   |                             |   | 10,377    |
| Stock awards vested                                    | 5,040                                 |                        | 30                       |  |                      | 66                | 73                          |   | 169       |
| Stock awards granted                                   |                                       |                        | 58                       |  |                      | 55                | (113)                       |   | -         |
| Exercise of stock options, net of tax benefit          | 24,417                                |                        | 201                      |  |                      | 69                |                             |   | 270       |
| Treasury stock purchases                               | (20,000)                              |                        |                          |  |                      | (611)             |                             |   | (611)     |
| Cash dividends declared, \$0.72 per share              |                                       |                        |                          |  | (4,503)              |                   |                             |   | (4,503)   |
| Effect of three-for-two stock split (in the form of a  |                                       |                        |                          |  |                      |                   |                             |   |           |
| Stock dividend)  | 2,089,437                             | 21                     | (21)                     |  |                      |                   |                             |   | -         |
| Other comprehensive income, net of tax                 |                                       |                        |                          |  |                      |                   |                             |   |           |
| Unrealized net losses in securities available for sale |                                       |                        |                          | (1,333)                                |                      |                   |                             | (1,333)   | (1,333)   |
| Minimum pension liability adjustment                   |                                       |                        |                          | 50                                     |                      |                   |                             | 50  | 50        |
| Comprehensive Income                                   |                                       |                        |                          | 9,094                                  |                      |                   |                             |   |           |
| Balance at   |                                       |                        |                          |  |                      |                   |                             |   |           |
| December 31, 2004                                      | 6,254,489                             | 64                     | 21,462                   |  | 27,856               | (2,330)           | (121)                       | 282   | 47,213    |
| Net income   |                                       |                        |                          | 9,623                                  | 9,623                |                   |                             |   | 9,623     |
| Stock awards vested                                    | 6,155                                 |                        | 36                       |  |                      | 28                | 65                          |   | 129       |
| Stock awards granted                                   |                                       |                        | 52                       |  |                      | 38                | (90)                        |   | -         |
| Stock awards forfeited                                 |                                       |                        | (17)                     |  |                      | (21)              | 38                          |   | -         |
| Exercise of stock options, net of tax benefit          | 21,821                                |                        | 98                       |  |                      | 134               |                             |   | 232       |
| Treasury stock purchases                               | (75,926)                              |                        |                          |  |                      | (2,134)           |                             |   | (2,134)   |

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|   |           |    |        |  |         |         |       |         |         |
|---|-----------|----|--------|--|---------|---------|-------|---------|---------|
| Cash dividends declared, \$0.91 per share   |           |    |        |  | (5,666) |         |       | (5,666) |         |
| Other comprehensive income, net of tax  |           |    |        |  |         |         |       |         |         |
| Unrealized net losses in securities available for sale  |           |    |        |  | (2,779) |         |       | (2,779) | (2,779) |
| Minimum pension liability adjustment  |           |    |        |  | 33      |         |       | 33      | 33      |
| Comprehensive Income  |           |    |        |  | 6,877   |         |       |         |         |
| Balance at December 31, 2005  | 6,206,539 | 64 | 21,631 |  | 31,813  | (4,285) | (108) | (2,464) | 46,651  |
| Net income  |           |    |        |  | 8,168   | 8,168   |       |         | 8,168   |
| Transfer due to adoption of SFAS 123(R)   |           |    | (108)  |  |         |         | 108   |         | -       |
| Stock awards vested   | 3,491     |    | 51     |  |         |         |       |         | 51      |
| Stock awards granted  | 15,987    |    | (189)  |  |         | 189     |       |         | -       |
| Stock awards forfeited  |           |    | 2      |  |         | (2)     |       |         | -       |
| Exercise of stock options, net of tax benefit   | 9,882     |    | 110    |  |         | (39)    |       |         | 71      |
| Stock option compensation expense   |           |    | 68     |  |         |         |       |         | 68      |
| Treasury stock purchases  | (157,334) |    |        |  |         | (4,039) |       |         | (4,039) |
| Cash dividends declared, \$0.92 per share   |           |    |        |  | (5,634) |         |       |         | (5,634) |
| Other comprehensive income, net of tax  |           |    |        |  |         |         |       |         |         |
| Change in unrealized net losses in securities available for sale, net of reclassification and tax effects |           |    |        |  | 851     |         |       | 851     | 851     |
| Adjustment to initially apply SFAS 158, net of tax  |           |    |        |  |         |         |       | (648)   | (648)   |
| Comprehensive Income  |           |    |        |  | 9,019   |         |       |         |         |

**Balance at**

|                          |           |    |    |    |        |  |    |        |    |         |  |   |    |         |    |        |
|--------------------------|-----------|----|----|----|--------|--|----|--------|----|---------|--|---|----|---------|----|--------|
| <b>December 31, 2006</b> | 6,078,565 | \$ | 64 | \$ | 21,565 |  | \$ | 34,347 | \$ | (8,176) |  | - | \$ | (2,261) | \$ | 45,539 |
|--------------------------|-----------|----|----|----|--------|--|----|--------|----|---------|--|---|----|---------|----|--------|

(1) Disclosure of reclassification amount:

|              |             |      |      |
|--------------|-------------|------|------|
| December 31, | <b>2006</b> | 2005 | 2004 |
|--------------|-------------|------|------|

Comprehensive

Income Items:

Unrealized gain

(loss) arising during

the period, net of tax

of \$456, (\$1,820),

and (\$591) in 2006,

|               |    |            |    |         |    |       |
|---------------|----|------------|----|---------|----|-------|
| 2005 and 2004 | \$ | <b>678</b> | \$ | (2,708) | \$ | (891) |
|---------------|----|------------|----|---------|----|-------|

Less: reclassification

adjustment, net of

taxes

of \$163, (\$46), and

(\$293) in 2006,

2005 and 2004

for (losses) gains

|                    |  |              |  |    |  |     |
|--------------------|--|--------------|--|----|--|-----|
| included in income |  | <b>(173)</b> |  | 71 |  | 442 |
|--------------------|--|--------------|--|----|--|-----|

|  |    |            |    |         |    |         |
|--|----|------------|----|---------|----|---------|
|  | \$ | <b>851</b> | \$ | (2,779) | \$ | (1,333) |
|--|----|------------|----|---------|----|---------|

*See accompanying notes to Consolidated Financial Statements.*

*Page 26*

Table of Contents**CONSOLIDATED STATEMENTS OF CASH FLOWS**

(In thousands)

| Year Ended December 31,  | 2006            | 2005            | 2004            |
|--|-----------------|-----------------|-----------------|
| Operating activities:  |                 |                 |                 |
| Net Income   | \$ 8,168        | \$ 9,623        | \$ 10,377       |
| Adjustments to reconcile net income to net cash provided by operating activities:    |                 |                 |                 |
| Provision for loan losses  | 85              | 300             | 300             |
| Depreciation and amortization  | 886             | 847             | 950             |
| Amortization and accretion, net  | 272             | 786             | 1,261           |
| Share based compensation expense   | 119             | 65              | 73              |
| SERP expense   | 268             | 153             | 149             |
| Net securities losses (gains)  | 289             | (116)           | (734)           |
| Increase in accrued interest receivable  | (68)            | (155)           | (110)           |
| (Provision) benefit for deferred income taxes  | (400)           | 21              | (179)           |
| Decrease (increase) in other assets  | 1,975           | (986)           | 1,118           |
| (Decrease) increase in accrued and other liabilities                                 | (35)            | 405             | 436             |
| <b>Net cash provided by operating activities</b>                                     | <b>11,559</b>   | <b>10,943</b>   | <b>13,641</b>   |
| Investing activities:  |                 |                 |                 |
| Purchases of securities available for sale   | (62,500)        | (32,273)        | (95,820)        |
| Purchases of securities, restricted  | (10,343)        | (190)           | (337)           |
| Purchases of securities held to maturity   | (9,444)         | (13,262)        | (21,213)        |
| Proceeds from sales of securities available for sale                                 | 19,537          | 21,173          | 56,005          |
| Proceeds from redemption of securities, restricted                                   | 10,842          | 792             | -               |
| Proceeds from maturing securities available for sale                                 | 5,675           | 2,995           | 4,750           |
| Proceeds from maturing securities held to maturity                                   | 10,012          | 24,463          | 14,396          |
| Proceeds from principal payments on mortgage-backed securities                       | 18,361          | 22,032          | 23,980          |
| Net increase in loans  | (23,689)        | (6,235)         | (23,202)        |
| Purchases of banking premises and equipment, net of disposals                        | (3,251)         | (2,670)         | (3,144)         |
| <b>Net cash (used) provided by investing activities</b>                              | <b>(44,800)</b> | <b>16,825</b>   | <b>(44,585)</b> |
| Financing activities:  |                 |                 |                 |
| Net increase (decrease) in deposits  | 36,387          | (1,286)         | 12,165          |
| Increase (decrease) in other borrowings  | 4,100           | (12,200)        | 20,800          |
| Purchase of Treasury stock   | (4,039)         | (2,134)         | (611)           |
| Net proceeds from exercise of stock options issued pursuant to equity incentive plan | 49              | 216             | 203             |
| Cash dividends paid  | (5,668)         | (5,551)         | (5,790)         |
|  | <b>30,829</b>   | <b>(20,955)</b> | <b>26,767</b>   |

**Net cash provided (used) by financing activities**

|  |           |               |           |        |           |         |
|--|-----------|---------------|-----------|--------|-----------|---------|
| (Decrease) increase in cash and cash equivalents |           | (2,412)       |           | 6,813  |           | (4,177) |
| Cash and cash equivalents beginning of year      |           | 15,675        |           | 8,862  |           | 13,039  |
| <b>Cash and cash equivalents end of year</b>     | <b>\$</b> | <b>13,263</b> | <b>\$</b> | 15,675 | <b>\$</b> | 8,862   |

**Supplemental Information-Cash Flows:**

## Cash paid for:

|   |    |       |    |       |    |       |
|---|----|-------|----|-------|----|-------|
| Interest                                    | \$ | 7,810 | \$ | 4,264 | \$ | 2,344 |
| Income taxes                                | \$ | 3,323 | \$ | 5,023 | \$ | 5,336 |
| Noncash investing and financing activities: |    |       |    |       |    |       |
| Dividends declared and unpaid               | \$ | 1,394 | \$ | 1,428 | \$ | 1,313 |

See accompanying notes to Consolidated Financial Statements.

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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

December 31, 2006, 2005 and 2004

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Bridge Bancorp, Inc. (the “Company”) is incorporated under the laws of the State of New York as a single bank holding company. The Company’s business currently consists of the operations of its wholly-owned subsidiary, The Bridgehampton National Bank (the “Bank”). The Bank’s operations include its real estate investment trust subsidiary, Bridgehampton Community, Inc. (“BCI) and a financial title insurance subsidiary; the now dissolved Bridgehampton Abstract Holding LLC, which had a 100% ownership in an investment in Bridge Abstract LLC (“Bridge Abstract”). Effective April 1, 2004, Bridgehampton Abstract Holding LLC ownership interest in Bridge Abstract increased to 100% from 51% ownership. Subsequent to December 31, 2004, Bridgehampton Abstract Holding LLC was dissolved. The financial statements have been prepared in accordance with U.S. generally accepted accounting principles and to general practices within the financial institution industry. The following is a description of the significant accounting policies that the Company follows in preparing its Consolidated Financial Statements.

a) Basis of Financial Statement Presentation

The accompanying Consolidated Financial Statements are prepared on the accrual basis of accounting and include the accounts of the Company and its wholly-owned subsidiary, the Bank. All material intercompany transactions and balances have been eliminated.

The preparation of financial statements, in conformity with U.S. generally accepted accounting principles, requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of each consolidated statement of condition and the related consolidated statement of income for the years then ended. Such estimates are subject to change in the future as additional information becomes available or previously existing circumstances are modified. Actual future results could differ significantly from those estimates. The allowance for loan losses, fair values of financial instruments, deferred taxes, prepayment speeds on mortgage-backed securities, and pension are particularly subject to change. Certain reclassifications have been made to prior year amounts, and the related discussion and analysis, to conform to the current year presentation.

b) Cash and Cash Equivalents

For purposes of reporting cash flows, cash and cash equivalents include cash on hand, amounts due from banks and federal funds sold, which mature overnight. Cash flows are reported net for customer loan and deposit transactions and overnight borrowings.

c) Securities

The Company is required to report readily-marketable equity and debt securities in one of the following categories: (i) “held-to-maturity” (management has a positive intent and ability to hold to maturity), which are to be reported at amortized cost and (ii) “available for sale” (all other debt and marketable equity securities), which are to be reported at fair value, with unrealized gains and losses reported net of tax, as accumulated other comprehensive income, a separate component of stockholders’ equity. Restricted securities, as disclosed on the balance sheet including Federal Home Loan Bank stock and Federal Reserve Bank stock, are carried at cost.

Premiums and discounts on securities are amortized to expense and accreted to income over the estimated life of the respective securities using the interest method. Gains and losses on the sales of securities are recognized upon realization based on the specific identification method. Declines in the fair value of securities below their cost that are

other than temporary are reflected as realized losses. In estimating other-than-temporary losses, management considers: (1) the length of time and extent that fair value has been less than cost, (2) the financial condition and near term prospects of the issuer, and (3) the Company's ability and intent to hold the security for a period sufficient to allow for any anticipated recovery in fair value.

d) Loans and Loan Interest Income Recognition

Loans are stated at the principal amount outstanding, less net deferred origination fees. Loan origination and commitment fees and certain direct and indirect costs incurred in connection with loan originations are deferred and amortized to income over the life of the related loans as an adjustment to yield. When a loan prepays, the remaining unamortized net deferred origination fees are recognized in the current year. Interest on loans is credited to income based on the principal outstanding during the period. Loans that are 90 days past due are automatically placed on nonaccrual and previously accrued interest is reversed and charged against interest income. However, if the Bank has reasonable assurance that the loan will be fully collectible based upon individual loan evaluation assessing such factors as collateral and collectibility, accrued interest will be recognized as earned. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

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A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value and the probability of collecting scheduled principal and interest payments when due. The impairment of a loan is measured at the reset value of expected future cash flows using the loan's effective interest rate, or at the loan's observable market price or the fair value of the collateral if the loan is collateral dependent. Generally, the Bank measures impairment of such loans by reference to the fair value of the collateral. Loans that experience minor payment delays and payment shortfall generally are not classified as impaired.

e) Allowance for Loan Losses

The Bank monitors its entire loan portfolio on a regular basis, with consideration given to detailed analyses of classified loans, repayment patterns, current delinquencies, probable incurred losses, past loss experience, current economic conditions, and various types of concentrations of credit. Additions to the allowance are charged to expense and realized losses, net of recoveries, are charged to the allowance. Based on the determination of management and the Classification Committee, the overall level of reserves is periodically adjusted to account for the inherent and specific risks within the entire portfolio. Based on the Classification Committee's review of the classified loans and the overall reserve levels as they relate to the entire loan portfolio at December 31, 2006, management believes the allowance for loan losses is adequate.

A loan is considered a potential charge-off when it is in default of either principal or interest for a period of 90, 120 or 180 days, depending upon the loan type, as of the end of the prior month. In addition to date criteria, other triggering events may include, but are not limited to, notice of bankruptcy by the borrower or guarantor, death of the borrower, and deficiency balance from the sale of collateral.

While management uses available information to recognize losses on loans, future additions to the allowance may be necessary based on changes in conditions. In addition, various regulatory agencies, as an integral part of the examination process, periodically review the Bank's allowance for loan losses. Such agencies may require the Bank to recognize additions to, or charge-offs against, the allowance based on their judgment about information available to them at the time of their examination.

f) Banking Premises and Equipment

Buildings, furniture and fixtures and equipment are stated at cost less accumulated depreciation. Buildings and related components are depreciated using the straight-line method using a useful life of fifty years for buildings and a range of two to ten years for equipment, computer hardware and software, and furniture and fixtures. Leasehold improvements are amortized over the lives of the respective leases or the service lives of the improvements whichever is shorter. Land is recorded at cost.

Improvements and major repairs are capitalized, while the cost of ordinary maintenance, repairs and minor improvements is charged to operations.

g) Other Real Estate Owned

Other real estate owned consists of real estate acquired by foreclosure or deed in lieu of foreclosure and is recorded at the lower of the net unpaid principal balance at the foreclosure date plus acquisition costs or fair value. Subsequent valuation adjustments are made if fair value less estimated costs to sell the property falls below the carrying amount. At December 31, 2006 and 2005, the Company carried no other real estate owned.

h) Loan Commitments and Related Financial Instruments

Financial instruments include off-balance sheet credit instruments, such as commitments to make loans and commercial letters of credit, issued to meet customer-financing needs. The face amount for these items represents the exposure to loss, before considering customer collateral or ability to repay.

i) Income Taxes

The Company follows the asset and liability approach, which requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the carrying amounts and the tax bases of assets and liabilities, computed using enacted tax rates. Deferred tax assets are recognized if it is more likely than not that a future benefit will be realized. It is management's position, as currently supported by the facts and circumstances, that no valuation allowance is necessary against any of the Company's deferred tax assets.

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## j) Treasury Stock

Repurchases of common stock are recorded as treasury stock at cost. Treasury stock is reissued using the first in, first out method.

## k) Earnings Per Share

Diluted earnings per share, which reflects the potential dilution that could occur if outstanding stock options were exercised and if stock awards were fully vested and resulted in the issuance of common stock that then shared in the earnings of the Company, is computed by dividing net income by the weighted average number of common shares and common stock equivalents.

## l) Dividends

Cash available for dividend distribution to shareholders of the Company must initially come from dividends paid by the Bank to the Company. The approval of the Regional Administrator of National Banks is required if the total of all dividends declared by the Bank in any calendar year exceeds the total of the Bank's net income of that year combined with its retained net income of the preceding two years. The Bank had approximately \$7,156,000 available as of December 31, 2006, which may be paid to the Company as a dividend without prior approval.

## m) Stock Activity

All references in the Consolidated Financial Statements and Notes thereto for per share amounts, and market prices of the common stock have been restated giving retroactive recognition to the stock split as of July 9, 2004.

The transactions affecting common stock issued and outstanding and treasury stock are reflected in the table below:

|                                 | Common Stock |             |          |
|---------------------------------|--------------|-------------|----------|
|                                 | Shares       |             |          |
|                                 | Shares       | Issued and  | Treasury |
|                                 | Issued       | Outstanding | Stock    |
| Balance at<br>December 31, 2004 | 6,386,306    | 6,254,489   | 131,817  |
| Stock awards<br>vested          |              | 6,155       | (6,155)  |
| Exercise of stock<br>options    |              | 21,821      | (21,821) |
| Purchase of<br>Treasury stock   |              | (75,926)    | 75,926   |
| Balance at<br>December 31, 2005 | 6,386,306    | 6,206,539   | 179,767  |
| Stock awards<br>vested          |              | 3,491       | (3,491)  |
| Stock awards<br>granted         |              | 15,987      | (15,987) |
|                                 |              | 9,882       | (9,882)  |

|                                     |                  |                  |                |
|-------------------------------------|------------------|------------------|----------------|
| Exercise of stock options           |                  |                  |                |
| Purchase of Treasury stock          | (157,334)        | 157,334          |                |
| <b>Balance at December 31, 2006</b> | <b>6,386,306</b> | <b>6,078,565</b> | <b>307,741</b> |

## n) Segment Reporting

While management monitors the revenue streams of the various products and services, the identifiable segments are not material and operations are managed and financial performance is evaluated on a Company-wide basis. Accordingly, all of the financial service operations are considered by management to be aggregated in one reportable operating segment.

## o) Stock Based Compensation Plans

Statement of Financial Accounting Standards 123(R) (“SFAS 123(R)”), “*Accounting for Stock-Based Compensation, Revised*,” requires all public companies to record compensation cost for stock options provided to employees in return for employee service. The cost is measured at the fair value of the options when granted, and this cost is expensed over the employee service period, which is normally the vesting period of the options. The Company adopted SFAS 123(R) beginning January 1, 2006 applying the modified prospective transition method. Under the modified prospective transition method, the financial statements will not reflect restated amounts.

Prior to 2006, substantially all of the options granted by the Company vested immediately; compensation expense would be recorded on the date of grant.

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The following table illustrates the effect on net income and earnings per share if expense was measured using the fair value recognition provisions of SFAS 123(R). The Black-Scholes option pricing model was used to estimate the grant date fair value of option grants.

| For the Year Ended<br>(In thousands, except per<br>share) |                 | 2005     | 2004      |
|---|-----------------|----------|-----------|
| Net Income:   | As<br>Reported: | \$ 9,623 | \$ 10,377 |
|   | Pro<br>Forma:   | 9,606    | 10,332    |
| Diluted EPS:  | As<br>Reported: | \$ 1.53  | \$ 1.64   |
|   | Pro<br>Forma:   | 1.53     | 1.64      |
| Basic EPS:  | As<br>Reported: | \$ 1.54  | \$ 1.66   |
|   | Pro<br>Forma:   | 1.54     | 1.65      |

## p) Comprehensive Income

Comprehensive income includes net income and all other changes in equity during a period, except those resulting from investments by owners and distributions to owners. Other comprehensive income includes revenues, expenses, gains and losses that under generally accepted accounting principles are included in comprehensive income but excluded from net income. Comprehensive income and accumulated other comprehensive income are reported net of related income taxes. Accumulated other comprehensive income for the Company includes unrealized holding gains or losses on available for sale securities, the minimum pension liability for the years prior to the adoption of SFAS No. 158, and the transition to adopt Statement of Financial Accounting Standards 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 employers to recognize the overfunded or underfunded status of a defined benefit postretirement plan as an asset or liability in its statement of financial position and to recognize changes in that funded status in the year the changes occur through comprehensive income. Such gains or losses are net of reclassification adjustments for realized gains (losses) on sales of available for sale securities.

## q) Fair Value of Financial Instruments

Fair values of financial instruments are estimated using relevant market information and other assumptions, as more fully disclosed in a separate note. Fair value estimates involve uncertainties and matters of significant judgment regarding interest rates, credit risk, prepayments, and other factors, especially in the absence of broad markets for particular items. Changes in assumptions or in market conditions could significantly affect the estimates.

## r) New Accounting Standards

In February 2006, the FASB issued SFAS No. 155, “*Accounting for Certain Hybrid Financial Instruments — An Amendment of FASB Statement No. 133 and 140*” (“SFAS 155”). SFAS 155 simplifies the accounting for certain hybrid financial instruments that contain an embedded derivative that otherwise would have required bifurcation. SFAS 155 also eliminates the interim guidance in FASB Statement No. 133, which provides that beneficial interest in securitized financial assets are not subject to the provisions of FASB Statement No. 133. SFAS 155 is effective for all financial instruments acquired or issued after the beginning of an entity’s first fiscal year that begins after September 15, 2006,

which for the Company will be as of the beginning of fiscal 2007. The Company does not believe that the adoption of SFAS 155 will have a significant effect on its financial statements as the Company does not have any hybrid financial instruments at this time.

In March 2006, the FASB issued SFAS No. 156, "*Accounting for Servicing of Financial Assets — An Amendment of FASB Statement No. 140*" ("SFAS 156"). SFAS 156 requires that all separately recognized servicing assets and servicing liabilities be initially measured at fair value, if practicable. The statement permits, but does not require, the subsequent measurement of servicing assets and servicing liabilities at fair value. SFAS 156 is effective as of the beginning of an entity's first fiscal year that begins after September 15, 2006. The Company does not believe that the adoption of SFAS 156 will have a significant effect on its financial statements as the Company does not have servicing assets/liabilities at this time.

In February 2006, the FASB issued FASB Staff Position No. FAS 123(R)-4, "*Classification of Options and Similar Instruments Issued as Employee Compensation That Allow for Cash Settlement upon the Occurrence of a Contingent Event.*" This position amends SFAS 123R to incorporate that a cash settlement feature that can be exercised only upon the occurrence of a contingent event that is outside the employee's control does not meet certain conditions in SFAS 123R until it becomes probable that the event will occur. The guidance in this FASB Staff Position was applied upon initial adoption of SFAS 123R and had no effect on the financial statements.



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In June 2006, the FASB issued Interpretation No. 48, “*Accounting for Uncertainty in Income Taxes - An interpretation of FASB No. 109*” (“FIN 48”). 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. The Interpretation is effective for fiscal years beginning after December 15, 2006. The Company has evaluated the impact of FIN 48 and believes the adoption will have an immaterial effect on its results of operations, financial position and liquidity.

In September 2006, the FASB issued SFAS No. 157, “*Fair Value Measurements*” (“SFAS 157”). SFAS 157 defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. This statement does not require any new fair value measurements. It is effective for financial statements issued for fiscal years beginning after November 15, 2007. The Company is currently evaluating the impact of the adoption of SFAS 157, with respect to its current practice of measuring fair value and disclosure in its financial statements.

In September 2006, the FASB issued SFAS No. 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”). SFAS 158 requires employers to recognize the overfunded or underfunded status of a defined benefit postretirement plan as an asset or liability in its statement of financial position, beginning with the year end 2006, and to recognize changes in that funded status in the year the changes occur through comprehensive income beginning in 2007. Additionally, defined benefit plan assets and obligations are to be measured as of the date of the employer’s fiscal year end, starting in 2008. This statement is effective as of the end of the fiscal year ending after December 15, 2006. The Company has adopted SFAS 158 and its effects on the 2006 balance sheet are as follows.

|   | Before<br>Application<br>of SFAS No.<br>158 Adjustments | After<br>Application<br>of SFAS No.<br>158 |
|---|---|--|
| (In thousands)                                |   |  |
| Liability for pension and SERP benefits       | \$ (169)  | \$ 1,226                                   |
| Deferred income taxes                         | (1,311)   | (490)                                      |
| <b>Total Liabilities</b>                      | <b>527,369</b>  | <b>736</b>                                 |
| Accumulated other comprehensive income/(loss) | (1,613)   | (648)                                      |
| <b>Total stockholders’ equity</b>             | <b>46,187</b>   | <b>(648)</b>                               |
|   |   | <b>45,539</b>                              |

In September 2006, the U.S. Securities and Exchange Commission (“SEC”) amended Part 211 of Title 17 of the Code of Federal Regulations by adding the Staff Accounting Bulletin No. 108, “*Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements*” (“SAB 108”). SAB 108 provides guidance on the consideration of the effects of prior year misstatements in quantifying current year misstatements for the purpose of a materiality assessment. SAB 108 is effective for fiscal years ending after November 15, 2006. The Company has reviewed SAB 108 and the application does not have an effect on the financial statements.

## s) Reclassifications

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

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## 2. SECURITIES

A summary of the amortized cost, gross unrealized gains, gross unrealized losses and estimated fair value of securities is as follows:

| December 31,<br>(In thousands)                       | 2006              |                              |                               |                            | 2005              |                              |                               |                            |
|--|-------------------|------------------------------|-------------------------------|----------------------------|-------------------|------------------------------|-------------------------------|----------------------------|
|  | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Estimated<br>Fair<br>Value | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Estimated<br>Fair<br>Value |
| Available for sale:                                  |                   |                              |                               |                            |                   |                              |                               |                            |
| U.S. Treasury and<br>government<br>agency securities | \$ 34,123         | \$ -                         | \$ (346)                      | \$ 33,777                  | \$ 38,443         | \$ 7                         | \$ (788)                      | \$ 37,662                  |
| State and municipal<br>obligations                   | 49,008            | 316                          | (481)                         | 48,843                     | 51,392            | 387                          | (559)                         | 51,220                     |
| Mortgage-backed<br>securities                        | 122,009           | 364                          | (2,403)                       | 119,970                    | 96,938            | 27                           | (3,046)                       | 93,919                     |
| Total available for sale                             | 205,140           | 680                          | (3,230)                       | 202,590                    | 186,773           | 421                          | (4,393)                       | 182,801                    |
| Held to maturity:                                    |                   |                              |                               |                            |                   |                              |                               |                            |
| State and municipal<br>obligations                   | 9,444             | -                            | (2)                           | 9,442                      | 10,012            | -                            | (23)                          | 9,989                      |
| Total held to maturity                               | 9,444             | -                            | (2)                           | 9,442                      | 10,012            | -                            | (23)                          | 9,989                      |
| Total debt and equity<br>securities                  | \$ 214,584        | \$ 680                       | \$ (3,232)                    | \$ 212,032                 | \$ 196,785        | \$ 421                       | \$ (4,416)                    | \$ 192,790                 |

Securities with unrealized losses at year-end 2006 and 2005, aggregated by category and length of time that individual securities have been in a continuous unrealized loss position, are as follows:

| December 31,<br>(In thousands)                       | 2006  |        |  |          | 2005   |          |  |          |
|--|---|--------|--|----------|--|----------|--|----------|
|  | Less than 12<br>months<br>Unrealized<br>Fair<br>Value |        | Greater than 12<br>months<br>Unrealized<br>Fair<br>Value |          | Less than 12 months<br>Unrealized<br>Fair<br>Value |          | Greater than 12<br>months<br>Unrealized<br>Fair<br>Value |          |
|  |   | Losses |  | Losses   |  | Losses   |  | Losses   |
| U.S. Treasury and<br>government<br>agency securities | \$ 13,684   | \$ 13  | \$ 20,093  | \$ 333   | \$ 14,132  | \$ 243   | \$ 18,048  | \$ 546   |
| State and municipal<br>obligations                   | 9,343   | 13     | 25,228   | 470      | 31,635   | 266      | 9,214  | 316      |
| Mortgage-backed<br>securities                        | 1,252   | 5      | 75,135   | 2,398    | 42,354   | 860      | 50,736   | 2,185    |
| Total temporarily<br>impaired securities             | \$ 24,279   | \$ 31  | \$ 120,456   | \$ 3,201 | \$ 88,121  | \$ 1,369 | \$ 77,998  | \$ 3,047 |

Unrealized losses on securities have not been recognized into income, as the losses on these securities would be expected to dissipate as they approach their maturity dates. The Company evaluates securities for other-than-temporary impairment periodically with increased frequency when economic or market concerns warrant

such evaluation. Consideration is given to the length of time and the extent to which the fair value has been less than cost, the financial condition and near-term prospects of the issuer, and the intent and ability of the Company to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value. In analyzing an issuer's financial condition, the Company may consider whether the securities are issued by the federal government or its agencies, whether downgrades by bond rating agencies have occurred, and the results of reviews of the issuer's financial condition.

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The following table sets forth the fair value, amortized cost, maturities and approximated weighted average yield (based on the estimated annual income divided by the average book value) at December 31, 2006. 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. Yields on tax-exempt obligations have been computed on a tax-equivalent basis.

December 31,  
2006

(Dollars in  
thousands)

|  | Within<br>One Year      |                             |       | After One But<br>Within Five Years |                             |       | After Five But<br>Within Ten Years |                             |       | After<br>Ten Years      |                             |       |
|--|-------------------------|-----------------------------|-------|------------------------------------|-----------------------------|-------|------------------------------------|-----------------------------|-------|-------------------------|-----------------------------|-------|
|  | Fair<br>Value<br>Amount | Amortized<br>Cost<br>Amount | Yield | Fair<br>Value<br>Amount            | Amortized<br>Cost<br>Amount | Yield | Fair<br>Value<br>Amount            | Amortized<br>Cost<br>Amount | Yield | Fair<br>Value<br>Amount | Amortized<br>Cost<br>Amount | Yield |
| Available for<br>sale:                                     |                         |                             |       |                                    |                             |       |                                    |                             |       |                         |                             |       |
| U.S. Treasury<br>and<br>government<br>agency<br>securities | \$ 21,566               | \$ 21,695                   | 6.76% | \$ 12,211                          | \$ 12,428                   | 5.51% | \$ -                               | \$ -                        | -%    | \$ -                    | \$ -                        | -%    |
| Mortgage-backed<br>securities                              | -                       | -                           | -     | 12,338                             | 12,739                      | 5.86  | 10,843                             | 11,138                      | 6.15  | 96,789                  | 98,132                      | 7.02  |
| State and<br>municipal<br>obligations                      | 6,931                   | 6,884                       | 7.18  | 19,926                             | 20,294                      | 4.22  | 14,675                             | 14,535                      | 5.52  | 7,311                   | 7,295                       | 5.60  |
| Total available<br>for sale                                | 28,497                  | 28,579                      | 6.86  | 44,475                             | 45,461                      | 5.03  | 25,518                             | 25,673                      | 5.79  | 104,100                 | 105,427                     | 6.92  |
| Held to maturity:  |                         |                             |       |                                    |                             |       |                                    |                             |       |                         |                             |       |
| State and<br>municipal<br>obligations                      | 9,442                   | 9,444                       | 5.46  | -                                  | -                           | -     | -                                  | -                           | -     | -                       | -                           | -     |
| Total held to<br>maturity                                  | 9,442                   | 9,444                       | 5.46  | -                                  | -                           | -     | -                                  | -                           | -     | -                       | -                           | -     |
| Total debt and<br>equity<br>securities                     | \$ 37,939               | \$ 38,023                   | 6.51% | \$ 44,475                          | \$ 45,461                   | 5.03% | \$ 25,518                          | \$ 25,673                   | 5.79% | \$ 104,100              | \$ 105,427                  | 6.92% |

There were \$19,537,000, \$21,173,000 and \$56,005,000 of proceeds on sales of available for sale securities in 2006, 2005, and 2004, respectively. Gross gains of approximately \$13,000, \$180,000, and \$1,126,000 were realized on sales of available for sale securities during 2006, 2005, and 2004, respectively. Gross losses of approximately \$302,000, \$65,000, and \$392,000 were realized on sales of available for sale securities during 2006, 2005, and 2004, respectively. There were no sales of held to maturity securities during 2006, 2005, and 2004.

Securities having a fair value of approximately \$198,967,000 and \$148,861,000 at December 31, 2006 and 2005, respectively, were pledged to secure public deposits and Federal Home Loan Bank and Federal Reserve Bank overnight borrowings. The Company did not hold any trading securities during the year ended December 31, 2006 or 2005.

There was no investment that exceeded 10% of stockholders' equity at December 31, 2006.

### 3. LOANS

The following table sets forth the major classifications of loans:

| December 31,<br>(In thousands)                   | 2006       | 2005       |
|--|------------|------------|
| Real estate mortgage loans                       | \$ 265,824 | \$ 242,928 |
| Commercial, financial, and agricultural<br>loans | 36,498     | 31,644     |
| Installment/consumer loans                       | 8,848      | 9,827      |
| Real estate construction loans                   | 14,767     | 17,960     |
| Total loans                                      | 325,937    | 302,359    |
| Net deferred loan cost and fees                  | 60         | (95)       |
|  | 325,997    | 302,264    |
| Allowance for loan losses                        | (2,512)    | (2,383)    |
| Net loans  | \$ 323,485 | \$ 299,881 |

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Table of Contents**Lending Risk**

The principal business of the Bank is lending, primarily in commercial real estate loans, construction loans, home equity loans, land loans, consumer loans, residential mortgages and commercial loans. The Bank considers its primary lending area to be eastern Long Island in Suffolk County, New York, and a substantial portion of the Bank's loans are secured by real estate in this area. Accordingly, the ultimate collectibility of such a loan portfolio is susceptible to changes in market and economic conditions in this region.

**Allowance for Loan Losses**

The following table sets forth changes in the allowance for loan losses.

| December 31,<br>(In thousands)                  | 2006     | 2005     | 2004     |
|---|----------|----------|----------|
| Allowance for loan losses                       |          |          |          |
| balance at beginning of period                  | \$ 2,383 | \$ 2,188 | \$ 2,144 |
| Charge-offs:                                    |          |          |          |
| Real estate mortgage loans                      | -        | 7        | 3        |
| Commercial, financial and agricultural loans    | 33       | 153      | 302      |
| Installment/consumer loans                      | 50       | 129      | 65       |
| Total   | 83       | 289      | 370      |
| Recoveries:                                     |          |          |          |
| Real estate mortgage loans                      | 7        | 17       | 23       |
| Real estate construction loans                  | -        | 100      | -        |
| Commercial, financial and agricultural loans    | 59       | 37       | 61       |
| Installment/consumer loans                      | 61       | 30       | 30       |
| Total   | 127      | 184      | 114      |
| Net recoveries (charge-offs)                    | 44       | (105)    | (256)    |
| Provision for loan losses charged to operations | 85       | 300      | 300      |
| Balance at end of period                        | \$ 2,512 | \$ 2,383 | \$ 2,188 |

**Past Due, Nonaccrual and Restructured Loans**

Nonaccrual loans at December 31, 2006 and 2005 were \$423,000 and \$658,000, respectively. There were no loans 90 days or more past due that were still accruing at December 31, 2006 and 2005. Gross interest income on nonaccrual loans that would have been recorded under original terms during the year ended December 31, 2006, 2005, and 2004 were \$10,000, \$38,000, and \$16,000, respectively. Gross interest income recorded on these loans during the year ended December 31, 2006, 2005 and 2004 were \$21,000, \$17,000, and \$12,000, respectively.

As of December 31, 2006 and 2005, the Bank did not have any impaired loans as defined in SFAS No. 114. For a loan to be considered impaired, management determines after review whether it is probable that the Company will not be able to collect all amounts due according to the contractual terms of the loan agreement. Additionally management applies its normal loan review procedures in making these judgments. As of December 31, 2006 there was one loan considered to be a troubled debt restructuring, totaling \$118,000, as defined by SFAS No. 114. After review of the estimated fair value of the underlying collateral less the costs to sell, management believes it will be able to collect all amounts due without a shortfall according to the modified terms of the loan agreements. There were no restructured

loans as December 31, 2005.

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Table of Contents**Related Party Loans**

Certain directors, executive officers, and their related parties, including their immediate families and companies in which they are principal owners, were loan customers of the Bank during 2006 and 2005.

The following table sets forth selected information about related party loans at December 31, 2006.

|  | Balance<br>Outstanding |
|--|------------------------|
| (In<br>thousands)                            |                        |
| Balance at<br>December<br>31, 2005           | \$ 1,788               |
| New loans                                    | 206                    |
| Effective<br>change in<br>related<br>parties | -                      |
| Advances                                     | 8                      |
| Repayments                                   | (823)                  |
| Balance at<br>December<br>31, 2006           | \$ 1,179               |

**4. BANKING PREMISES AND EQUIPMENT**

Banking premises and equipment consist of:

| December 31,<br>(In thousands)                     | 2006             | 2005      |
|--|------------------|-----------|
| Land   | \$ 6,142         | \$ 6,142  |
| Construction in progress                           | 3,242            | 426       |
| Building and improvements                          | 8,741            | 8,632     |
| Furniture and fixtures                             | 7,108            | 6,797     |
| Leasehold improvements                             | 1,238            | 1,234     |
|  | <b>26,471</b>    | 23,231    |
| Less: accumulated<br>depreciation and amortization | <b>(8,466)</b>   | (7,591)   |
|  | <b>\$ 18,005</b> | \$ 15,640 |

**5. DEPOSITS****Time Deposits**

The following table sets forth the remaining maturities of the Bank's time deposits at December 31, 2006.

| (In thousands) | \$100,000<br>Less than<br>\$100,000 | or<br>Greater | Total |
|----------------|-------------------------------------|---------------|-------|
|                |                                     |               |       |



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|                               |           |           |           |
|-------------------------------|-----------|-----------|-----------|
| 3 months or less              | \$ 13,633 | \$ 22,453 | \$ 36,086 |
| Over 3 thru 6 months          | 9,149     | 4,640     | 13,789    |
| Over 6 thru 12 months         | 3,778     | 2,484     | 6,262     |
| Over 12 months thru 24 months | 2,739     | 630       | 3,369     |
| Over 24 months thru 36 months | 534       | 110       | 644       |
| Over 36 months thru 48 months | 467       | 201       | 668       |
| Over 48 months thru 60 months | -         | -         | -         |
| Over 60 months                | -         | -         | -         |
| Total                         | \$ 30,300 | \$ 30,518 | \$ 60,818 |

Deposits from principal officers, directors and their affiliates at year-end 2006 and 2005 were approximately \$2,938,000 and \$3,526,000, respectively. Public fund deposits at year-end 2006 and 2005 were \$119,823,000 and \$75,399,000, respectively.

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## 6. INCOME TAXES

The components of the provision for income taxes are as follows:

| Year Ended<br>December 31,<br>(In thousands) | 2006            | 2005     | 2004     |
|--|-----------------|----------|----------|
| Current:                                     |                 |          |          |
| Federal                                      | \$ 2,967        | \$ 4,087 | \$ 4,453 |
| State  | 484             | 863      | 1,139    |
|  | <b>3,451</b>    | 4,950    | 5,592    |
| Deferred:                                    |                 |          |          |
| Federal                                      | 310             | (22)     | 152      |
| State  | 90              | 1        | 27       |
|  | <b>400</b>      | (21)     | 179      |
| Total  | \$ <b>3,851</b> | \$ 4,929 | \$ 5,771 |

The reconciliation of the expected Federal income tax expense at the statutory tax rate to the actual provision follows:

| Year Ended December<br>31,<br>(Dollars in thousands)   | 2006     |                                      | 2005     |                                      | 2004     |                                      |
|--|----------|--------------------------------------|----------|--------------------------------------|----------|--------------------------------------|
|  | Amount   | Percentage<br>of Pre-tax<br>Earnings | Amount   | Percentage<br>of Pre-tax<br>Earnings | Amount   | Percentage<br>of Pre-tax<br>Earnings |
| Federal income tax<br>expense computed by<br>applying<br>the statutory rate to income<br>before income taxes | \$ 4,087 | 34%                                  | \$ 4,984 | 34%                                  | \$ 5,531 | 34%                                  |
| Tax exempt interest  | (706)    | (6)                                  | (665)    | (5)                                  | (552)    | (4)                                  |
| State taxes, net of Federal<br>income tax benefit  | 379      | 3                                    | 568      | 4                                    | 767      | 5                                    |
| Other  | 91       | 1                                    | 42       | 1                                    | 25       | 1                                    |
| Provision for income<br>taxes  | \$ 3,851 | 32%                                  | \$ 4,929 | 34%                                  | \$ 5,771 | 36%                                  |

Deferred tax assets and liabilities are comprised of the following:

| December 31,<br>(In thousands) | 2006         | 2005     |
|--------------------------------|--------------|----------|
| Deferred tax assets:           |              |          |
| Allowance for loan<br>losses   | \$ 1,102     | \$ 1,026 |
| Depreciation                   | -            | 15       |
| Total                          | <b>1,102</b> | 1,041    |
| Deferred tax liabilities:      |              |          |
| Pension expense                | (265)        | (211)    |
| Other                          | (219)        | (203)    |
| Depreciation                   | (332)        | -        |

|   |                 |          |
|---|-----------------|----------|
| Total                                   | <b>(816)</b>    | (414)    |
| Total before other comprehensive income | <b>286</b>      | 627      |
| SFAS 115 deferred tax asset             | <b>1,025</b>    | 1,596    |
| Minimum SERP liability adjustment       | -               | 59       |
| Transition to SFAS 158                  | <b>490</b>      | -        |
| Net deferred tax asset                  | <b>\$ 1,801</b> | \$ 2,282 |

Since the Bank has exceeded the threshold of \$500,000,000 in average assets, the tax basis in the bad debt reserve prior to January 1, 2004 is to be recaptured for federal tax purposes. The Bank intends to recapture this using the deferral method and has previously provided for the taxes relating to this recapture. Subsequent to January 1, 2004, the Bank is on a specific charge-off method for federal tax purposes.

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## 7. EMPLOYEE BENEFITS

## a) Pension Plan and Supplemental Executive Retirement Plan

The Bank maintains a noncontributory pension plan through the New York State Bankers Association Retirement System covering all eligible employees. The Bank uses a September 30 measurement date for this plan.

During 2001, the Bank adopted the Bridgehampton National Bank Supplemental Executive Retirement Plan (“SERP”). The SERP provides benefits to certain employees, as recommended by the Compensation Committee of the Board of Directors and approved by the full Board of Directors, whose benefits under the pension plan are limited by the applicable provisions of the Internal Revenue Code. The benefit under the SERP is equal to the additional amount the employee would be entitled to under the Pension Plan and the 401(k) Plan in the absence of such Internal Revenue Code limitations. The assets of the SERP are held in a rabbi trust to maintain the tax-deferred status of the individuals in the plan. As a result, the assets of the trust are reflected on the Consolidated Statements of Condition of the Company. The effective date of the SERP was January 1, 2001. SERP expense was \$148,000, \$208,000, and \$149,000 in 2006, 2005 and 2004, respectively. During 2006, a payout from the SERP of approximately \$105,000 was made pursuant to a severance agreement with the former Chief Operating Officer.

The following table sets forth the plans’ changes in obligations and funded status projected as of September 30, 2006 and 2005 (measurement dates).

| At December 31,<br>(In thousands)               | Pension Benefits |          | SERP Benefits |            |
|---|------------------|----------|---------------|------------|
|   | 2006             | 2005     | 2006          | 2005       |
| <b>Change in benefit obligation</b>             |                  |          |               |            |
| Benefit obligation at beginning of year         | \$ 4,631         | \$ 3,776 | \$ 1,181      | \$ 1,453   |
| Service cost                                    | 424              | 317      | 65            | 87         |
| Expenses  | (43)             | (40)     | -             | -          |
| Interest cost                                   | 252              | 223      | 55            | 71         |
| Benefits paid                                   | (152)            | (130)    | (105)         | -          |
| Assumption changes and other                    | (169)            | 485      | (77)          | (430)      |
| Benefit obligation at end of year               | \$ 4,943         | \$ 4,631 | \$ 1,119      | \$ 1,181   |
| <b>Change in plan assets, at fair value</b>     |                  |          |               |            |
| Plan assets at beginning of year                | \$ 4,034         | \$ 3,759 | -             | -          |
| Actual return on plan assets                    | 500              | 445      | -             | -          |
| Employer contribution                           | 666              | -        | -             | -          |
| Benefit paid                                    | (152)            | (130)    | -             | -          |
| Expenses  | (43)             | (40)     | -             | -          |
| Plan assets at end of year                      | \$ 5,005         | \$ 4,034 | -             | -          |
| <b>Funded status (plan assets less benefit)</b> | \$ 916           | \$ (596) | \$ (852)      | \$ (1,181) |

|   |    |            |    |       |    |              |          |
|---|----|------------|----|-------|----|--------------|----------|
| <b>obligations)</b>                       |    |            |    |       |    |              |          |
| Unrecognized net actuarial loss/(gain)    | -  | 1,107      | -  | 78    |    |              |          |
| Unrecognized prior service cost           | -  | 137        | -  | -     |    |              |          |
| Unrecognized transition (asset) liability | -  | (3)        | -  | 399   |    |              |          |
| Minimum additional pension liability      | -  | -          | -  | (147) |    |              |          |
| Prepaid benefit (accrued) cost            | \$ | <b>916</b> | \$ | 645   | \$ | <b>(852)</b> | \$ (851) |

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Prior to adoption of SFAS 158, amount recognized in the balance sheet at December 31, 2005 consist of:

|   | Pension<br>Benefits<br>2005 | SERP<br>Benefits<br>2005 |
|---|-----------------------------|--------------------------|
| At December 31,<br>(In thousands)       |                             |                          |
| Prepaid benefit cost                    | \$ 645                      | \$ -                     |
| Accrued benefit cost                    | -                           | (704)                    |
| Minimum additional pension<br>liability | -                           | (147)                    |
| Other                                   | -                           | -                        |
| Net amount recognized                   | \$ 645                      | \$ (851)                 |

Amounts recognized in accumulated other comprehensive income at December 31, 2006 consist of:

|   | Pension<br>Benefits<br>2006 | SERP<br>Benefits<br>2006 |
|---|-----------------------------|--------------------------|
| At December 31,<br>(In thousands)       |                             |                          |
| Net loss                                | \$ 725                      | \$ -                     |
| Prior service cost                      | 128                         | -                        |
| Net transition obligation               | -                           | 371                      |
| Minimum additional pension<br>liability | -                           | (147)                    |
| Net amount recognized                   | \$ 853                      | \$ 224                   |

The accumulated benefit obligation was \$3,717,000 and \$945,000 for the pension plan and the SERP, respectively, as of December 31, 2006. As of December 31, 2005, the accumulated benefit obligation was \$3,463,000 and \$851,000 for the pension plan and the SERP, respectively.

| At December 31,<br>(In thousands)   | Pension Benefits |        |        | SERP Benefits |        |        |
|---|------------------|--------|--------|---------------|--------|--------|
|   | 2006             | 2005   | 2004   | 2006          | 2005   | 2004   |
| <b>Components of net periodic<br/>benefit cost and other<br/>amounts recognized in<br/>Other Comprehensive<br/>Income</b> |                  |        |        |               |        |        |
| Service cost  | \$ 424           | \$ 317 | \$ 277 | \$ 65         | \$ 87  | \$ 63  |
| Interest cost   | 252              | 223    | 200    | 55            | 71     | 52     |
| Expected return on plan assets  | (327)            | (296)  | (208)  | -             | -      | -      |
| Amortization of net loss  | 40               | 25     | 25     | -             | 22     | 6      |
| Amortization of unrecognized<br>prior service cost  | 9                | 10     | 9      | -             | -      | -      |
| Amortization of unrecognized<br>transition (asset) obligation   | (3)              | (9)    | (8)    | 28            | 28     | 28     |
| Net periodic benefit cost   | \$ 395           | \$ 270 | \$ 295 | \$ 148        | \$ 208 | \$ 149 |

The estimated net loss and prior service costs for the defined benefit pension plan that will be amortized from accumulated other comprehensive income into net periodic benefit cost over the next fiscal year are \$14,000 and \$9,000. The estimated unrecognized net transition obligation for the SERP that will be amortized from accumulated other comprehensive income into net periodic benefit cost over the next fiscal year is \$28,000.

Contributions to the pension plan were \$665,900 while no contributions were made to the SERP for the year ended December 31, 2006. The Company is not required to contribute to the pension plan or SERP in 2007.

The following benefit payments, which reflect expected future service, as appropriate are expected to be paid as follows:

| Year<br>(In thousands) | Pension and SERP<br>Payments |
|------------------------|------------------------------|
| 2007                   | \$ 136                       |
| 2008                   | 136                          |
| 2009                   | 135                          |
| 2010                   | 1,397                        |
| 2011                   | 191                          |
| 2012-2016              | 930                          |

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The Company's pension plan weighted-average asset allocations at September 30, 2006 and 2005 by asset category are as follows:

| Plan Assets at<br>September 30,<br>Asset Category: | 2006          | 2005   |
|--|---------------|--------|
| Equity Securities                                  | <b>59.8%</b>  | 58.8%  |
| Debt Securities                                    | <b>39.9</b>   | 41.2   |
| Other  | <b>0.3</b>    | -      |
| Total  | <b>100.0%</b> | 100.0% |

## Investment Policies

The New York State Bankers Retirement System (the "System") was established in 1938 to provide for the payment of benefits to employees of participating banks. The System is overseen by a Board of Trustees ("Trustees"), who meet quarterly, and set the investment policy guidelines.

The System utilizes two investment management firms (which will be referred to as "Firm I" and "Firm II"). Firm I is investing approximately 68% of the portfolio and Firm II is investing approximately 32% of the portfolio. The System's investment objective is to exceed the investment benchmarks in each asset category. Each firm operates under a separate written investment policy approved by the Trustees and designed to achieve an allocation approximating 60% invested in Equity Securities and 40% invested in Debt Securities.

Each Firm reports at least quarterly to the investment committee of the System and semi-annually to the Trustees.

**Equities:** The target allocation percentage for equity securities is 60% but may vary from 50%-70% at the investment manager's discretion.

Firm I is employed for its expertise as a Value Manager. It is allowed to invest a certain amount of the equity portfolio under its management in international securities and to hedge said international securities so as to protect against currency devaluations.

The equities managed by Firm II are in a separately managed Large Cap Core Equity Fund. The portfolio is permitted to invest in a diversified range of securities in the United States ("US") equity markets. Although the portfolio holds primarily common stocks, from time to time the portfolio may invest in other types of investments on an opportunistic basis.

**Fixed Income:** For both investment portfolios, the target allocation percentage for debt securities is 40%, but may vary from 30% to 50% at the investment manager's discretion.

The Fixed Income Portfolio managed by Firm I operates with guidelines relating to types of debt securities, quality ratings, maturities, and maximum single and sector allocations.

The portfolio may trade foreign currencies in both spot and forward markets to affect securities transactions and to hedge underlying asset positions. The purchase and sale of futures and options on futures on foreign currencies and on foreign and domestic bonds, bond indices and short-term securities is permitted; however, purchases may not be used to leverage the portfolio. Currency transactions may only be used to hedge 0-100% of currency exposure of foreign securities.



The Fixed Income managed by Firm II is a Core Bond Fixed Income Fund. The portfolio investments are limited to US Dollar denominated, fixed income securities and selective derivatives designed to have similar attributes of such fixed income securities. The term “fixed income security” is defined to include instruments with fixed, floating, variable, adjustable, auction-rate, zero, or other coupon features.

#### Expected Long-Term Rate-of-Return

The expected long-term rate-of-return on plan assets reflects long-term earnings expectations on existing plan assets and those contributions expected to be received during the current plan year. In estimating that rate, appropriate consideration was given to historical returns earned by plan assets in the fund and the rates of return expected to be available for reinvestment. Average rates of return over the past 1, 3, 5 and 10-year periods were determined and subsequently adjusted to reflect current capital market assumptions and changes in investment allocations.

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| At December 31,<br><b>Weighted Average<br/>Assumptions Used to<br/>Determine Benefit<br/>Obligations</b> | Pension Benefits |       |       | SERP Benefits |       |       |
|--|------------------|-------|-------|---------------|-------|-------|
|  | 2006             | 2005  | 2004  | 2006          | 2005  | 2004  |
| Discount rate  | 5.75%            | 5.50% | 6.00% | 4.69%         | 4.68% | 4.90% |
| Rate of compensation increase  | 4.50             | 4.50  | 4.00  | 5.00          | 5.00  | 4.00  |
| <b>Weighted Average<br/>Assumptions Used to<br/>Determine Net Periodic<br/>Benefit Cost (Income)</b>     |                  |       |       |               |       |       |
| Discount rate  | 5.50%            | 6.00% | 6.00% | 4.73%         | 4.90% | 5.14% |
| Rate of compensation increase  | 4.50             | 4.00  | 4.00  | 4.00          | 4.00  | 4.00  |
| Expected long-term rate of return  | 8.00             | 8.00  | 8.00  | -             | -     | -     |

## b) 401(k) Plan

A savings plan is maintained under Section 401(k) of the Internal Revenue Code and covers substantially all current employees. Newly hired employees can elect to participate in the savings plan after completing six months of service. Under the provisions of the savings plan, employee contributions are partially matched by the Bank with cash contributions. Participants can invest their account balances into several investment alternatives. The savings plan does not allow for investment in the Company's common stock. During the years ended December 31, 2006, 2005 and 2004 the Bank made cash contributions of \$128,000, \$114,000, and \$110,000, respectively.

## c) Equity Incentive Plan

During 2006, the Bridge Bancorp, Inc. Equity Incentive Plan (the "Plan") was approved by the shareholders to provide for the grant of options to purchase shares of common stock of the Company and for the award of shares of common stock as a bonus up to a total of 620,000. The plan supersedes the Bridge Bancorp, Inc. Equity Incentive Plan that was approved in 1996 and amended in 2001. Of the total 620,000 shares of common stock approved for issuance under the Plan, at December 31, 2006, 540,030 shares remain available for issuance.

The Compensation Committee of the Board of Directors determines options awarded under the Plan. The Company accounts for this Plan under SFAS 123(R).

The fair value of each option granted is estimated on the date of the grant using the Black-Scholes option-pricing model with the following weighted average assumptions used for the following years:

| For the Year Ended      | 2006  | 2005  | 2004  |
|-------------------------|-------|-------|-------|
| Risk free interest rate | 4.70% | 3.66% | 3.02% |
| Expected dividend yield | 3.67  | 3.76  | 2.75  |
| Expected volatility     | 20.2  | 21.3  | 23.5  |



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A summary of the status of the Company's stock options as of December 31, 2006 follows.

|                                   | Number<br>of<br>Options | Weighted<br>Average<br>Exercise<br>Price | Weighted<br>Average<br>Remaining<br>Contractual<br>Life | Aggregate<br>Intrinsic<br>Value |
|-----------------------------------|-------------------------|--|---|---------------------------------|
| Outstanding,<br>December 31, 2005 | 83,107                  | \$ 16.88                                 |   |                                 |
| Granted                           | 63,983                  | \$ 25.25                                 |   |                                 |
| Exercised                         | (16,078)                | \$ 12.82                                 |   |                                 |
| Forfeited                         | (2,767)                 | \$ 25.68                                 |   |                                 |
| Outstanding,<br>December 31, 2006 | 128,245                 | \$ 21.37                                 | 7.38<br>years   | \$ 444,835                      |
| Exercisable,<br>December 31, 2006 | 74,059                  | \$ 18.49                                 | 5.78<br>years   | \$ 444,835                      |
|                                   |                         |  |   |                                 |
|                                   | Number<br>of            |  |   |                                 |
| Range of Exercise<br>Prices       | Shares                  | Price                                    |   |                                 |
|                                   | 9,900                   | \$ 12.53                                 |   |                                 |
|                                   | 19,683                  | \$ 13.17-14.67                           |   |                                 |
|                                   | 17,100                  | \$ 15.47                                 |   |                                 |
|                                   | 11,471                  | \$ 24.00                                 |   |                                 |
|                                   | 63,983                  | \$ 25.25                                 |   |                                 |
|                                   | 6,108                   | \$ 26.00-\$30.60                         |   |                                 |

The aggregate intrinsic value for options outstanding and exercisable as of December 31, 2006 is \$444,835. The figure is the same because the options that are unvested are antidilutive.

A summary of activity related to the stock option plan follows.

| December 31,<br>(Dollars in thousands,<br>except for per share data) | 2006    | 2005    | 2004    |
|--|---------|---------|---------|
| Intrinsic value of options<br>exercised                              | \$ 180  | \$ 289  | \$ 549  |
| Cash received from<br>option exercised                               | 49      | 216     | 203     |
| Tax benefit realized from<br>option exercises                        | 21      | 16      | 21      |
| Weighted average fair<br>value of options granted                    | \$ 4.45 | \$ 4.39 | \$ 4.12 |

A summary of the status of the Company's unvested restricted stock shares as of December 31, 2006 follows.

Weighted

|                                | Shares         | Average<br>Grant-Date<br>Fair Value |
|--------------------------------|----------------|-------------------------------------|
| Unvested,<br>December 31, 2005 | <b>7,214</b>   | <b>\$ 23.44</b>                     |
| Granted                        | <b>15,987</b>  | <b>\$ 25.25</b>                     |
| Vested                         | <b>(3,491)</b> | <b>\$ 20.10</b>                     |
| Forfeited                      | <b>(12)</b>    | <b>\$ 30.60</b>                     |
| Unvested,<br>December 31, 2006 | <b>19,698</b>  | <b>\$ 25.50</b>                     |

During the year ended December 31, 2006 the Company granted 63,983 options to purchase shares of common stock of the Company. These options vest ratably over five years beginning December 31, 2006 and have a 10 year contractual term. Compensation expense attributable to these options was \$68,000 for the year ended December 31, 2006. As of December 31, 2006, there was \$217,000 of total unrecognized compensation costs related to nonvested stock options granted under the Plan.

The Company's Equity Incentive Plan also provides for issuance of restricted stock awards. During the year ended December 31, 2006 the Company granted restricted stock awards of 15,987 shares. These awards cliff vest as of December 31, 2008. During the year ended December 31, 2005, the Company granted restricted stock awards of 1,239 shares. These awards vest over three years in

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January of each year following the date of the award. Such shares are subject to restrictions based on continued service as employees of the Company or employees of subsidiaries of the Company. Compensation expense attributable to these awards was approximately \$51,000, \$65,000 and \$73,000 for the years ended December 31, 2006, 2005, and 2004, respectively. The related tax benefit recorded in 2006, 2005 and 2004 was \$21,000, \$22,000 and \$26,000, respectively. The total fair value of shares vested during the years ended December 31, 2006, 2005 and 2004 was \$85,000, \$188,000 and \$186,000, respectively. As of December 31, 2006, there was \$411,000 of total unrecognized compensation costs related to nonvested restricted stock awards granted under the Plan.

## 8. EARNINGS PER SHARE

The following is a reconciliation of earnings per share for December 31, 2006, 2005 and 2004. All share and per share amounts have been adjusted for the three-for-two stock split effective July 9, 2004.

| For the Year Ended December 31,<br>(In thousands, except per share data) | 2006     | 2005     | 2004      |
|--|----------|----------|-----------|
| Net income   | \$ 8,168 | \$ 9,623 | \$ 10,377 |
| Common equivalent shares:  |          |          |           |
| Weighted average common shares outstanding                               | 6,139    | 6,241    | 6,255     |
| Weighted average common equivalent shares                                | 20       | 34       | 75        |
| Weighted average common and common equivalent shares                     | 6,159    | 6,275    | 6,330     |
| Basic earnings per share   | \$ 1.33  | \$ 1.54  | \$ 1.66   |
| Diluted earnings per share   | \$ 1.33  | \$ 1.53  | \$ 1.64   |

There are approximately 70,091 options outstanding at December 31, 2006 that were not included in the computation of diluted earnings per share because the options' exercise prices were greater than the average market price of common stock and were, therefore, antidilutive.

## 9. COMMITMENTS AND CONTINGENCIES AND OTHER MATTERS

In the normal course of business, there are various outstanding commitments and contingent liabilities, such as claims and legal actions, minimum annual rental payments under non-cancelable operating leases, guarantees and commitments to extend credit, which are not reflected in the accompanying consolidated financial statements. No material losses are anticipated as a result of these actions or claims.

## a) Leases

The Company is obligated to make minimum annual rental payments under non-cancelable operating leases on its premises. Projected minimum rentals under existing leases are as follows:

| December 31,<br>2006<br>(In thousands) |        |
|--|--------|
| 2007                                   | \$ 692 |
| 2008                                   | 628    |
| 2009                                   | 619    |

|                          |          |
|--------------------------|----------|
| 2010                     | 435      |
| 2011                     | 307      |
| Thereafter               | 1,299    |
| Total minimum<br>rentals | \$ 3,980 |

Certain leases contain renewal options and rent escalation clauses. In addition, certain leases provide for additional payments based upon real estate taxes, interest and other charges. Rental expenses under these leases for the years ended December 31, 2006, 2005 and 2004 approximated \$516,000, \$456,000, and \$501,000, respectively.

b) Loan commitments

Some financial instruments, such as loan commitments, credit lines, letters of credit, and overdraft protection, are issued to meet customer financing needs. These are agreements to provide credit or to support the credit of others, as long as conditions established in the contract are met, and usually have expiration dates. Commitments may expire without being used. Off-balance-sheet risk to credit loss exists up to the face amount of these instruments, although material losses are not anticipated. The same credit policies are used to make such commitments as are used for loans, often including obtaining collateral at exercise of the commitment.

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The following represents commitments outstanding:

| December 31,<br>(In thousands)                 | 2006       | 2005      |
|--|------------|-----------|
| Standby letters of credit                      | \$ 2,736   | \$ 1,955  |
| Loan commitments<br>outstanding <sup>(1)</sup> | 16,718     | 11,839    |
| Unused equity lines                            | 49,553     | 42,432    |
| Unused construction lines                      | 4,627      | 1,324     |
| Unused lines of credit                         | 31,220     | 23,154    |
| Unused overdraft lines                         | 13,560     | 12,268    |
| Total commitments<br>outstanding               | \$ 118,414 | \$ 92,972 |

(1) Of the \$16,718,000 of loan commitments outstanding, \$1,710,000 are fixed rate commitments and \$15,008,000 are variable rate commitments.

## c) Other

During 2006, the Bank was required to maintain certain cash balances with the Federal Reserve Bank of New York for reserve and clearing requirements. These balances averaged \$807,000 in 2006.

During 2006, 2005 and 2004, the Bank maintained an overnight line of credit with the Federal Home Loan Bank of New York ("FHLB"). The Bank has the ability to borrow against its unencumbered residential mortgages and investment securities owned by the Bank. At December 31, 2006, the Bank had aggregate lines of credit of \$52,000,000 with unaffiliated correspondent banks to provide short-term credit for liquidity requirements. Of these aggregate lines of credit, \$32,000,000 is available on an unsecured basis. As of December 31, 2006, the Bank had \$18,600,000 in such borrowings outstanding.

In March 2001, the Bank entered into a Master Repurchase Agreement with the FHLB whereby the FHLB agrees to purchase securities from the Bank, upon the Bank's request, with the simultaneous agreement to sell the same or similar securities back to the Bank at a future date. Securities are limited, under the agreement, to government securities, securities issued, guaranteed or collateralized by any agency or instrumentality of the U.S. Government or any government sponsored enterprise, and non-agency AA and AAA rated mortgage-backed securities. At December 31, 2006, there was \$52,500,100 available for transactions under this agreement. There were no balances outstanding at year-end.

## 10. ESTIMATED FAIR VALUE OF FINANCIAL INSTRUMENTS

Fair value estimates are made at a specific point in time and are based on existing on-and off-balance sheet financial instruments. Such estimates are generally subjective in nature and dependent upon a number of significant assumptions associated with each financial instrument or group of financial instruments, including estimates of discount rates, risks associated with specific financial instruments, estimates of future cash flows, and relevant available market information. Changes in assumptions could significantly affect the estimates. In addition, fair value



estimates do not reflect the value of anticipated future business, premiums or discounts that could result from offering for sale at one time the Bank's entire holdings of a particular financial instrument, or the tax consequences of realizing gains or losses on the sale of financial instruments.

The Company used the following method and assumptions in estimating the fair value of its financial instruments:

**Cash and Due from Banks and Federal Funds Sold:** Carrying amounts approximate fair value, since these instruments are either payable on demand or have short-term maturities.

**Securities Available for Sale and Held to Maturity:** The estimated fair values are based on independent dealer quotations and quoted market prices.

**Loans:** The estimated fair values of real estate mortgage loans and other loans receivable are based on discounted cash flow calculations that use available market benchmarks when establishing discount factors for the types of loans. All nonaccrual loans are carried at their current fair value. Exceptions may be made for adjustable rate loans (with resets of one year or less), which would be discounted straight to their rate index plus or minus an appropriate spread.

**The Bank's Deposits:** The estimated fair value of certificates of deposits are based on discounted cash flow calculations that use a replacement cost of funds approach to establishing discount rates for certificates of deposits maturities. Stated value is fair value for all other deposits.

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Wholesale Funding: The estimated fair value of borrowed funds and wholesale certificates of deposit are based on discounted cash flow calculations that use a replacement cost of funds approach to establishing discount rates for funding maturities.

Accrued Interest Receivable and Payable: For these short-term instruments, the carrying amount is a reasonable estimate of the fair value.

Off-Balance-Sheet Liabilities: The fair value of off-balance-sheet commitments to extend credit is estimated using fees currently charged to enter into similar agreements.

The estimated fair values and recorded carrying values of the Bank's financial instruments are as follows:

| December 31,<br>(In thousands)           | 2006               |               | 2005               |               |
|--|--------------------|---------------|--------------------|---------------|
|  | Carrying<br>Amount | Fair<br>Value | Carrying<br>Amount | Fair<br>Value |
| <b>Financial Assets:</b>                 |                    |               |                    |               |
| Cash and due from<br>banks               | \$ 13,231          | \$ 13,231     | \$ 15,649          | \$ 15,649     |
| Interest bearing<br>deposits with banks  | 32                 | 32            | 26                 | 26            |
| Securities available<br>for sale         | 202,590            | 202,590       | 182,801            | 182,801       |
| Securities restricted                    | 878                | 878           | 1,377              | 1,377         |
| Securities held to<br>maturity           | 9,444              | 9,442         | 10,012             | 9,989         |
| Loans                                    | 323,485            | 318,697       | 299,881            | 305,096       |
| Accrued interest<br>receivable           | 2,692              | 2,692         | 2,624              | 2,624         |
| <b>Financial Liabilities:</b>            |                    |               |                    |               |
| Demand and other<br>deposits             | 504,412            | 504,365       | 468,025            | 467,544       |
| Overnight<br>borrowings                  | 18,600             | 18,600        | 14,500             | 14,500        |
| Accrued interest<br>payable              | 855                | 855           | 328                | 328           |
| <b>Off-Balance-Sheet<br/>Liabilities</b> |                    |               |                    |               |
| Commitments to<br>extend credit          | 16,718             | -             | 11,839             | -             |

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## 11. REGULATORY MATTERS

The Company and the Bank are subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can result in certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Company's and the Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company and the Bank must meet specific capital guidelines that involve quantitative measures of the Company's and Bank's assets, liabilities, and certain off-balance sheet items calculated under regulatory accounting practices. The Company's and Bank's capital amounts and classification also are subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Company and the Bank to maintain minimum amounts and ratios (set forth in the following table) of total and Tier 1 capital (as defined in the regulations) to risk weighted assets (as defined), and of Tier 1 capital (as defined) to average assets (as defined). Management believes, as of December 31, 2006, that the Company and the Bank meet all capital adequacy requirements with which it must comply.

As of December 31, 2006, the most recent notification from the Federal Deposit Insurance Corporation categorized the Bank as "well capitalized" under the regulatory framework for prompt corrective action. To be categorized as "well capitalized," the Bank must maintain minimum total risk-based, Tier 1 risk-based and Tier 1 leverage ratios as set forth in the table. Since that notification, there are no conditions or events that management believes have changed the institution's category.

The Company and the Bank's actual capital amounts and ratios are presented in the following table:

|  |    | <b>Bridge Bancorp,<br/>Inc. (Consolidated)<br/>As of December 31,<br/>(Dollars in<br/>thousands)</b> |              |  |               |  |              |            |
|--|----|--|--------------|--|---------------|--|--------------|------------|
|  |    | <b>2006</b>  |              |  |               | <b>To Be Well<br/>Capitalized Under<br/>Prompt Corrective<br/>Action Provision</b>   |              |            |
|  |    | <b>Actual</b>  |              | <b>For Capital<br/>Adequacy<br/>Purposes</b> |               |  |              |            |
|  |    | <b>Amount</b>  | <b>Ratio</b> | <b>Amount</b>                                | <b>Ratio</b>  | <b>Amount</b>  | <b>Ratio</b> |            |
| Total Capital (to risk weighted assets)                  | \$ | <b>50,312</b>  | <b>12.6%</b> | \$   | <b>32,032</b> | <b>&gt;8.0%</b>  | <b>n/a</b>   | <b>n/a</b> |
| Tier 1 Capital (to risk weighted assets)                 |    | <b>47,800</b>  | <b>11.9%</b> |  | <b>16,016</b> | <b>&gt;4.0%</b>  | <b>n/a</b>   | <b>n/a</b> |
| Tier 1 Capital (to average assets)                       |    | <b>47,800</b>  | <b>8.3%</b>  |  | <b>23,075</b> | <b>&gt;4.0%</b>  | <b>n/a</b>   | <b>n/a</b> |
| <b>As of December 31,<br/>(Dollars in<br/>thousands)</b> |    | <b>2005</b>  |              |  |               |  |              |            |
|  |    | <b>Actual</b>  |              | <b>For Capital<br/>Adequacy<br/>Purposes</b> |               | <b>To Be Well<br/>Capitalized Under<br/>Prompt Corrective<br/>Actions Provisions</b> |              |            |
|  |    | <b>Amount</b>  | <b>Ratio</b> | <b>Amount</b>                                | <b>Ratio</b>  | <b>Amount</b>  | <b>Ratio</b> |            |

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|  |           |       |           |       |     |     |
|--|-----------|-------|-----------|-------|-----|-----|
| Total Capital (to risk weighted assets)  | \$ 51,410 | 14.0% | \$ 29,399 | >8.0% | n/a | n/a |
| Tier 1 Capital (to risk weighted assets) | 49,115    | 13.4% | 14,699    | >4.0% | n/a | n/a |
| Tier 1 Capital (to average assets)       | 49,115    | 9.1%  | 21,517    | >4.0% | n/a | n/a |

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**Bridgehampton  
National Bank  
As of December 31,  
(Dollars in  
thousands)**

2006

|  | Actual    |       | For Capital Adequacy Purposes |       | To Be Well Capitalized Under Prompt Corrective Action Provisions |        |
|--|-----------|-------|-------------------------------|-------|--|--------|
|  | Amount    | Ratio | Amount                        | Ratio | Amount   | Ratio  |
| Total Capital (to risk weighted assets)  | \$ 50,152 | 12.5% | \$ 32,019                     | >8.0% | \$ 40,024  | >10.0% |
| Tier 1 Capital (to risk weighted assets) | 47,640    | 11.9% | 16,010                        | >4.0% | 24,015   | > 6.0% |
| Tier 1 Capital (to average assets)       | 47,640    | 8.3%  | 23,073                        | >4.0% | 28,841   | > 5.0% |

As of December 31,  
(Dollars in  
thousands)

2005

|  | Actual    |       | For Capital Adequacy Purposes |       | To Be Well Capitalized Under Prompt Corrective Action Provisions |        |
|--|-----------|-------|-------------------------------|-------|--|--------|
|  | Amount    | Ratio | Amount                        | Ratio | Amount   | Ratio  |
| Total Capital (to risk weighted assets)  | \$ 51,234 | 14.0% | \$ 29,392                     | >8.0% | \$ 35,805  | >10.0% |
| Tier 1 Capital (to risk weighted assets) | 48,851    | 13.3% | 14,696                        | >4.0% | 21,483   | > 6.0% |
| Tier 1 Capital (to average assets)       | 48,851    | 9.0%  | 21,658                        | >4.0% | 27,073   | > 5.0% |

Under its current rules, the Federal Deposit Insurance Corporation does not impose a deposit insurance assessment on financial institutions, such as the Bank, that are, among other criteria, well-capitalized. On November 2, 2006, the Federal Deposit Insurance Corporation adopted final regulations establishing a risk-based assessment system that will enable the Federal Deposit Insurance Corporation to more closely tie each financial institution's premiums to the risk it poses to the deposit insurance fund. Under the new risk-based assessment system, which becomes effective in the beginning of 2007, the Federal Deposit Insurance Corporation will evaluate the risk of each financial institution based on three primary sources of information: (1) its supervisory rating, (2) its financial ratios, and (3) its long-term debt issuer rating, if the institution has one. The new rates for nearly all of the financial institution industry will vary between five and seven cents for every \$100 of domestic deposits. Once effective, this increased assessment will reduce our income.

## 12. BRIDGE BANCORP, INC. (PARENT COMPANY ONLY)

## Condensed Statements of Financial Condition

| December 31,  | 2006             | 2005             |
|---|------------------|------------------|
| (In thousands, except share data)                     |                  |                  |
| <b>ASSETS</b>   |                  |                  |
| Cash and cash equivalents                             | \$ 2             | \$ 80            |
| Dividend receivable                                   | 1,408            | 1,441            |
| Other assets  | 157              | 82               |
| Investment in the Bank                                | 45,379           | 46,489           |
| <b>Total Assets</b>                                   | <b>\$ 46,946</b> | <b>\$ 48,092</b> |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>           |                  |                  |
| <b>EQUITY</b>   |                  |                  |
| Liabilities   |                  |                  |
| Dividends payable                                     | \$ 1,394         | \$ 1,428         |
| Other liabilities                                     | 13               | 13               |
| <b>Total Liabilities</b>                              | <b>1,407</b>     | <b>1,441</b>     |
| Stockholders' Equity                                  | 53,715           | 50,936           |
| Treasury stock at cost, 323,728 and 179,767 shares at |                  |                  |
| December 31, 2006 and 2005, respectively              | (8,176)          | (4,285)          |
| <b>Total Stockholders' Equity</b>                     | <b>45,539</b>    | <b>46,651</b>    |
| <b>Total Liabilities and Stockholders' Equity</b>     | <b>\$ 46,946</b> | <b>\$ 48,092</b> |

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## Condensed Statements of Income

| Year Ended December 31,<br>(In thousands)                                   | 2006     | 2005     | 2004      |
|---|----------|----------|-----------|
| Dividend income from the Bank   | \$ 9,482 | \$ 6,390 | \$ 5,104  |
| Other operating expenses  | 1        | 1        | -         |
| Income before income taxes and equity in undistributed earnings of the Bank | 9,481    | 6,389    | 5,104     |
| Income tax provision  | -        | -        | -         |
| Income before equity in undistributed earnings of the Bank                  | 9,481    | 6,389    | 5,104     |
| Equity in (overdistributed) undistributed earnings of the Bank              | (1,313)  | 3,234    | 5,273     |
| Net income  | \$ 8,168 | \$ 9,623 | \$ 10,377 |

## Condensed Statements of Cash Flows

| Year Ended December 31,<br>(In thousands)   | 2006     | 2005     | 2004      |
|---|----------|----------|-----------|
| Operating Activities:   |          |          |           |
| Net income  | \$ 8,168 | \$ 9,623 | \$ 10,377 |
| Adjustments to reconcile net income to net cash provided by operating activities: |          |          |           |
| Equity in overdistributed (undistributed) earnings of the Bank                    | 1,313    | (3,234)  | (5,273)   |
| Income tax benefit from exercise of employee stock options                        | 21       | 16       | 7         |
| Decrease in other assets  | 623      | 109      | 1,432     |
| (Decrease) increase in other liabilities  | (545)    | 11       | (5)       |
| Net cash provided by operating activities   | 9,580    | 6,525    | 6,538     |
| Cash flows used by financing activities:  |          |          |           |
| Net proceeds from issuance of common stock upon exercise of stock options         | 49       | 216      | 203       |
| Payment for the purchase of treasury stock  | (4,039)  | (2,134)  | (611)     |
| Dividends paid  | (5,668)  | (5,551)  | (5,790)   |
| Net cash used by financing activities   | (9,658)  | (7,469)  | (6,198)   |
| Net increase in cash and cash equivalents   | (78)     | (944)    | 340       |
| Cash and cash equivalents at beginning of year                                    | 80       | 1,024    | 684       |
| Cash and cash equivalents at end of year  | \$ 2     | \$ 80    | \$ 1,024  |

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## 13. QUARTERLY FINANCIAL DATA (Unaudited)

## Selected Consolidated Quarterly Financial Data

| <b>2006 Quarter Ended,</b><br>(In thousands, except per share amounts) | <b>March 31,</b> | <b>June 30,</b> | <b>September 30,</b> | <b>December 31,</b> |
|--|------------------|-----------------|----------------------|---------------------|
| Interest income  | \$ 7,555         | \$ 7,674        | \$ 8,281             | \$ 8,520            |
| Interest expense   | 1,576            | 1,882           | 2,267                | 2,612               |
| Net interest income  | 5,979            | 5,792           | 6,014                | 5,908               |
| Provision for loan losses  | -                | -               | -                    | 85                  |
| Net interest income after provision for loan losses                    | 5,979            | 5,792           | 6,014                | 5,823               |
| Other income   | 739              | 1,260           | 1,200                | 1,214               |
| Other expenses   | 3,769            | 4,073           | 4,137                | 4,023               |
| Income before income taxes   | 2,949            | 2,979           | 3,077                | 3,014               |
| Provision for income taxes   | 1,010            | 941             | 925                  | 975                 |
| Net income   | \$ 1,939         | \$ 2,038        | \$ 2,152             | \$ 2,039            |
| Basic earnings per share   | \$ 0.31          | \$ 0.33         | \$ 0.35              | \$ 0.34             |
| Diluted earnings per share   | \$ 0.31          | \$ 0.33         | \$ 0.35              | \$ 0.34             |
| <b>2005 Quarter Ended,</b><br>(In thousands, except per share amounts) | <b>March 31,</b> | <b>June 30,</b> | <b>September 30,</b> | <b>December 31,</b> |
| Interest income  | \$ 6,912         | \$ 7,004        | \$ 7,373             | \$ 7,424            |
| Interest expense   | 916              | 1,033           | 1,118                | 1,252               |
| Net interest income  | 5,996            | 5,971           | 6,255                | 6,172               |
| Provision for loan losses  | -                | 150             | 150                  | -                   |
| Net interest income after provision for loan losses                    | 5,996            | 5,821           | 6,105                | 6,172               |
| Other income   | 1,021            | 1,339           | 1,391                | 1,354               |
| Other expenses   | 3,568            | 3,645           | 3,771                | 3,663               |
| Income before income taxes   | 3,449            | 3,515           | 3,725                | 3,863               |
| Provision for income taxes   | 1,199            | 1,190           | 1,251                | 1,289               |
| Net income   | \$ 2,250         | \$ 2,325        | \$ 2,474             | \$ 2,574            |
| Basic earnings per share   | \$ 0.36          | \$ 0.37         | \$ 0.40              | \$ 0.41             |
| Diluted earnings per share   | \$ 0.36          | \$ 0.37         | \$ 0.39              | \$ 0.41             |



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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Audit Committee  
Board of Directors  
Bridge Bancorp, Inc.  
Bridgehampton, New York

We have audited the accompanying balance sheets of Bridge Bancorp, Inc. as of December 31, 2006 and 2005, and the related statements of income, stockholders' equity and cash flows for each of the years in the three-year period ended December 31, 2006. We also have audited management's assessment, included in the accompanying Report By Management On Internal Control Over Financial Reporting, that Bridge Bancorp, Inc. maintained effective internal control over financial reporting as of December 31, 2006, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Bridge Bancorp, Inc.'s management is responsible for these financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on these financial statements, an opinion on management's assessment, and an opinion on the effectiveness of the company's internal control over financial reporting based on our audits.

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 audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audit of financial statements included 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, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Bridge Bancorp, Inc. as of December 31, 2006 and 2005, and the results of its operations and its cash flows for each of the years in the three-year period ended December 31, 2006 in conformity with U.S. generally accepted accounting principles. Also in our opinion, management's assessment that Bridge Bancorp, Inc. maintained effective internal control over financial reporting as of December 31, 2006, is fairly stated, in all material respects, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of

the Treadway Commission (COSO). Furthermore, in our opinion, Bridge Bancorp, Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2006, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

As discussed in Note 7 of the consolidated financial statements, Bridge Bancorp, Inc. changed its method of accounting for defined benefit pension and other postretirement plans as of December 31, 2006, in accordance with Financial Accounting Standards Board Statement No. 158, *Employers' Accounting for Defined Benefit and Other Postretirement Plans*.

/s/ Crowe Chizek and Company LLC  
Crowe Chizek and Company LLC

Livingston, New Jersey  
February 24, 2007  
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**Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure**

None.

**Item 9A. Controls and Procedures**

*Disclosure Controls and Procedures*

An evaluation was performed under the supervision and with the participation of the Company's management, including the Principal Executive Officer and Principal Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in Rule 13a-15(e) promulgated under the Securities and Exchange Act of 1934, as amended) as of December 31, 2006. Based on that evaluation, the Company's Principal Executive Officer and Principal Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective as of the end of the period covered by the annual report.

*Report By Management On Internal Control Over Financial Reporting*

Management of Bridge Bancorp, Inc. ("the Company") is responsible for establishing and maintaining an effective system of internal control over financial reporting. The Company's system of internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. There are inherent limitations in the effectiveness of any system of internal control over financial reporting, including the possibility of human error and circumvention or overriding of controls. Accordingly, even an effective system of internal control over financial reporting can provide only reasonable assurance with respect to financial statement preparation. Projections of any evaluation of effectiveness to future periods are subject to the risks that controls may become inadequate because of changes in conditions or that the degree of compliance with the policies or procedures may deteriorate.

Management assessed the Company's systems of internal control over financial reporting as of December 31, 2006. This assessment was based on criteria for effective internal control over financial reporting described in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this assessment, management believes that, as of December 31, 2006, the Company maintained effective internal control over financial reporting based on those criteria.

The Company's independent registered public accounting firm that audited the financial statements that are included in this annual report on Form 10-K, has issued an attestation report on management's assessment of the Company's internal control over financial reporting. The attestation report of Crowe Chizek and Company LLC appears on the previous page.

*Changes in Internal Control Over Financial Reporting*

There has been no change in the Company's internal control over financial reporting during the year that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

**Item 9B. Other Information**

None.

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**PART III**

**Item 10. Directors, Executive Officers and Corporate Governance**

“Item 1 - Election of Directors,” “Compliance with Section 16 (a) of the Exchange Act,” and “Code of Ethics” set forth in the Registrant’s Proxy Statement for the Annual Meeting of Shareholders to be held on April 27, 2007, are incorporated herein by reference.

**Item 11. Executive Compensation**

“Compensation of Directors,” “Compensation of Executive Officers,” “Report of the Compensation Committee on Executive Compensation,” “Compensation Committee Interlocks and Insider Participation,” and “Employment Contracts and Severance Agreements” set forth in the Registrant’s Proxy Statement for the Annual Meeting of Shareholders to be held on April 27, 2007, are incorporated herein by reference.

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

“Beneficial Ownership” and “Item 1 - Election of Directors”, set forth in the Registrant’s Proxy Statement for the Annual Meeting of Shareholders to be held on April 27, 2007, are incorporated herein by reference.

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

“Certain Relationships and Related Transactions, and Director Independence” set forth in the Registrant’s Proxy Statement for the Annual Meeting of Shareholders to be held on April 27, 2007, is incorporated herein by reference.

**Item 14. Principal Accountant Fees and Services**

“Item 2 - Ratification of the Appointment of Independent Auditors,” “Fees Paid to Crowe Chizek,” and “Policy on Audit Committee Pre-approval Of Audit and Non-audit Services of Independent Auditor” set forth in the Registrant’s Proxy Statement for the Annual Meeting of Shareholders to be held on April 27, 2007, is incorporated herein by reference.

**PART IV**

**Item 15. Exhibits and Financial Statement Schedules**

(a) The following Consolidated Financial Statements, including notes thereto, and financial schedules of the Company, required in response to this item are included in Part II, Item 8.

| 1. Financial Statements                                    | Page No. |
|--|----------|
| <u>Consolidated Statements of Condition</u>                | 24       |
| <u>Consolidated Statements of Income</u>                   | 25       |
| <u>Consolidated Statements of Stockholders’ Equity</u>     | 26       |
| <u>Consolidated Statements of Cash Flows</u>               | 27       |
| <u>Notes to Consolidated Financial Statements</u>          | 28       |
| <u>Report of Independent Registered Public Accountants</u> | 50       |
| <br>2. Financial Statement Schedules                       |          |

Financial Statement Schedules have been omitted because they are not applicable or the required information is shown in the Consolidated Financial Statements or Notes thereto under Item 8, "Financial Statements and Supplementary Data."

3. Exhibits.

See [Index of Exhibits](#) on page 54.



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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities and Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

BRIDGE BANCORP, INC.

Registrant

March 15, 2007

/s/ Thomas J. Tobin  
Thomas J. Tobin  
President and Chief Executive Officer

March 15, 2007

/s/ Janet T. Verneuille  
Janet T. Verneuille,  
Executive Vice President, Chief Financial  
Officer  
and Treasurer

Pursuant to the requirements of the Securities and Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

March 15, 2007

/s/ Raymond                   ,Director  
Wesnofske  
Raymond Wesnofske

March 15, 2007

/s/ Thomas J. Tobin   ,Director  
Thomas J. Tobin

March 15, 2007

/s/ Thomas E. Halsey   ,Director  
Thomas E. Halsey

March 15, 2007

/s/ Marcia Z. Hefter   ,Director  
Marcia Z. Hefter

March 15, 2007

/s/ R. Timothy Maran   ,Director  
R. Timothy Maran

March 15, 2007

/s/ Charles I. Massoud,Director  
Charles I. Massoud

March 15, 2007

/s/ Howard H. Nolan   ,Director

Howard H. Nolan

March 15, 2007

/s/ Dennis A. Suskind ,Director  
Dennis A. Suskind

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| <b>Exhibit Number</b> | <b>Description of Exhibit</b>   | <b>Exhibit</b> |
|-----------------------|---|----------------|
| 3.1                   | Certificate of Incorporation of the registrant (incorporated by reference to Registrant's amended Form 10, File No. 0-18546, filed October 15, 1990)                        | *              |
| 3.1(i)                | Certificate of Amendment of the Certificate of Incorporation of the Registrant (incorporated by reference to Registrant's Form 10, File No. 0-18546, filed August 13, 1999) | *              |
| 3.2                   | Revised By-laws of the Registrant (incorporated by reference to Registrant's Form 10-Q, File No. 0-18546, filed November 2, 2004)   | *              |
| 10.1                  | Employment Contract - Thomas J. Tobin (incorporated by reference to Registrant's Form 10-Q, File No. 0-18546, filed November 7, 2001)                                       | *              |
| 10.2                  | Employment Contract - Janet T. Verneuille (incorporated by reference to Registrant's Form 10-Q, File No. 0-18546, filed November 7, 2001)                                   | *              |
| 10.3                  | Employment Contract - Howard H. Nolan (incorporated by reference to Registrant's Form 10-Q, File No. 0-18546, filed November 7, 2006)                                       |                |
| 10.5                  | Equity Incentive Plan (incorporated by reference to Registrant's Form S-8, File No. 0-18546, filed August 14, 2006)   | *              |
| 23                    | <u>Accountants' Consent</u>   |                |
| 31.1                  | <u>Certification of Principal Executive Officer pursuant to Rule 13a-14(a)</u>  |                |
| 31.2                  | <u>Certification of Principal Financial Officer pursuant to Rule 13a-14(a)</u>  |                |
| 32.1                  | <u>Certification of Chief Executive Officer and Chief Financial Officer pursuant to Rule 13a-14(b) and U.S.C. Section 1350</u>  |                |

\* Denotes incorporated by reference.

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