LAKELAND BANCORP INC
Form 10-K
March 16, 2007

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-K

(MARK ONE)

[X] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE FISCAL YEAR ENDED DECEMBER 31, 2006.

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 or 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE TRANSITION PERIOD FROM _____ TO _____.

Commission file number:

33-27312

LAKELAND BANCORP, INC.

(Exact name of registrant as specified in its charter)

New Jersey	**22-2953275**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

250 Oak Ridge Road, Oak Ridge, New Jersey 07438
(Address of principal executive offices) (Zip code)

Registrant s telephone number, including area code: **(973)697-2000**

Securities registered pursuant to Section 12(b) of the Act: **None**

Securities registered pursuant to Section 12(g) of the Act:

Title of Each Class
Common Stock, no par value

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

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

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

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

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

Large accelerated filer ____ Accelerated filer _X_ Non-accelerated filer ____

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

As of June 30, 2006, the aggregate market value of the registrant s common stock held by non-affiliates of the registrant was approximately $283,000,000, based on the closing sale price as reported on the NASDAQ Global Select Market.

The number of shares outstanding of the registrant s Common Stock, as of February 1, 2007, was 22,057,964.

DOCUMENTS INCORPORATED BY REFERENCE:

Lakeland Bancorp, Inc s. Proxy Statement for its 2007 Annual Meeting of Shareholders (Part III).

LAKELAND BANCORP, INC.

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PART I

ITEM 1 - Business

GENERAL

Lakeland Bancorp, Inc. (the Company) is a bank holding company headquartered in Oak Ridge, New Jersey. The Company was organized in March of 1989 and commenced operations on May 19, 1989, upon the consummation of the acquisition of all of the outstanding stock of Lakeland Bank, formerly named Lakeland State Bank (Lakeland). Through Lakeland, the Company operates 48 banking offices, located in Morris, Passaic, Sussex, Warren, Essex and Bergen counties in New Jersey. Lakeland offers a full range of lending services, including commercial loans and leases, real estate and consumer loans to small and medium-sized businesses, professionals and individuals located in its markets.

The Company has grown substantially over the last several years, through a combination of organic growth and acquisitions. Lakeland has opened eight new branches since January 1, 2001.

The Company also has grown through acquisitions. Since 1998, the Company has acquired four community banks with an aggregate asset total of approximately $780 million. All of the acquired banks have been merged into Lakeland and their holding companies, if applicable, have been merged into the Company. A summary of the Company s community bank acquisitions is as follows:

Year	Financial Institutions Acquired	Assets of Financial Institutions Acquired(1)
1998	Metropolitan State Bank	$ 85.5 million
1999	High Point Financial Corp. and its National Bank of Sussex County subsidiary	$ 252.7 million
2003	CSB Financial Corp. and its Community State Bank subsidiary	$ 122.2 million
2004	Newton Financial Corp. and its Newton Trust Company subsidiary	$ 320.5 million

(1) Measured as of the end of the last quarter prior to the Company s announcement of the acquisition.

The Company has also diversified its business through opportunistic purchases of specialized lending platforms. In 2000, Lakeland acquired NIA National Leasing and opened a leasing division which provides equipment lease financing to small and medium-sized business clients. In 2004, Lakeland acquired $25.0 million of net receivables and opened an asset based lending department which specializes in utilizing particular assets to fund the working capital needs of borrowers.

At December 31, 2006, the Company had total consolidated assets of $2.3 billion, total consolidated deposits of $1.9 billion, total consolidated loans, net of the allowance for loan losses, of $1.6 billion and total consolidated stockholders equity of $199.5 million.

This Annual Report on Form 10-K contains certain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 (Forward-Looking Statements). Such statements are subject to risks and uncertainties that could cause actual results to differ materially from those projected in such Forward-Looking Statements. Certain factors which could materially affect such results and the future performance of the Company are described in Item 1A - Risk Factors to this Annual Report on Form 10-K.

Commercial Bank Services

Through Lakeland, the Company offers a broad range of lending, depository, and related financial services to individuals and small to medium sized businesses located primarily in northern New Jersey. In the lending area, these services include short and medium term loans, lines of credit, letters of credit, inventory

and accounts receivable financing, real estate construction loans and mortgage loans. Depository products include demand deposits, savings accounts, and time accounts. In addition, the Company offers collection, wire transfer, and night depository services. The Lakeland Bank Equipment Leasing Division provides a solution to small and medium sized companies who prefer to lease equipment over other financial alternatives. Lakeland s asset-based lending portfolio provides commercial borrowers with another lending alternative.

Consumer Banking

Lakeland also offers a broad range of consumer banking services, including checking accounts, savings accounts, NOW accounts, money market accounts, certificates of deposit, secured and unsecured loans, consumer installment loans, mortgage loans, and safe deposit services.

Other Services

Investment and advisory services for individuals are also available.

Competition

Lakeland faces considerable competition in its market areas for deposits and loans from other depository institutions. Many of Lakeland s depository institution competitors have substantially greater resources, broader geographic markets, and higher lending limits than Lakeland and are also able to provide more services and make greater use of media advertising. In recent years, intense market demands, economic pressures, increased customer awareness of products and services, and the availability of electronic services have forced banking institutions to diversify their services and become more cost-effective.

Lakeland also competes with credit unions, brokerage firms, insurance companies, money market mutual funds, consumer finance companies, mortgage companies and other financial companies, some of which are not subject to the same degree of regulation and restrictions as Lakeland in attracting deposits and making loans. Interest rates on deposit accounts, convenience of facilities, products and services, and marketing are all significant factors in the competition for deposits. Competition for loans comes from other commercial banks, savings institutions, insurance companies, consumer finance companies, credit unions, mortgage banking firms and other institutional lenders. Lakeland primarily competes for loan originations through its handling of loans and the overall quality of service. Competition is affected by the availability of lendable funds, general and local economic conditions, interest rates, and other factors that are not readily predictable.

The Company expects that competition will continue in the future.

Concentration

The Company is not dependent for deposits or exposed by loan concentrations to a single customer or a small group of customers the loss of any one or more of which would have a material adverse effect upon the financial condition of the Company.

Employees

At December 31, 2006, the Company had 538 employees. None of these employees is covered by a collective bargaining agreement. The Company considers relations with its employees to be good.

SUPERVISION AND REGULATION

General

The Company is a registered bank holding company under the federal Bank Holding Company Act of 1956, as amended (the Holding Company Act), and is required to file with the Federal Reserve Board an annual report and such additional information as the Federal Reserve Board may require pursuant to the

Holding Company Act. The Company is subject to examination by the Federal Reserve Board.

Lakeland is a state chartered banking association subject to supervision and examination by the Department of Banking and Insurance of the State of New Jersey (the Department) and the Federal Deposit Insurance Corporation (the FDIC). The regulations of the State of New Jersey and FDIC govern most aspects of Lakeland s business, including reserves against deposits, loans, investments, mergers and acquisitions, borrowings, dividends, and location of branch offices. Lakeland is subject to certain restrictions imposed by law on, among other things, (i) the maximum amount of obligations of any one person or entity which may be outstanding at any one time, (ii) investments in stock or other securities of the Company or any subsidiary of the Company, and (iii) the taking of such stock or securities as collateral for loans to any borrower.

In June 2006, Lakeland entered into an agreement with the Department and the FDIC, in which Lakeland agreed to take certain actions to ensure its compliance with the federal Bank Secrecy Act. The Bank Secrecy Act was adopted by Congress to prevent banks and other financial service providers from being used as intermediaries for, or to hide the transfer or deposit of money derived from, criminal activity. Lakeland has submitted a plan to the Department and the FDIC which describes the steps Lakeland has taken pursuant to this agreement, including the adoption of controls, policies and procedures and an employee training program, to ensure compliance with the Bank Secrecy Act.

The Holding Company Act

The Holding Company Act limits the activities which may be engaged in by the Company and its subsidiaries to those of banking, the ownership and acquisition of assets and securities of banking organizations, and the management of banking organizations, and to certain non-banking activities which the Federal Reserve Board finds, by order or regulation, to be so closely related to banking or managing or controlling a bank as to be a proper incident thereto. The Federal Reserve Board is empowered to differentiate between activities by a bank holding company or a subsidiary thereof and activities commenced by acquisition of a going concern.

With respect to non-banking activities, the Federal Reserve Board has by regulation determined that several non-banking activities are closely related to banking within the meaning of the Holding Company Act and thus may be performed by bank holding companies. Although the Company s management periodically reviews other avenues of business opportunities that are included in that regulation, the Company has no present plans to engage in any of these activities other than providing brokerage services.

With respect to the acquisition of banking organizations, the Company is required to obtain the prior approval of the Federal Reserve Board before it may, by merger, purchase or otherwise, directly or indirectly acquire all or substantially all of the assets of any bank or bank holding company, if, after such acquisition, it will own or control more than 5% of the voting shares of such bank or bank holding company.

Regulation of Bank Subsidiaries

There are various legal limitations, including Sections 23A and 23B of the Federal Reserve Act, which govern the extent to which a bank subsidiary may finance or otherwise supply funds to its holding company or its holding company s non-bank subsidiaries. Under federal law, no bank subsidiary may, subject to certain limited exceptions, make loans or extensions of credit to, or investments in the securities of, its parent or the non-bank subsidiaries of its parent (other than direct subsidiaries of such bank which are not financial subsidiaries) or take their securities as collateral for loans to any borrower. Each bank subsidiary is also subject to collateral security requirements for any loans or extensions of credit permitted by such exceptions.

Commitments to Affiliated Institutions

The policy of the Federal Reserve Board provides that a bank holding company is expected to act as a source of financial strength to its subsidiary banks and to commit resources to support such subsidiary banks in circumstances in which it might not do so absent such policy.

Interstate Banking

The Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994 permits bank holding companies to acquire banks in states other than their home state, regardless of applicable state law. This act also authorizes banks to merge across state lines, thereby creating interstate branches. Under the act, each state had the opportunity either to opt out of this provision, thereby prohibiting interstate branching in such state, or to opt in . A state may opt in with respect to de novo branching, thereby permitting a bank to open new branches in a state in which the bank does not already have a branch. Without de novo branching, an out-of-state bank can enter the state only by acquiring an existing bank. New Jersey enacted legislation to authorize interstate banking and branching and the entry into New Jersey of foreign country banks. New Jersey did not authorize de novo branching into the state. However, under federal law, federal savings banks, which meet certain conditions, may branch de novo into a state, regardless of state law.

Gramm-Leach Bliley Act of 1999

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

- allows bank holding companies meeting management, capital, and Community Reinvestment Act standards to engage in a substantially broader range of nonbanking activities than previously was permissible, including insurance underwriting and making merchant banking investments in commercial and financial companies; if a bank holding company elects to become a financial holding company, it files a certification, effective in 30 days, and thereafter may engage in certain financial activities without further approvals;
- allows insurers and other financial services companies to acquire banks;
- removes various restrictions that previously applied to bank holding company ownership of securities firms and mutual fund advisory companies; and
- establishes the overall regulatory structure applicable to bank holding companies that also engage in insurance and securities operations.

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

The USA PATRIOT Act

In response to the events of September 11, 2001, the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (the USA PATRIOT Act), was signed into law on October 26, 2001. The USA PATRIOT Act gives the federal government new powers to address terrorist threats through enhanced domestic security measures, expanded surveillance powers, increased information sharing, and broadened anti-money laundering requirements. By way of amendments to the Bank Secrecy Act, Title III of the USA PATRIOT Act encourages information sharing among bank regulatory agencies and law enforcement bodies. Further, certain provisions of Title III impose affirmative obligations on a broad range of financial institutions, including banks, thrifts, brokers, dealers, credit unions, money transfer agents and parties registered under the Commodity Exchange Act.

Among other requirements, Title III of the USA PATRIOT Act imposes the following requirements with respect to financial institutions:

- All financial institutions must establish anti-money laundering programs that include, at a minimum: (i) internal policies, procedures, and controls; (ii) specific designation of an anti-money laundering compliance officer; (iii) ongoing employee training programs; and (iv) an independent audit function to test the anti-money laundering program.

- The Secretary of the Department of Treasury, in conjunction with other bank regulators, was authorized to issue regulations that provide for minimum standards with respect to customer identification at the time new accounts are opened.

Financial institutions that establish, maintain, administer, or manage private banking accounts or correspondence accounts in the United States for non-United States persons or their representatives (including foreign individuals visiting the United States) are required to establish appropriate, specific and, where necessary, enhanced due diligence policies, procedures, and controls designed to detect and report money laundering.

Financial institutions are prohibited from establishing, maintaining, administering or managing correspondent accounts for foreign shell banks (foreign banks that do not have a physical presence in any country), and will be subject to certain record keeping obligations with respect to correspondent accounts of foreign banks.

Bank regulators are directed to consider a holding company s effectiveness in combating money laundering when ruling on Federal Reserve Act and Bank Merger Act applications.

The United States Treasury Department has issued a number of implementing regulations which apply to various requirements of the USA PATRIOT Act to financial institutions such as Lakeland. These regulations impose obligations on financial institutions to maintain appropriate policies, procedures and controls to detect, prevent and report money laundering and terrorist financing and to verify the identity of their customers.

Sarbanes-Oxley Act of 2002

On July 30, 2002, President Bush signed into law the Sarbanes-Oxley Act of 2002, or the SOA. The stated goals of the SOA are to increase corporate responsibility, to provide for enhanced penalties for accounting and auditing improprieties at publicly traded companies and to protect investors by improving the accuracy and reliability of corporate disclosures pursuant to the securities laws.

The SOA generally applies to all companies, both U.S. and non-U.S., that file or are required to file periodic reports with the Securities and Exchange Commission (the SEC) under the Securities Exchange Act of 1934 (the Exchange Act).

The SOA includes very specific additional disclosure requirements and new corporate governance rules, requires the SEC and securities exchanges to adopt extensive additional disclosure, corporate governance and other related rules and mandates further studies of certain issues by the SEC and the Comptroller General. The SOA represents significant federal involvement in matters traditionally left to state regulatory systems, such as the regulation of the accounting profession, and to state corporate law, such as the relationship between a board of directors and management and between a board of directors and its committees.

The SOA addresses, among other matters:

audit committees for all reporting companies;

certification of financial statements by the chief executive officer and the chief financial officer;

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

a prohibition on insider trading during pension plan black out periods;

disclosure of off-balance sheet transactions;

a prohibition on personal loans to directors and officers (other than loans made by an insured depository institution (as defined in the Federal Deposit Insurance Act), if the loan is subject to the insider lending restrictions of section 22(h) of the Federal Reserve Act);

expedited filing requirements for Forms 4 s;

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

real time filing of periodic reports;

the formation of a public accounting oversight board;

auditor independence; and

various increased criminal penalties for violations of securities laws.

The SEC has enacted various rules to implement various provisions of the SOA with respect to, among other matters, disclosure in periodic filings pursuant to the Exchange Act.

Regulation W

Transactions between a bank and its affiliates are quantitatively and qualitatively restricted under the Federal Reserve Act. The Federal Deposit Insurance Act applies Sections 23A and 23B to insured nonmember banks in the same manner and to the same extent as if they were members of the Federal Reserve System. The Federal Reserve Board has also issued Regulation W, which codifies prior regulations under Sections 23A and 23B of the Federal Reserve Act and interpretative guidance with respect to affiliate transactions. Regulation W incorporates the exemption from the affiliate transaction rules but expands the exemption to cover the purchase of any type of loan or extension of credit from an affiliate. Affiliates of a bank include, among other entities, the bank s holding company and companies that are under common control with the bank. The Company is considered to be an affiliate of Lakeland. In general, subject to certain specified exemptions, a bank or its subsidiaries are limited in their ability to engage in covered transactions with affiliates:

to an amount equal to 10% of the bank s capital and surplus, in the case of covered transactions with any one affiliate; and

to an amount equal to 20% of the bank s capital and surplus, in the case of covered transactions with all affiliates.

In addition, a bank and its subsidiaries may engage in covered transactions and other specified transactions only on terms and under circumstances that are substantially the same, or at least as favorable to the bank or its subsidiary, as those prevailing at the time for comparable transactions with nonaffiliated companies. A covered transaction includes:

a loan or extension of credit to an affiliate;

a purchase of, or an investment in, securities issued by an affiliate;

a purchase of assets from an affiliate, with some exceptions;

the acceptance of securities issued by an affiliate as collateral for a loan or extension of credit to any party; and

the issuance of a guarantee, acceptance or letter of credit on behalf of an affiliate.

In addition, under Regulation W:

a bank and its subsidiaries may not purchase a low-quality asset from an affiliate;

covered transactions and other specified transactions between a bank or its subsidiaries and an affiliate must be on terms and conditions that are consistent with safe and sound banking practices; and

with some exceptions, each loan or extension of credit by a bank to an affiliate must be secured by certain types of collateral with a market value ranging from 100% to 130%, depending on the type of collateral, of the amount of the loan or extension of credit.

Regulation W generally excludes all non-bank and non-savings association subsidiaries of banks from treatment as affiliates, except to the extent that the Federal Reserve Board decides to treat these subsidiaries as affiliates.

Community Reinvestment Act

Under the Community Reinvestment Act (CRA), as implemented by FDIC regulations, a state bank has a continuing and affirmative obligation consistent with its safe and sound operation to help meet the credit needs of its entire community, including low and moderate income neighborhoods. The CRA does not establish specific lending requirements or programs for financial institutions nor does it limit an institution s discretion to develop the types of products and services that it believes are best suited to its particular community. The CRA requires the FDIC, in connection with its examination of a state non-member bank, to assess the bank s record of meeting the credit needs of its community and to take that record into account in its evaluation of certain applications by the bank. Under the FDIC s CRA evaluation system, the FDIC focuses on three tests: (i) a lending test, to evaluate the institution s record of making loans in its service areas; (ii) an investment test, to evaluate the institution s record of investing in community development projects, affordable housing and programs benefiting low or moderate income individuals and businesses; and (iii) a service test, to evaluate the institution s delivery of services through its branches, ATMs and other offices.

Securities and Exchange Commission

The Common Stock of the Company is registered with the SEC under the Exchange Act. As a result, the Company and its officers, directors, and major stockholders are obligated to file certain reports with the SEC. The Company is subject to proxy and tender offer rules promulgated pursuant to the Exchange Act. You may read and copy any document the Company files with the SEC at the SEC s Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information about the Public Reference Room. The SEC maintains a website at http://www.sec.gov that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC, such as the Company.

The Company maintains a website at http://www.lakelandbank.com. The Company makes available on its website the proxy statements and reports on Forms 8-K, 10-K and 10-Q that it files with the SEC as soon as reasonably practicable after such material is electronically filed with or furnished to the SEC. Additionally, the Company has adopted and posted on its website a Code of Ethics that applies to its principal executive officer, principal financial officer and principal accounting officer. The Company intends to disclose any amendments to or waivers of the Code of Ethics on its website.

Effect of Government Monetary Policies

The earnings of the Company are and will be affected by domestic economic conditions and the monetary and fiscal policies of the United States government and its agencies. The monetary policies of the Federal Reserve Board have had, and will likely continue to have, an important impact on the operating results of commercial banks through the Board s power to implement national monetary policy in order to, among other things, curb inflation or combat a recession. The Federal Reserve Board has a major effect upon the levels of bank loans, investments and deposits through its open market operations in United States government securities and through its regulation of, among other things, the discount rate of borrowings of banks and the reserve requirements against bank deposits. It is not possible to predict the nature and impact of future changes in monetary fiscal policies.

Dividend Restrictions

The Company is a legal entity separate and distinct from Lakeland. Virtually all of the revenue of the Company available for payment of dividends on its capital stock will result from amounts paid to the Company by Lakeland. All such dividends are subject to various limitations imposed by federal and state laws and by regulations and policies adopted by federal and state regulatory agencies. Under State law, a bank may not pay dividends unless, following the dividend payment, the capital stock of the bank would be unimpaired and either (a) the bank will have a surplus of not less than 50% of its capital stock, or, if not, (b) the payment of the dividend will not reduce the surplus of the bank.

If, in the opinion of the FDIC, a bank under its jurisdiction is engaged in or is about to engage in an unsafe or unsound practice (which could include the payment of dividends), the FDIC may require, after notice and hearing, that such bank cease and desist from such practice or, as a result of an unrelated practice, require the bank to limit dividends in the future. The Federal Reserve Board has similar authority with respect to bank holding companies. In addition, the Federal Reserve Board and the FDIC have issued policy statements which provide that insured banks and bank holding companies should generally only pay dividends out of current operating earnings. Regulatory pressures to reclassify and charge off loans and to establish additional loan loss reserves can have the effect of reducing current operating earnings and thus impacting an institution s ability to pay dividends. Further, as described herein, the regulatory authorities have established guidelines with respect to the maintenance of appropriate levels of capital by a bank or bank holding company under their jurisdiction. Compliance with the standards set forth in these policy statements and guidelines could limit the amount of dividends which the Company and Lakeland may pay. Under the Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA), banking institutions which are deemed to be undercapitalized will, in most instances, be prohibited from paying dividends. See FDICIA . See also Note 18 - Regulatory Matters of the Notes to Consolidated Financial Statements for further information regarding dividends.

Capital Adequacy Guidelines

The Federal Reserve Board has adopted Risk-Based Capital Guidelines. These guidelines establish minimum levels of capital and require capital adequacy to be measured in part upon the degree of risk associated with certain assets. Under these guidelines all banks and bank holding companies must have a core or Tier 1 capital to risk-weighted assets ratio of at least 4% and a total capital to risk-weighted assets ratio of at least 8%. At December 31, 2006, the Company s Tier 1 capital to risk-weighted assets ratio and total capital to risk-weighted assets ratio were 10.13% and 10.96%, respectively.

In addition, the Federal Reserve Board and the FDIC have approved leverage ratio guidelines (Tier 1 capital to average quarterly assets, less goodwill) for bank holding companies such as the Company. These guidelines provide for a minimum leverage ratio of 3% for bank holding companies that meet certain specified criteria, including that they have the highest regulatory rating. All other holding companies are required to maintain a leverage ratio of 3% plus an additional cushion of at least 100 to 200 basis points. The Company s leverage ratio was 7.51% at December 31, 2006.

Under FDICIA, federal banking agencies have established certain additional minimum levels of capital which accord with guidelines established under that act. See FDICIA .

FDICIA

Enacted in December 1991, FDICIA substantially revised the bank regulatory provisions of the Federal Deposit Insurance Act and several other federal banking statutes. Among other things, FDICIA requires federal banking agencies to broaden the scope of regulatory corrective action taken with respect to banks that do not meet minimum capital requirements and to take such actions promptly in order to minimize losses to the FDIC. Under FDICIA, federal banking agencies were required to establish minimum levels of capital (including both a leverage limit and a risk-based capital requirement) and specify for each capital measure the levels at which depository institutions will be considered well capitalized , adequately capitalized , undercapitalized , significantly undercapitalized or critically undercapitalized .

Under regulations adopted under these provisions, for an institution to be well capitalized it must have a total risk-based capital ratio of at least 10%, a Tier 1 risk-based capital ratio of at least 6% and a Tier 1 leverage ratio of at least 5% and not be subject to any specific capital order or directive. For an institution to be adequately capitalized it must have a total risk-based capital ratio of at least 8%, a Tier 1 risk-based capital ratio of at least 4% and a Tier 1 leverage ratio of at least 4% (or in some cases 3%). Under the regulations, an institution will be deemed to be undercapitalized if it has a total risk-based capital ratio that is less than 8%, a Tier 1 risk-based capital ratio that is less than 4%, or a Tier 1 leverage ratio of less than 4% (or in some cases 3%). An institution will be deemed to be significantly undercapitalized if it has a total risk-based capital ratio that is less than 6%, a Tier 1 risk-based capital ratio that is less than 3%, or a leverage ratio that is less than 3% and will be deemed to be critically undercapitalized if it has a ratio of tangible equity to total assets that is equal to or less than 2%. An institution may be deemed to be in a capitalization category that is lower than is indicated by its actual capital position if it receives an unsatisfactory examination rating or is deemed to be in an unsafe or unsound condition or to be engaging in unsafe or unsound practices. As of December 31, 2006, the Company and Lakeland met all regulatory requirements for classification as well capitalized under the regulatory framework for prompt corrective action.

In addition, FDICIA requires banking regulators to promulgate standards in a number of other important areas to assure bank safety and soundness, including internal controls, information systems and internal audit systems, credit underwriting, asset growth, compensation, loan documentation and interest rate exposure.

Deposit Insurance and Premiums

Effective March 31, 2006, the FDIC merged the Bank Insurance Fund (BIF) and the Savings Association Insurance Fund (SAIF) into the Deposit Insurance Fund (DIF). As part of this legislation, the following changes were enacted. Effective April 1, 2006, the coverage limit for retirement accounts was increased to $250,000 with other accounts remaining at $100,000. Additionally, the amount of the premium assessment was determined by the FDIC s risk-based insurance assessment system in which each insured bank is placed in one of several assessment risk classifications based on the FDIC s evaluation. Banks with higher levels of capital and a low degree of supervisory concern are assessed lower premiums than banks with lower levels of capital or a higher degree of supervisory concern. Lakeland qualified for the lowest premium calculation and therefore was not required to pay any deposit premiums in 2006.

In November 2006, the FDIC adopted a new risk-based insurance assessment system effective January 1, 2007, designed to base what banks pay for deposit insurance on the risk they pose. In 2007, assessment rates will range between 5 cents per $100 of assessable deposits in the lowest risk category to 43 cents per $100 of assessable deposits in the highest risk category. An FDIC assessment credit for prior contributions is expected to offset this assessment for 2007.

In addition to deposit insurance assessments, the FDIC is required to continue to collect from institutions payments for the servicing of obligations of the Financing Corporation (FICO) that were issued in connection with the failure of certain savings and loan associations, so long as such obligations remain outstanding. Lakeland paid a FICO premium of $226,000 in 2006.

Proposed Legislation

From time to time proposals are made in the United States Congress, the New Jersey Legislature, and before various bank regulatory authorities, which would alter the powers of, and place restrictions on, different types of banking organizations. It is impossible to predict the impact, if any, of potential legislative trends on the business of the Company and its subsidiaries.

In accordance with federal law providing for deregulation of interest on all deposits, banks and thrift organizations are now unrestricted by law or regulation from paying interest at any rate on most time deposits. It is not clear whether deregulation and other pending changes in certain aspects of the banking industry will result in further increases in the cost of funds in relation to prevailing lending rates.

ITEM 1A - Risk Factors.

Our business, financial condition, operating results and cash flows can be affected by a number of factors, including, but not limited to, those set forth below, any one of which could cause our actual results to vary materially from recent results or from our anticipated future results.

We are subject to interest rate risk and variations in interest rates may negatively affect our financial performance.

We are unable to predict actual fluctuations of market interest rates. Rate fluctuations are influenced by many factors, including:

inflation or recession;

a rise or fall in unemployment;

tightening or expansion of the money supply;

domestic and international disorder; and

instability in domestic and foreign financial markets.

Both increases and decreases in the interest rate environment may reduce our profits. We expect that we will continue to realize income from the difference or spread between the interest we earn on loans, securities and other interest-earning assets, and the interest we pay on deposits, borrowings and other interest-bearing liabilities. Our net interest spreads are affected by the differences between the maturities and repricing characteristics of our interest-earning assets and interest-bearing liabilities. Our interest-earning assets may not reprice as slowly or rapidly as our interest-bearing liabilities. Changes in market interest rates could materially and adversely affect our net interest spread, asset quality, levels of prepayments, cash flows, the market value of our securities portfolio, loan and deposit growth, costs and yields on loans and deposits and our overall profitability.

Lakeland s ability to pay dividends is subject to regulatory limitations which, to the extent that our holding company requires such dividends in the future, may affect our holding company s ability to pay its obligations and pay dividends to shareholders.

As a bank holding company, the Company is a separate legal entity from Lakeland and its subsidiaries, and we do not have significant operations of our own. We currently depend on Lakeland s cash and liquidity to pay our operating expenses and dividends to shareholders. The availability of dividends from Lakeland is limited by various statutes and regulations. The inability of the Company to receive dividends from Lakeland could adversely affect our financial condition, results of operations, cash flows and prospects and the Company s ability to pay dividends.

Our allowance for loan and lease losses may not be adequate to cover actual losses.

Like all commercial banks, we maintain an allowance for loan and lease losses to provide for loan and lease defaults and non-performance. If our allowance for loan and lease losses is not adequate to cover actual loan and lease losses, we may be required to significantly increase future provisions for loan and lease losses, which could materially and adversely affect our operating results. Our allowance for loan and lease losses is determined by analyzing historical loan and lease losses, current trends in delinquencies and charge-offs, plans for problem loan and lease resolution, the opinions of our regulators, changes in the size and composition of the loan and lease portfolio and industry information. We also consider the possible effects of economic events, which are difficult to predict. The amount of future losses is affected by changes in economic, operating and other conditions, including changes in interest rates, many of which are beyond our control. These losses may exceed our current estimates. Federal regulatory agencies, as an integral part of

their examination process, review our loans and the allowance for loan and lease losses. While we believe that our allowance for loan and lease losses in relation to our current loan portfolio is adequate to cover current losses, we cannot assure you that we will not need to increase our allowance for loan and lease losses or that regulators will not require us to increase this allowance. An increase in our allowance for loan and lease losses could materially and adversely affect our earnings and profitability.

We are subject to various lending and other economic risks that could adversely affect our results of operations and financial condition.

Economic, political and market conditions, trends in industry and finance, legislative and regulatory changes, changes in governmental monetary and fiscal policies and inflation affect our business. These factors are beyond our control. A deterioration in economic conditions, particularly in New Jersey, could have the following consequences, any of which could materially adversely affect our business:

- loan and lease delinquencies may increase;
- problem assets and foreclosures may increase;
- demand for our products and services may decrease; and
- collateral for loans made by us may decline in value, in turn reducing the borrowing ability of our customers.

A downturn in the real estate market, particularly in New Jersey, could hurt our business. If there is a significant decline in real estate values in New Jersey, our ability to recover on defaulted loans by selling the underlying real estate would be reduced, and we would be more likely to suffer losses on defaulted loans.

We may suffer losses in our loan portfolio despite our underwriting practices.

We seek to mitigate the risks inherent in our loan portfolio by adhering to specific underwriting practices. Although we believe that our underwriting criteria are appropriate for the various kinds of loans that we make, we may incur losses on loans that meet our underwriting criteria, and these losses may exceed the amounts set aside as reserves in our allowance for loan and lease losses.

Factors outside our control could have an adverse effect on our liquidity and operating results.

Like all commercial banking institutions, we rely on deposits as one of our sources of funds to make loans and meet our other liquidity needs. We believe that recently, a more competitive interest rate environment has caused a flow of funds away from financial institutions such as Lakeland into investments in equity securities, real estate, money market funds and other investments where the potential returns and liquidity characteristics may be more appealing to certain depositors. In addition, a significant amount of our deposits are from municipalities, which typically withdraw funds periodically. This results in more volatility in our level of deposits than would otherwise be the case. If we are unable to continue to attract new deposits, our liquidity could be adversely affected. If we are required to pay higher rates on deposits to attract and retain them, our operating results could be adversely affected.

We face strong competition from other financial institutions, financial service companies and other organizations offering services similar to the services that we provide.

Many competitors offer the types of loans and banking services that we offer. These competitors include other state and national banks, savings associations, regional banks and other community banks. We also face competition from many other types of financial institutions, including finance companies, brokerage firms, insurance companies, credit unions, mortgage banks and other financial intermediaries. Many of our competitors have greater financial resources than we do, which may enable them to offer a broader range of services and products, and to advertise more extensively, than we do. Our inability to compete effectively

would adversely affect our business.

If we do not successfully integrate any banks that we may acquire in the future, the combined company may be adversely affected.

If we make acquisitions in the future, we will need to integrate the acquired entities into our existing business and systems. We may experience difficulties in accomplishing this integration or in effectively managing the combined company after any future acquisition. Any actual cost savings or revenue enhancements that we may anticipate from a future acquisition will depend on future expense levels and operating results, the timing of certain events and general industry, regulatory and business conditions. Many of these events will be beyond our control, and we cannot assure you that if we make any acquisitions in the future, we will be successful in integrating those businesses into our own.

ITEM 1B - Unresolved Staff Comments

Not Applicable.

ITEM 2 Properties

The Company s principal office is located at 250 Oak Ridge Road, Oak Ridge, New Jersey 07438. It also maintains an operations center in Branchville, New Jersey.

The Company operates 48 banking locations in Passaic, Morris, Sussex, Bergen, Essex and Warren Counties, New Jersey. The following chart provides information about the Company s leased offices:

Location	Lease Expiration Date
Caldwell	April 30, 2024
Carlstadt	December 31, 2015
Cedar Crest	August 19, 2011
Fairfield	February 28, 2010
Hackensack	September 1, 2008
Hampton	September 30, 2018
Little Falls	November 30, 2010
Morristown	August 31, 2009
Newton	December 31, 2011
Park Ridge	December 31, 2009
Pompton Plains	March 31, 2008
Ringwood	February 28, 2008
Rockaway	August 15, 2008
Sussex/Wantage	July 31 2012
Vernon	September 30, 2011
Wantage	October 31, 2011
Wharton	July 24, 2010
Woodland Commons	August 31, 2016

For information regarding all of the Company s rental obligations, see Notes to Consolidated Financial Statements.

All other offices of the Company and Lakeland are owned and are unencumbered.

ITEM 3 - Legal Proceedings

In 2001, a complaint captioned Ronnie Clayton dba Clayton Trucking, et al v. Ronald Fisher, et al was filed in the Los Angeles County Superior Court against Lakeland and others. Plaintiffs are certain of the lessees who had entered into leases with Commercial Money Center, Inc. (CMC). (As previously disclosed,

Lakeland had purchased four separate portfolios of predominantly commercial leases from CMC.) Plaintiffs allege, among other things, that these leases are not true leases but are instead loans which charge usurious interest rates. They further allege that because of various California Financial Code violations by CMC, the lease instruments are either void or must be reformed and all amounts paid by the lessees must be returned to them. The action against Lakeland has been stayed while an appeal by plaintiffs is pending concerning the dismissal of certain of plaintiffs claims against defendants.

From time to time, the Company and its subsidiaries are defendants in legal proceedings relating to their respective businesses. While the ultimate outcome of any pending matter cannot be determined at this time, management does not believe that the outcome of any pending legal proceeding will materially affect the consolidated financial position of the Company, but could possibly be material to the consolidated results of operations of any one period.

ITEM 4 - Submission of Matters to a Vote of Security Holders

There were no matters submitted to a vote of security holders of the Company during the fourth quarter of 2006.

ITEM 4A - Executive Officers of the Registrant

The following table sets forth the name and age of each executive officer of the Company. Each officer is appointed by the Company s Board of Directors. Unless otherwise indicated, the persons named below have held the position indicated for more than the past five years.

Name and Age	Officer of The Company Since	Position with the Company, its Subsidiary Banks, and Business Experience
Roger Bosma Age 64	1999	President and Chief Executive Officer of the Company (June, 1999 Present); President and Chief Executive Officer of Lakeland Bank (January, 2002 Present)
Robert A. Vandenbergh Age 55	1999	Senior Executive Vice President and Chief Lending Officer of the Company (December, 2006 Present); Executive Vice President and Chief Lending Officer of the Company (October, 1999 December, 2006); President, The National Bank of Sussex County (November, 1998 June, 2001)
Joseph F. Hurley Age 56	1999	Executive Vice President and Chief Financial Officer of the Company (November, 1999 Present)
Jeffrey J. Buonforte Age 55	1999	Executive Vice President and Chief Retail Officer of the Company (November, 1999 Present)
Louis E. Luddecke Age 60	1999	Executive Vice President and Chief Operations Officer of the Company (October, 1999 Present)
Steven Schachtel Age 49	2000	President, Lakeland Bank Equipment Leasing Division (April, 2000 Present)
James R. Noonan Age 55	2003	Executive Vice President and Chief Credit Officer of the Company (December, 2003 Present); Senior Vice President and Chief Credit Officer of the Company (March, 2003 December, 2003); Senior Credit Officer, Fleet National Bank (prior years March, 2003)

PART II

ITEM 5 MARKET FOR THE REGISTRANT S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Shares of the Common Stock of Lakeland Bancorp, Inc. have been traded under the symbol LBAI on the NASDAQ Global Select Market (or the Nasdaq National Market) since February 22, 2000 and in the over the counter market prior to this date. As of December 31, 2006, there were 3,846 shareholders of record of Common Stock. The following table sets forth the range of the high and low daily closing prices of the Common Stock as provided by Nasdaq and dividends declared for the periods presented. Prices and dividends have been adjusted to reflect the Company s 5% stock dividend paid on August 15, 2006.

Year ended December 31, 2006	High	Low	Dividends Declared
First Quarter	$ 15.29	$ 13.71	$ 0.095
Second Quarter	14.92	12.67	0.095
Third Quarter	15.29	13.35	0.095
Fourth Quarter	15.43	12.88	0.100

Year ended December 31, 2005	High	Low	Dividends Declared
First Quarter	$ 16.22	$ 13.87	$ 0.091
Second Quarter	15.01	12.80	0.091
Third Quarter	15.53	14.05	0.095
Fourth Quarter	15.56	13.61	0.095

Dividends on the Company s Common Stock are within the discretion of the Board of Directors of the Company and are dependent upon various factors, including the future earnings and financial condition of the Company and Lakeland and bank regulatory policies.

The Bank Holding Company Act of 1956 restricts the amount of dividends the Company can pay. Accordingly, dividends should generally only be paid out of current earnings, as defined.

The New Jersey Banking Act of 1948 restricts the amount of dividends paid on the capital stock of New Jersey chartered banks. Accordingly, no dividends shall be paid by such banks on their capital stock unless, following the payment of such dividends, the capital stock of the bank will be unimpaired and the bank will have a surplus of not less than 50% of its capital stock, or, if not, the payment of such dividend will not reduce the surplus of the bank. Under this limitation, approximately $141.3 million was available for the payment of dividends from Lakeland to the Company as of December 31, 2006.

Capital guidelines and other regulatory requirements may further limit the Company s and Lakeland s ability to pay dividends. See Item 1 Business Supervision and Regulation Dividend Restrictions.

Equity Compensation Plan Information

The following table gives information about the Company s Common Stock that may be issued upon the exercise of options under the Company s Amended and Restated 2000 Equity Compensation Program (the Stock Option Plan), as of December 31, 2006. This plan was Lakeland s only equity compensation plan in existence as of December 31, 2006. No warrants or rights may be granted, or are outstanding, under the Stock Option Plan.

Plan Category	(a) Number Of Securities To Be Issued Upon Exercise Of Outstanding Options, Warrants and Rights	(b) Weighted-Average Exercise Price Of Outstanding Options, Warrants and Rights	(c) Number Of Securities Remaining Available For Future Issuance Under Equity Compensation Plans (Excluding Securities Reflected In Column (a))
Equity Compensation Plans Approved by Shareholders	**1,176,628**	**$ 13.07**	**656,770**
Equity Compensation Plans Not Approved by Shareholders			
TOTAL	**1,176,628**	**$ 13.07**	**656,770**

The number in column (a) includes 36,028 shares subject to restricted stock awards granted under the Company s Stock Option Plan, including unvested shares. Shares subject to restricted stock awards have been excluded for purposes of calculating the weighted-average exercise price in column (b).

Item 6

SELECTED CONSOLIDATED FINANCIAL DATA

(Not covered by Report of Independent Registered Public Accounting Firm)

Years Ended December 31	2006	2005	2004 [2]	2003 [3]	2002
			(in thousands except per share data)		
Interest income	**$ 119,808**	$ 103,839	$ 83,319	$ 66,922	$ 65,520
Interest expense	**53,104**	33,632	21,817	16,224	17,346
Net interest income	**66,704**	70,207	61,502	50,698	48,174
Provision for loan and lease losses	**1,726**	1,555	3,602	3,000	10,500
Noninterest income	**17,175**	15,128	12,761	10,926	9,001
Gains (losses) on sales of investment securities	**(2,995)**	(583)	638	1,857	876
Noninterest expenses	**54,721**	53,392	47,185	38,287	33,587
Income before income taxes	**24,437**	29,805	24,114	22,194	13,964
Income tax provision	**7,460**	9,584	7,619	7,087	3,887
Net income	**$ 16,977**	$ 20,221	$ 16,495	$ 15,107	$ 10,077
Per-Share Data[1]					
Weighted average shares outstanding:					
Basic	**22,039**	22,511	20,295	16,847	16,577
Diluted	**22,183**	22,681	20,545	17,081	16,886
Earnings per share:					
Basic	**$ 0.77**	$ 0.90	$ 0.81	$ 0.90	$ 0.61
Diluted	**$ 0.77**	$ 0.89	$ 0.80	$ 0.88	$ 0.60
Cash dividend per common share	**$ 0.39**	$ 0.37	$ 0.36	$ 0.34	$ 0.30
Book value per common share	**$ 9.04**	$ 8.65	$ 8.53	$ 6.31	$ 5.51
At December 31					
Investment securities available for sale	**$ 280,509**	$ 515,903	$ 582,106	$ 557,402	$ 361,760
Investment securities held to maturity	**142,838**	154,569	162,922	43,009	46,083
Loans, net of deferred fees	**1,591,644**	1,312,767	1,176,005	851,536	719,658
Goodwill and other identifiable intangible assets	**92,053**	93,395	94,119	27,609	3,020
Total assets	**2,263,573**	2,206,033	2,141,021	1,585,290	1,207,105
Total deposits	**1,860,627**	1,798,160	1,726,804	1,325,682	1,059,092
Total core deposits	**1,357,748**	1,350,567	1,360,980	1,038,195	807,747
Long-term borrowings	**148,413**	101,764	98,991	89,500	31,000
Total stockholders equity	**199,500**	191,781	194,548	110,951	90,767
Performance ratios					
Return on Average Assets	**0.76%**	0.94%	0.90%	1.10%	0.89%
Return on Average Equity	**8.85%**	10.55%	10.79%	15.45%	11.29%
Return on Tangible Equity[4]	**17.14%**	20.69%	17.99%	17.58%	11.69%
Efficiency ratio	**62.28%**	59.76%	60.70%	60.32%	57.23%
Net Interest Margin (tax equivalent basis)	**3.39%**	3.73%	3.82%	4.12%	4.75%
Loans to Deposits	**85.54%**	73.01%	68.10%	64.23%	67.95%
Capital ratios					
Tier 1 leverage ratio	**7.51%**	7.49%	7.71%	7.84%	7.01%
Total risk-based capital ratio	**10.96%**	12.47%	13.27%	15.96%	12.20%

The following reconciliation table provides a more detailed analysis of this non-GAAP performance measure:

Years Ended December 31	2006	2005	2004	2003	2002
Return on average equity	**8.85%**	10.55%	10.79%	15.45%	11.29%
Effect of intangibles	**8.29%**	10.14%	7.20%	2.13%	0.40%
Return on average tangible equity	**17.14%**	20.69%	17.99%	17.58%	11.69%

(1) Restated for 5% stock dividends in 2006, 2005, 2003 and 2002.
(2) The results of operations include Newton Trust Company from July 1, 2004 forward.
(3) The results of operations include Community State Bank from August 25, 2003 forward.
(4) This is a non-GAAP ratio. Return on Tangible Equity is defined as net income as a percentage of average total equity reduced by recorded intangible assets. This may be important to investors that are interested in analyzing our return on equity exclusive of the effect of changes in intangible assets on equity.

Item 7

MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION

AND RESULTS OF OPERATIONS

This section presents a review of Lakeland Bancorp, Inc. s consolidated results of operations and financial condition. You should read this section in conjunction with the selected consolidated financial data that is presented on the preceding page as well as the accompanying financial statements and notes to financial statements. As used in the following discussion, the term Company refers to Lakeland Bancorp, Inc. and Lakeland refers to the Company s wholly owned banking subsidiary Lakeland Bank. The Newton Trust Company (Newton) was merged into Lakeland on November 4, 2005. Newton Financial Corporation (NFC), the parent company of Newton, was merged into the Company on July 1, 2004 and Community State Bank (CSB) was merged into Lakeland on August 25, 2003.

Statements Regarding Forward-Looking Information

The information disclosed in this document includes various forward-looking statements that are made in reliance upon the safe harbor provisions of the Private Securities Litigation Reform Act of 1995 with respect to credit quality (including delinquency trends and the allowance for loan and lease losses), corporate objectives, and other financial and business matters. The words anticipates, projects, intends, estimates, expects, believes, plans, may, will, should, could, and other sim intended to identify such forward-looking statements. The Company cautions that these forward-looking statements are necessarily speculative and speak only as of the date made, and are subject to numerous assumptions, risks and uncertainties, all of which may change over time. Actual results could differ materially from such forward-looking statements.

In addition to the factors disclosed by the Company elsewhere in this document, the following factors, among others, could cause the Company s actual results to differ materially and adversely from such forward-looking statements: pricing pressures on loan and deposit products; competition; changes in economic conditions nationally, regionally and in the Company s markets; the extent and timing of actions of the Federal Reserve Board; changes in levels of market interest rates; clients acceptance of the Company s products and services; credit risks of lending activities; changes in the conditions of the capital markets in general and in the capital markets for financial institutions in particular and the impact of the war in Iraq on such markets; and the extent and timing of legislative and regulatory actions and reforms.

The above-listed risk factors are not necessarily exhaustive, particularly as to possible future events, and new risk factors may emerge from time to time. Certain events may occur that could cause the Company s actual results to be materially different than those described in the Company s periodic filings with the Securities and Exchange Commission. Any statements made by the Company that are not historical facts should be considered to be forward-looking statements. The Company is not obligated to update and does not undertake to update any of its forward-looking statements made herein.

Significant Accounting Policies, Judgments and Estimates

The accounting and reporting policies of the Company and Lakeland conform with accounting principles generally accepted in the United States of America and predominant practices within the banking industry. The consolidated financial statements include the accounts of the Company, Lakeland, Lakeland Investment Corp., and Lakeland NJ Investment Corp. All intercompany balances and transactions have been eliminated.

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements. These estimates and assumptions also affect reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates. Significant estimates implicit in these financial statements are as follows.

The principal estimates that are particularly susceptible to significant change in the near term relate to the allowance for loan and lease losses, the Company s deferred tax asset and the analysis of goodwill impairment. The evaluation of the adequacy of the allowance for loan and lease losses includes, among other factors, an analysis of historical loss rates, by category, applied to current loan totals. However, actual losses may be higher or lower than historical trends, which vary. Actual losses on specified problem loans, which also are provided for in the

evaluation, may vary from estimated loss percentages, which are established based upon a limited number of potential loss classifications.

The allowance for loan and lease losses is established through a provision for loan and lease losses charged to expense. Loan principal considered to be uncollectible by management is charged against the allowance for loan and lease losses. The allowance is an amount that management believes will be adequate to absorb losses on existing loans that may become uncollectible based upon an evaluation of known and inherent risks in the loan portfolio. The evaluation takes into consideration such factors as changes in the nature and size of the loan portfolio, overall portfolio quality, specific problem loans, and current economic conditions which may affect the borrowers ability to pay. The evaluation also details historical losses by loan category, the resulting loss rates for which are projected at current loan total amounts. Loss estimates for specified problem loans are also detailed. All of the factors considered in the analysis of the adequacy of the allowance for loan and lease losses may be subject to change. To the extent actual outcomes differ from management estimates, additional provisions for loan losses may be required that would adversely impact earnings in future periods.

The Company accounts for impaired loans in accordance with SFAS No. 114, Accounting by Creditors for Impairment of a Loan, as amended by SFAS No. 118, Accounting by Creditors for Impairment of a Loan - Income Recognition and Disclosures. Impairment is measured based on the present value of expected future cash flows discounted at the loan s effective interest rate, except that as a practical expedient, a creditor may measure impairment based on a loan s observable market price, or the fair value of the collateral if the loan is collateral-dependent. Regardless of the measurement method, a creditor must measure impairment based on the fair value of the collateral when the creditor determines that foreclosure is probable.

The Company accounts for income taxes under the liability method of accounting for income taxes. Deferred tax assets and liabilities are determined based on the difference between the financial statement and tax bases of assets and liabilities as measured by the enacted tax rates that will be in effect when these differences reverse. Deferred tax expense is the result of changes in deferred tax assets and liabilities. The principal types of differences between assets and liabilities for financial statement and tax return purposes are allowance for loan and lease losses, core deposit intangible, deferred loan fees, deferred compensation and securities available for sale.

The Company accounts for goodwill and other identifiable intangible assets in accordance with SFAS No. 142, Goodwill and Intangible Assets. SFAS No. 142 includes requirements to test goodwill and indefinite lived intangible assets for impairment rather than amortize them. The Company tests goodwill for impairment annually at the reporting unit level using various market valuation methodologies. The Company has tested the goodwill as of December 31, 2006 and has determined that it is not impaired.

Financial Overview

The year ended December 31, 2006 represented a year of continued growth for the Company. In 2006, the Company opened two new branches and sold one branch in a non-contiguous market. The Company also completed a balance sheet restructuring where it sold $97.3 million in securities yielding 3.47% in order to lower its borrowings and to fund loan growth resulting in improved net interest income in future periods. As discussed in this management s discussion and analysis:

- Total loans and leases increased by $278.7 million or 21%.

- Lakeland sold $97.3 million in securities in fourth quarter 2006 for a loss of $3.3 million to lower its borrowings and to fund loan growth.

- Net income decreased $3.2 million or 16% from 2005 to 2006, primarily as a result of the balance sheet restructuring discussed above.

Net income for 2006 was $17.0 million or $0.77 per diluted share compared to net income of $20.2 million and $0.89 per diluted share in 2005. For 2006, Return on Average Assets was 0.76% and Return on Average Equity was 8.85%. For 2005, Return on Average Assets was 0.94% and Return on Average Equity was 10.55%.

The impact of the loss of $3.3 million resulting from the balance sheet restructuring, and the write-off of $300,000 in costs related to a stock offering, which the Company elected not to complete, reduced after tax income by $2.3 million or $0.10 per share.

In 2004, net income was $16.5 million or $0.80 per diluted share with a Return on Average Assets of 0.90% and a Return on Average Equity of 10.79%.

Net interest income

Net interest income is the difference between interest income on earning assets and the cost of funds supporting those assets. The Company s net interest income is determined by: *(i)* the volume of interest-earning assets that it holds and the yields that it earns on those assets, and *(ii)* the volume of interest-bearing liabilities that it has assumed and the rates that it pays on those liabilities. Net interest income increases when the Company can use noninterest- bearing deposits to fund or support interest-earning assets.

Net interest income for 2006 on a tax equivalent basis was $68.7 million, representing a decrease of $3.5 million or 5% from the $72.2 million earned in 2005. Net interest income for 2004 on a tax equivalent basis was $63.2 million. The decrease in net interest income from 2005 to 2006 resulted from an increase in the Company s cost of funds of 101 basis points and a $90.7 million increase in average interest-bearing liabilities partially offset by a $91.5 million increase in average interest-earning assets and a 55 basis point increase in the yield on average interest-earning assets. The increase in net interest income in 2005 from 2004 resulted from an increase in earning assets of $279.3 million partially offset by a $257.7 million increase in interest-bearing liabilities and a 47 basis point increase in the cost of funds. Factors contributing to the decline in the net interest margin will be discussed in further detail below.

Interest income and expense volume/rate analysis. The following table shows the impact that changes in average balances of the Company s assets and liabilities and changes in average interest rates have had on the Company s net interest income over the past three years. This information is presented on a tax equivalent basis assuming a 35% tax rate. If a change in interest income or expense is attributable to a change in volume and a change in rate, the amount of the change is allocated proportionately.

INTEREST INCOME AND EXPENSE VOLUME/RATE ANALYSIS

(tax equivalent basis, in thousands)

	2006 vs. 2005 Increase (Decrease)			2005 vs. 2004 Increase (Decrease)		
	Due to Change in:		**Total**	Due to Change in:		Total
	Volume	**Rate**	**Change**	Volume	Rate	Change
Interest Income						
Loans	**$ 12,926**	**$ 5,595**	**$ 18,521**	$ 13,722	$ 3,714	$ 17,436
Taxable investment securities	**(4,652)**	**1,740**	**(2,912)**	1,700	491	2,191
Tax-exempt investment securities	**161**	**(63)**	**98**	801	(162)	639
Federal funds sold	**(14)**	**310**	**296**	(14)	492	478
Total interest income	**8,421**	**7,582**	**16,003**	16,209	4,535	20,744
Interest Expense						
Savings deposits	**(65)**	**2,328**	**2,263**	85	236	321
Interest-bearing transaction accounts	**219**	**6,910**	**7,129**	1,183	3,649	4,832
Time deposits	**1,881**	**5,441**	**7,322**	2,241	1,911	4,152
Borrowings	**1,247**	**1,511**	**2,758**	2,645	(135)	2,510
Total interest expense	**3,282**	**16,190**	**19,472**	6,154	5,661	11,815
NET INTEREST INCOME (TAX EQUIVALENT BASIS)	**$ 5,139**	**$ (8,608)**	**$ (3,469)**	$ 10,055	$ (1,126)	$ 8,929

The following table reflects the components of the Company s net interest income, setting forth for the years presented, (1) average assets, liabilities and stockholders equity, (2) interest income earned on interest-earning assets and interest expense paid on interest-bearing liabilities, (3) average yields earned on interest-earning assets and average rates paid on interest-bearing liabilities, (4) the Company s net interest spread (i.e., the average yield on interest-earning assets less the average cost of interest-bearing liabilities) and (5) the Company s net interest margin. Rates are computed on a tax equivalent basis assuming a 35% tax rate.

CONSOLIDATED STATISTICS ON A TAX EQUIVALENT BASIS

	2006			2005			2004		
	Average Balance	**Interest Income/ Expense**	**Average rates earned/ paid**	Average Balance	Interest Income/ Expense	Average rates earned/ paid	Average Balance	Interest Income/ Expense	Average rates earned/ paid
				(dollars in thousands)					
Assets									
Interest-earning assets:									
Loans (A)	**$ 1,419,272**	**$ 94,909**	**6.69%**	$ 1,222,084	$ 76,388	6.25%	$ 999,865	$ 58,952	5.90%
Taxable investment securities	**485,607**	**20,115**	**4.14%**	593,789	23,027	3.88%	549,728	20,836	3.79%
Tax-exempt securities	**102,003**	**5,729**	**5.62%**	99,110	5,631	5.68%	84,889	4,992	5.88%
Federal funds sold (B)	**21,379**	**1,060**	**4.96%**	21,798	764	3.50%	23,034	286	1.24%
Total interest-earning assets	**2,028,261**	**121,813**	**6.01%**	1,936,781	105,810	5.46%	1,657,516	85,066	5.13%
Noninterest earning assets:									
Allowance for loan and lease losses	**(13,007)**			(15,513)			(18,150)		
Other assets	**218,901**			232,455			191,100		
TOTAL ASSETS	**$ 2,234,155**			$ 2,153,723			$ 1,830,466		
Liabilities and Stockholders Equity									
Interest-bearing liabilities:									
Savings accounts	**$ 332,821**	**$ 4,347**	**1.31%**	$ 343,219	$ 2,084	0.61%	$ 327,965	$ 1,763	0.54%
Interest-bearing transaction accounts	**708,224**	**18,836**	**2.66%**	695,415	11,707	1.68%	602,575	6,875	1.14%
Time deposits	**474,693**	**18,363**	**3.87%**	411,704	11,041	2.68%	319,808	6,889	2.15%
Borrowings	**217,148**	**11,558**	**5.32%**	191,807	8,800	4.59%	134,082	6,290	4.69%
Total interest-bearing liabilities	**1,732,886**	**53,104**	**3.06%**	1,642,145	33,632	2.05%	1,384,430	21,817	1.58%
Noninterest-bearing liabilities:									
Demand deposits	**296,853**			308,025			284,638		
Other liabilities	**12,684**			11,945			8,503		
Stockholders equity	**191,732**			191,608			152,895		
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	**$ 2,234,155**			$ 2,153,723			$ 1,830,466		
Net interest income/spread		**68,709**	**2.94%**		72,178	3.42%		63,249	3.56%
Tax equivalent basis adjustment		**2,005**			1,971			1,747	
NET INTEREST INCOME		**$ 66,704**			$ 70,207			$ 61,502	
Net interest margin (C)			**3.39%**			3.73%			3.82%

(A) Includes non-accrual loans, the effect of which is to reduce the yield earned on loans, and deferred loan fees.
(B) Includes interest-bearing cash accounts.
(C) Net interest income divided by interest-earning assets.

Total interest income on a tax equivalent basis increased from $105.8 million in 2005 to $121.8 million in 2006, an increase of $16.0 million. The increase in interest income from 2005 to 2006 was primarily due to a $91.5 million increase in interest-earning assets due to growth in the loan portfolio. The increase in interest income was also due to a 55 basis point increase in the average yield on earning assets due to the increasing rate environment and to a shift in the Company s mix in earning assets from lower yielding investment securities and federal funds sold to higher yielding loans. Loans as a percent of average interest-earning assets

increased from 63% in 2005 to 70% in 2006.

The increase in interest income from $85.1 million in 2004 to $105.8 million in 2005 resulted from a $279.3 million increase in average interest-earning assets and a 33 basis point increase in the yield on average interest-earning assets reflecting an increasing rate environment and a shift in the Company s mix in earning assets from lower yielding investment securities to higher yielding loans.

Total interest expense increased from $33.6 million in 2005 to $53.1 million in 2006 as a result of an increase in average rates paid on interest-bearing liabilities from 2.05% in 2005 to 3.06% in 2006. An increase in interest-bearing liabilities of $90.7 million to $1.7 billion in 2006 also contributed to the increase in interest expense. A change in the mix of the deposits from lower costing core deposits to higher costing time deposits also had the effect of increasing the Company s cost of funds. Average savings and interest-bearing transaction accounts decreased from 63% of total interest-bearing liabilities in 2005 to 60% in 2006. Noninterest-bearing demand deposits also

decreased from $308.0 million in 2005 to $296.9 million in 2006. Higher yielding time deposits increased from 25% of interest-bearing liabilities in 2005 to 27% of total deposits in 2006.

Interest expense increased from $21.8 million in 2004 to $33.6 million in 2005 due to the increase in the volume of interest-bearing liabilities of $257.7 million and to an increase in the cost of funds of 47 basis points. The cost of funds increased as a result of an increase in market interest rates and from a shift from core deposits to time deposits.

Net Interest Margin

Net interest margin is calculated by dividing net interest income on a fully taxable equivalent basis by average interest-earning assets. The Company s net interest margin was 3.39%, 3.73% and 3.82% for 2006, 2005 and 2004, respectively. The decrease in the net interest margin from 2005 to 2006 resulted from deposits repricing faster than interest-earning assets and from a shift in interest-bearing liabilities from core deposits to time deposits and borrowings. The 55 basis point increase in the average yield on interest-earning assets and the 101 basis point increase in the average rate paid on interest-bearing liabilities resulted in a lower net interest spread and a lower net interest margin. The decrease in the net interest margin from 2004 to 2005 also resulted from interest-bearing liabilities repricing faster than interest-earning assets.

Provision for Loan and Lease Losses

In determining the provision for loan and lease losses, management considers national and local economic conditions; trends in the portfolio including orientation to specific loan types or industries; experience, ability and depth of lending management in relation to the complexity of the portfolio; adequacy and adherence to policies, procedures and practices; levels and trends in delinquencies, impaired loans and net charge-offs and the results of independent third party loan review. The provision for loan and lease losses at $1.7 million in 2006 increased from $1.6 million in 2005 due to management s evaluation of the loan portfolio. For more information, see Financial Condition Risk Elements below. Net charge-offs decreased from $5.0 million in 2005 to $1.4 million in 2006. Charge-offs in 2005 included a charge-off of $3.0 million in one of the commercial lease pools due to the settlement with the last surety company which issued surety bonds to guarantee the income stream of such lease pool. Net charge-offs as a percent of average loans outstanding decreased from 0.41% in 2005 to 0.10% in 2006. Without the impact of the commercial lease pool charge-offs, net charge-offs as a percentage of average loans outstanding would have been 0.16% for 2005.

The 2005 provision for loan and lease losses at $1.6 million decreased from $3.6 million in 2004 due to management s evaluation of the loan portfolio including its evaluation of the risk in the commercial lease pools discussed above. Net charge-offs were $6.2 million in 2004, including a $3.4 million charge-off in one of the commercial lease pools due to a settlement with one of the surety companies which issued surety bonds to guarantee the income stream of several commercial lease pools. The ratio of net charge-offs to average loans outstanding was 0.62%. Without the impact of the commercial lease pool charge-off in 2004, the ratio of net-charge-offs to average loans outstanding would have been 0.28%.

Noninterest Income

Noninterest income declined from $14.5 million in 2005 to $14.2 million in 2006 as a result of a balance sheet restructuring in fourth quarter 2006 in which we sold $97.3 million in securities at a loss of $3.3 million. As a result, losses on sales of investment securities increased from $583,000 in 2005 to $3.0 million in 2006. Offsetting the impact of the loss on the sale of securities was a $1.2 million or 12% increase in service charges on deposit accounts from 2005 to 2006 resulting from the overdraft privilege program that was implemented in May of 2005. Commissions and fees increased $521,000 or 17% to $3.6 million in 2006 due to an increase in investment services brokerage income from $284,000 in 2005 to $1.0 million in 2006. In 2005, Lakeland received commission income on the sales of investment services net of commission expense paid to the licensed sales representatives. In 2006, Lakeland employed its own sales representatives, and as a result, has recorded gross commission income received on the sales of investments and $495,000 in commission expense paid to its sales representatives in salaries and benefit expense. Partially offsetting the increase in commission income is a decrease in loan fees of $186,000. Other income increased $340,000 to $1.6 million as a result of a gain on the sale of a branch completed in first

quarter 2006. Noninterest income represented 17.5% of total revenue in 2006. (Total revenue is defined as net interest income plus non-interest income.)

Noninterest income increased $1.1 million or 9% to $14.5 million in 2005 from $13.4 million in 2004 and represented 17.2% of total revenue for 2005. A primary source of this increase in revenue was an increase in service charges on demand deposit accounts from $7.8 million in 2004 to $9.6 million in 2005, a $1.8 million or 23% increase. This increase resulted from fee income generated by Lakeland s overdraft privilege program implemented in second quarter of 2005 and a full year of income from the Newton branches. Gains (losses) on sales of securities decreased from a gain of $638,000 in 2004 to a loss of $583,000 in 2005 as a result of a decline in the market value of securities due to the interest rate environment and from a sale of securities so that Lakeland could position its portfolio to take advantage of higher yielding bonds. Income from bank owned life insurance (BOLI) increased as a result of a full year of income earned on $5.5 million in BOLI policies acquired in the Newton acquisition. Other income increased from $803,000 in 2004 to $1.2 million in 2005 as a result of leasing income.

Noninterest Expense

Noninterest expense increased $1.3 million or 2% from $53.4 million in 2005 to $54.7 million in 2006. Total salaries and benefit expense increased $2.3 million or 8% from $28.5 million in 2005 to $30.8 million in 2006. Part of this increase resulted from the termination of the Company s post-retirement benefit plan in 2005 and the reduction of a $750,000 accrual related to the post retirement benefit plan in 2005. Also impacting the increase in salary expense were normal salary and benefit increases and staffing increases including the licensed investment sales representatives referred to above. Partially offsetting the increased salary and benefit costs were declines in medical insurance expense relating to a revision of the Company s medical insurance program which resulted in a $359,000 or 11% decrease in costs from 2005 to 2006. Stationery, supplies and postage expense declined $175,000 or 10% from $1.8 million in 2005 to $1.6 million in 2006 primarily as a result of decreased supply expenses resulting from the merger of Newton into Lakeland. Legal fees declined from $811,000 in 2005 to $618,000 in 2006 resulting from a recovery of litigation costs from the Company s insurance carrier related to the purchased lease pools discussed in Note 15 of the Consolidated Financial Statements-Commitments and Contingencies-Litigation. Other expenses declined from $9.6 million in 2005 to $8.8 million in 2006, a decline of $737,000 or 8%. This decrease included a $196,000 decline in director fees from 2005 to 2006 resulting from the merger of Newton with Lakeland and from a decline in the Company s provision for unfunded lending commitments from $525,000 in 2005 to $61,000 in 2006.

Noninterest expense increased from $47.2 million in 2004 to $53.4 million in 2005, a $6.2 million or 13% increase. Salaries and benefits, the largest component of noninterest expense, increased by $3.4 million or 13%. A full year of the salaries paid to Newton s 119 employees contributed to this increase as well as normal salary and benefit increases. Occupancy expense increased from $4.4 million in 2004 to $5.4 million in 2005 as a result of expenses related to the ten branches and one administration center acquired in the Newton acquisition. Occupancy expense also included $161,000 in expenses relating to the closing of three branch offices. Furniture and equipment expenses increased $373,000 or 9% due to costs related to upgrading the Company s computer system as well as additional costs incurred from the acquisition of the Newton branches. Stationery, supplies and postage increased $254,000 or 16% from 2004 to 2005 as a result of expenses related to the Newton merger as well as expenses related to internal growth. Marketing expense increased from $1.5 million in 2004 to $1.6 million in 2005 primarily as a result of expenses related to the merger of Newton into Lakeland and to the opening of two new branches. Core deposit intangible expense increased from $810,000 in 2004 to $1.2 million in 2005 resulting from a full year s amortization of core deposit intangible acquired in the Newton acquisition. Other expenses increased from $8.1 million in 2004 to $9.6 million in 2005, a $1.4 million or 18% increase. Other expenses included a $408,000 increase in director fees which included a full year of fees related to Newton, costs related to the merger of Newton into Lakeland, and costs related to the increased size of the Company s Board of Directors in connection with the merger of NFC into the Company. Other expenses also included the establishment of a provision for unfunded lending commitments of $525,000 in 2005, a $200,000 increase in telecommunications expense, and a $139,000 increase in expenses related to personnel recruitment. The remainder of the increase in other expenses resulted from a full year of expenses related to Newton and expense related to our increased customer base.

The efficiency ratio expresses the relationship between non-interest expense (excluding other real estate expense and core deposit amortization) to total tax-equivalent revenue (excluding gains (losses) on sales of securities). In 2006, the Company s efficiency ratio on a tax equivalent basis increased to 62.3% from 59.8% in

2005. The efficiency ratio was 60.7% in 2004. The increase in the efficiency ratio from 2005 to 2006 resulted from a decline in total revenue during that period. The ratio of noninterest expense to average assets is another measure of efficiency for a financial institution. Noninterest expense as a percent of average assets decreased to 2.45% in 2006 from 2.48% in 2005 and 2.58% in 2004. The decline in this ratio reflects efficiencies realized from merging Newton into Lakeland and other expense reductions discussed above.

Income Taxes

The Company s effective income tax rate was 30.5%, 32.2% and 31.6%, in the years ended December 31, 2006, 2005 and 2004, respectively. The Company s effective tax rate declined from 2005 to 2006 because the Company s pre-tax income declined 18%, and its interest on tax-exempt securities as a percent of pre-tax income increased.

Financial Condition

Total assets increased from $2.21 billion on December 31, 2005 to $2.26 billion on December 31, 2006, an increase of $57.5 million, or 3%. Total assets at year-end 2005 increased $65.0 million or 3% from year-end 2004.

Loans

Lakeland primarily serves Northern New Jersey and the surrounding areas. Its leasing division serves a broader national market. All of its borrowers are U.S. residents or entities.

Total loans increased from $1.31 billion on December 31, 2005 to $1.59 billion on December 31, 2006, an increase of $278.7 million or 21%. The increase in loans occurred in all major loan categories. Commercial loans increased from $589.6 million to $714.5 million, an increase of $124.9 million or 21%. Leases increased from $90.1 million to $196.5 million, an increase of $106.3 million or 118%. The home equity and consumer installment portfolio increased from $302.2 million in 2005 to $315.0 million in 2006, an increase of $12.8 million or 4%. The residential real estate mortgage portfolio also increased $15.5 million or 6%. Real estate construction loans, which include both residential and commercial construction loans, increased from $68.3 million in 2005 to $87.6 million in 2006, an increase of $19.2 million or 28%. Total loans increased from $1.17 billion in 2004 to $1.31 billion in 2005, an increase of $136.3 million or 12%. The majority of the growth was in the commercial loan portfolio which increased $76.8 million or 15%.

The following table sets forth the classification of the Company s loans by major category as of December 31 for each of the last five years:

	December 31,				
	2006	**2005**	**2004**	**2003**	**2002**
	(in thousands)				
Commercial	**$ 714,496**	$ 589,646	$ 512,810	$ 330,101	$ 263,362
Leases	**196,518**	90,194	87,787	62,278	34,744
Real estate mortgage	**272,102**	256,621	217,500	178,404	161,469
Real estate construction	**87,562**	68,325	62,687	20,476	19,567
Home equity and consumer installment	**315,038**	302,236	289,920	254,039	234,259
	$ 1,585,716	$ 1,307,022	$ 1,170,704	$ 845,298	$ 713,401

The following table shows the percentage distributions of loans by category as of December 31 for each of the last five years.

	December 31,				
	2006	**2005**	**2004**	**2003**	**2002**
Commercial	**45.0%**	45.1%	43.7%	39.0%	36.9%
Leases	**12.4%**	6.9%	7.5%	7.4%	4.9%
Real estate mortgage	**17.2%**	19.7%	18.6%	21.1%	22.6%
Real estate construction	**5.5%**	5.2%	5.4%	2.4%	2.8%
Home equity and consumer installment	**19.9%**	23.1%	24.8%	30.1%	32.8%
	100.0%	100.0%	100.0%	100.0%	100.0%

At December 31, 2006, there were no concentrations of loans exceeding 10% of total loans outstanding other than loans that are secured by real estate. Loan concentrations are considered to exist when there are amounts loaned to a multiple number of borrowers engaged in similar activities which would cause them to be similarly impacted by economic or other related conditions.

The following table sets forth certain categories of loans as of December 31, 2006, in terms of contractual maturity date:

	Within one year	**After one but within five years**	**After five years**	**Total**
		(in thousands)		
Types of Loans:				
Commercial	$ 101,910	$ 102,627	$ 509,959	$ 714,496
Real Estate construction	61,100	3,154	23,308	87,562
Total	$ 163,010	$ 105,781	$ 533,267	$ 802,058
Amount of such loans with:				
Predetermined rates	$ 35,729	$ 74,947	$ 107,048	$ 217,724
Floating or adjustable rates	127,281	30,834	426,219	584,334
Total	$ 163,010	$ 105,781	$ 533,267	$ 802,058

Risk Elements

Commercial loans and leases are placed on a non-accrual status with all accrued interest and unpaid interest reversed if (a) because of the deterioration in the financial position of the borrower they are maintained on a cash basis (which means payments are applied when and as received rather than on a regularly scheduled basis), (b) payment in full of interest or principal is not expected, or (c) principal and interest has been in default for a period of 90 days or more unless the obligation is both well secured and in process of collection. Residential mortgage loans are placed on non-accrual status at the time when foreclosure proceedings are commenced except where there exists sufficient collateral to cover the defaulted principal and interest payments, and management s knowledge of the specific circumstances warrant continued accrual. Consumer loans are generally charged off when principal and interest payments are four months in arrears unless the obligations are well secured and in the process of collection. Interest thereafter on such charged-off consumer loans is taken into income when received only after full recovery of principal.

The following schedule sets forth certain information regarding the Company s non-accrual, past due and renegotiated loans and other real estate owned as of December 31, for each of the last five years:

	2006	2005	At December 31, 2004	2003	2002
			(in thousands)		
Non-performing assets:					
Non-accrual loans	**4,437**	3,907	13,017	16,653	19,985
Other real estate owned			650		
TOTAL NON-PERFORMING ASSETS	**$ 4,437**	$ 3,907	$ 13,667	$ 16,653	$ 19,985
Non-performing assets as a percent of total assets	**0.20%**	0.18%	0.64%	1.05%	1.66%
Past due loans*	**$ 876**	$ 5,127	$ 2,347	$ 1,248	$ 1,342

* Represents loans as to which payments of interest or principal are contractually past due ninety days or more, but which are currently accruing income at the contractually stated rates. A determination is made to continue accruing income on such loans only if collection of the debt is proceeding in due course and collection efforts are reasonably expected to result in repayment of the debt or in its restoration to a current status.

Non-accrual loans increased from $3.9 million at December 31, 2005 to $4.4 million on December 31, 2006. In 2005, non-accruals decreased $9.1 million from the prior year, resulting primarily from the settlement with the one remaining surety company which had guaranteed the income stream of $6.4 million of commercial lease pools. The settlement included a $3.3 million principal payment and a charge-off of the remaining $3.0 million. Other real estate owned decreased from $650,000 in 2004 to $0 in 2005 as a result of the sale of other real estate property that had been acquired in the Newton acquisition. All non-accrual loans are in various stages of litigation, foreclosure, or workout.

For 2006, the gross interest income that would have been recorded, had the loans classified at year-end as non-accrual been performing in conformance with their original loan terms, is approximately $299,000. The amount of interest income actually recorded on those loans for 2006 was $315,000. The resultant income of $16,000 for 2006 compares to losses of $338,000 and $1.3 million for 2005 and 2004, respectively.

Loans specifically evaluated are deemed impaired when, based on current information and events, it is probable that the Company will be unable to collect all amounts due according to the contractual terms of the loan agreements. Loans which are in process of collection will not be classified as impaired. A loan is not impaired during the process of collection of payment if the Company expects to collect all amounts due, including interest accrued at the contractual interest rate. All commercial loans identified as impaired in excess of $250,000 are evaluated by an independent loan review consultant. The Company aggregates consumer loans and residential mortgages for evaluation purposes.

The Company s policy concerning commercial non-accrual loans states that, except for loans which are considered to be fully collectible by virtue of collateral held and in the process of collection, loans are placed on a non-accrual status when payments are 90 days delinquent or more. It is possible for a loan to be on non-accrual status and not be classified as impaired if the balance of such loan is relatively small and, therefore, that loan has not been specifically reviewed for impairment.

Loans, or portions thereof, are charged off in the period that the loss is identified. Until such time, an allowance for loan loss is maintained for estimated losses. With regard to interest income recognition for payments received on impaired loans, as well as all non-accrual loans, the Company follows regulatory guidelines, which apply any payments to principal as long as there is doubt as to the collectibility of the loan balance.

As of December 31, 2006, based on the above criteria, the Company had impaired loans totaling $4.1 million (including $4.0 million in non-accrual loans). The impairment of these loans is based on the fair value of the underlying collateral for these loans. Based upon such evaluation, $1,351,000 has been allocated to the allowance for loan and lease losses for impairment. At December 31, 2006, the Company also had $10.8 million in loans that were rated substandard and $22,000 rated as doubtful that were not classified as non-performing or impaired.

There were no loans at December 31, 2006, other than those designated non-performing, impaired, substandard or doubtful where the Company was aware of any credit conditions of any borrowers that would indicate a strong possibility of the borrowers not complying with the present terms and conditions of repayment and which may result in such loans being included as non-accrual, past due or renegotiated at a future date.

The following table sets forth for each of the five years ended December 31, 2006, the historical relationships among the amount of loans outstanding, the allowance for loan and lease losses, the provision for loan and lease losses, the amount of loans charged off and the amount of loan recoveries:

	2006	2005	December 31, 2004 (in thousands)	2003	2002
Balance of the allowance at the beginning of the year	**$ 13,173**	$ 16,638	$ 16,899	$ 17,940	$ 8,220
Loans charged off:					
Commercial*	**1,207**	3,872	3,449	4,100	501
Leases	**90**	478	1,515	0	0
Home equity and consumer	**1,493**	1,923	1,718	1,817	926
Real estate mortgage					
Total loans charged off	**2,790**	6,273	6,682	5,917	1,427
Recoveries:					
Commercial	**728**	552	102	637	446
Leases	**83**	201	43	16	0
Home equity and consumer	**531**	499	363	350	195
Real estate mortgage	**3**	1	10	1	6
Total Recoveries	**1,345**	1,253	518	1,004	647
Net charge-offs:	**1,445**	5,020	6,164	4,913	780
Addition related to acquisitions			2,301	872	
Provision for loan and lease losses charged to operations	**1,726**	1,555	3,602	3,000	10,500
Ending balance	**$ 13,454**	$ 13,173	$ 16,638	$ 16,899	$ 17,940
Ratio of net charge-offs to average loans outstanding	**0.10%**	0.41%	0.62%	0.64%	0.12%
Ratio of allowance at end of year as a percentage of year-end total loans	**0.85%**	1.00%	1.41%	1.98%	2.49%

* Includes charge-offs of $3.0 million, $3.4 million and $2.1 million in 2005, 2004 and 2003, respectively, related to the settlement of litigation concerning the commercial lease pools which are further described in Note 15 to the Consolidated Financial Statements.

The ratio of the allowance for loan and lease losses to loans outstanding reflects management s evaluation of the underlying credit risk inherent in the loan portfolio. The determination of the adequacy of the allowance for loan and lease losses and the periodic provisioning for estimated losses included in the consolidated financial statements is the responsibility of management. The evaluation process is undertaken on a quarterly basis.

Methodology employed for assessing the adequacy of the allowance consists of the following criteria:

The establishment of reserve amounts for all specifically identified classified loans that have been designated as requiring attention by the Company or the Company s external loan review consultant.

The establishment of reserves for pools of homogeneous types of loans not subject to specific review, including 1 4 family residential mortgages, and consumer loans.

The establishment of reserve amounts for the non-classified loans in each portfolio based upon the historical average loss experience for these portfolios and management s evaluation of key factors.

Consideration is given to the results of ongoing credit quality monitoring processes, the adequacy and expertise of the Company s lending staff, underwriting policies, loss histories, delinquency trends, and the cyclical nature of economic and business conditions. Since many of the Company s loans depend on the sufficiency of collateral as a secondary source of repayment, any adverse trend in the real estate markets could affect underlying values available to protect the Company from loss.

Based upon the process employed and giving recognition to all accompanying factors related to the loan portfolio, management considers the allowance for loan and lease losses to be adequate at December 31, 2006. The preceding statement constitutes a forward-looking statement under the Private Securities Litigation Reform Act of 1995.

The following table shows how the allowance for loan and lease losses is allocated among the various types of loans that the Company has outstanding. This allocation is based on management s specific review of the credit risk of the outstanding loans in each category as well as historical trends.

	At December 31,				
	2006	**2005**	**2004**	**2003**	**2002**
	(in thousands)				
Commercial	**$ 8,327**	$ 8,578	$ 12,215	$ 13,042	$ 15,569
Leases	**1,589**	1,243	1,383	994	517
Home equity and consumer	**2,591**	2,592	2,411	2,117	1,109
Real estate construction	**648**	350	146	54	54
Real estate mortgage	**299**	410	483	692	691
	$ 13,454	$ 13,173	$ 16,638	$ 16,899	$ 17,940

Investment Securities

The Company has classified its investment securities into the available for sale and held to maturity categories pursuant to SFAS No. 115 Accounting for Certain Investments in Debt and Equity Securities.

The following table sets forth the carrying value of the Company s investment securities, both available for sale and held to maturity, as of December 31 for each of the last three years. Investment securities available for sale are stated at fair value while securities held for maturity are stated at cost, adjusted for amortization of premiums and accretion of discounts.

	December 31,		
	2006	**2005**	**2004**
		(in thousands)	
U.S. Treasury and U.S. government agencies	**$ 81,635**	$ 195,914	$ 194,378
Obligations of states and political subdivisions	**86,193**	109,862	101,023
Mortgage-backed securities	**219,369**	335,081	403,150
Equity securities	**22,025**	19,067	18,352
Other debt securities	**14,125**	10,548	28,125
	$ 423,347	$ 670,472	$ 745,028

The following table sets forth the maturity distribution and weighted average yields (calculated on the basis of the stated yields to maturity, considering applicable premium or discount), on a fully taxable equivalent basis, of investment securities available for sale as of December 31, 2006:

Available for sale	Within one year	Over one but within five years	Over five but within ten years	After ten years	Total
			(dollars in thousands)		
U.S. government agencies					
Amount	$ 12,956	$ 15,913	$ 9,723	$ 3,787	$ 42,379
Yield	4.46%	4.28%	4.64%	4.85%	4.47%
Obligations of states and political subdivisions					
Amount	3,861	14,058	9,844	1,447	29,210
Yield	5.72%	5.34%	5.55%	5.43%	5.46%
Mortgage-backed securities					
Amount		10,183	24,470	139,723	174,376
Yield	%	4.09%	4.07%	4.63%	4.52%
Other debt securities					
Amount	565	595	9,421	1,938	12,519
Yield	4.24%	4.53%	3.84%	6.33%	4.27%
Other equity securities					
Amount	22,025				22,025
Yield	0.50%	%	%	%	0.50%
Total securities					
Amount	$ 39,407	$ 40,749	$ 53,458	$ 146,895	$ 280,509
Yield	2.36%	4.60%	4.40%	4.67%	4.28%

The following table sets forth the maturity distribution and weighted average yields (calculated on the basis of the stated yields to maturity, considering applicable premium or discount), on a fully taxable equivalent basis, of investment securities held to maturity as of December 31, 2006:

Held to maturity	Within one year	Over one but within five years	Over five but within ten years	After ten years	Total
			(dollars in thousands)		
U.S. government agencies					
Amount	$ 2,000	$ 33,267	$ 3,989	$	$ 39,256
Yield	3.60%	4.18%	4.26%	%	4.15%
Obligations of states and political subdivisions					
Amount	12,194	12,633	24,137	8,019	56,983
Yield	5.48%	4.82%	5.07%	5.59%	5.18%
Mortgage-backed securities					
Amount	66	3,681	3,718	37,528	44,993
Yield	3.48%	3.96%	3.84%	5.06%	4.87%
Other debt securities					
Amount			508	1,098	1,606
Yield	0.00%	%	5.00%	5.50%	5.34%
Total securities					
Amount	$ 14,260	$ 49,581	$ 32,352	$ 46,645	$ 142,838
Yield	5.21%	4.32%	4.82%	5.16%	4.80%

Deposits

Total deposits increased from $1.798 billion on December 31, 2005 to $1.861 billion on December 31, 2006, an increase of $62.5 million, or 3%, net of a sale of an $8.0 million branch in the first quarter of 2006. The major factor driving deposit growth in 2006 was a growth in time deposits, which increased from $447.6 million at December 31, 2005 to $502.9 million at December 31, 2006, an increase of $55.3 million or 12%. The increase was primarily in certificates of deposits over $100,000, which included municipal deposits and $30.1 million in brokered deposits.

Total noninterest bearing demand accounts decreased from $312.5 million to $303.6 million, a $9.0 million or 3% decrease. Savings and interest bearing transaction accounts increased from $1.04 billion to $1.05 billion, an increase of $16.2 million or 2%. Total core deposits, which are defined as noninterest bearing deposits and savings and interest-bearing transaction accounts, increased from $1.351 billion on December 31, 2005 to $1.358 billion on December 31, 2006, an increase of $7.2 million or 1%. Total deposits in 2005 increased $71.4 million or 4% from December 31, 2004.

The average amount of deposits and the average rates paid on deposits for the years indicated are summarized in the following table:

	Year Ended December 31, 2006		Year Ended December 31, 2005		Year Ended December 31, 2004	
	Average Balance	Average Rate	Average Balance	Average Rate	Average Balance	Average Rate
	(Dollars in thousands)					
Noninterest-bearing demand deposits	**$ 296,853**	**%**	$ 308,025	%	$ 284,638	%
Interest-bearing transaction accounts	**708,224**	**2.66%**	695,415	1.68%	602,575	1.14%
Savings	**332,821**	**1.31%**	343,219	0.61%	327,965	0.54%
Time deposits	**474,693**	**3.87%**	411,704	2.68%	319,808	2.15%
Total	**$ 1,812,591**	**2.29%**	$ 1,758,363	1.41%	$ 1,534,986	1.01%

As of December 31, 2006, the aggregate amount of outstanding time deposits issued in amounts of $100,000 or more, broken down by time remaining to maturity, was as follows (in thousands):

Maturity	
Within 3 months	$ 107,921
Over 3 through 6 months	41,090
Over 6 through 12 months	53,177
Over 12 months	7,383
Total	$ 209,571

Liquidity

Liquidity measures whether an entity has sufficient cash flow to meet its financial obligations and commitments on a timely basis. The Company is liquid when its subsidiary bank has the cash available to meet the borrowing and cash withdrawal requirements of customers and the Company can pay for current and planned expenditures and satisfy its debt obligations.

Lakeland funds loan demand and operation expenses from four sources:

- Net income.
- Deposits. Lakeland can offer new products or change its rate structure in order to increase deposits. In 2006, the Company generated $70.5 million in deposit growth excluding the impact of the sale of one branch in first quarter 2006.
- Sales of securities and overnight funds. At year-end 2006, the Company had $280.5 million in securities designated available for sale.
- Overnight credit lines. Lakeland is a member of the Federal Home Loan Bank of New York (FHLB). One membership benefit is that members can borrow overnight funds. Lakeland has lines of credit totaling $200.0 million available for it to borrow from the FHLB. Lakeland also has overnight federal funds lines available for it to borrow up to $110.0 million.

The Company s management believes that its current level of liquidity is sufficient to meet its current and anticipated operational needs including current loan commitments, deposit maturities and other obligations. This constitutes a forward-looking statement under the Private Securities Litigation Reform Act of 1995. Actual results

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could differ materially from anticipated results due to a variety of factors, including uncertainties relating to general economic conditions; unanticipated decreases in deposits; changes in or failure to comply with governmental regulations; and uncertainties relating to the analysis of the Company s assessment of rate sensitive assets and rate sensitive liabilities and the extent to which market factors indicate that a financial institution such as Lakeland should match such assets and liabilities.

The following table sets forth contractual obligations and other commitments representing required and potential cash outflows as of December 31, 2006:

(dollars in thousands)	Total	Within one year	After one but within three years	After three but within five years	After five years
Minimum annual rentals or noncancellable operating leases	$ 7,847	$ 1,118	$ 1,798	$ 1,340	$ 3,591
Benefit plan commitments	2,530	35	332	370	1,793
Remaining contractual maturities of time deposits	502,879	468,526	29,967	3,282	1,104
Subordinated debentures	56,703				56,703
Loan commitments	385,789	335,425	12,811	2,820	34,733
Long-term borrowed funds	91,710	30,855	30,855	20,000	10,000
Standby letters of credit	9,754	7,978	1,776		
Total	$ 1,057,212	$ 843,937	$ 77,539	$ 27,812	$ 107,924

Interest Rate Risk

Closely related to the concept of liquidity is the concept of interest rate sensitivity (i.e., the extent to which assets and liabilities are sensitive to changes in interest rates). Interest rate sensitivity is often measured by the extent to which mismatches or gaps occur in the repricing of assets and liabilities within a given time period. Gap analysis is utilized to quantify such mismatches. A positive gap results when the amount of earning assets repricing within a given time period exceeds the amount of interest-bearing liabilities repricing within that time period. A negative gap results when the amount of interest-bearing liabilities repricing within a given time period exceeds the amount of earning assets repricing within such time period.

In general, a financial institution with a positive gap in relevant time periods will benefit from an increase in market interest rates and will experience erosion in net interest income if such rates fall. Likewise, a financial institution with a negative gap in relevant time periods will normally benefit from a decrease in market interest rates and will be adversely affected by an increase in rates. By maintaining a balanced interest rate sensitivity position, where interest rate sensitive assets roughly equal interest sensitive liabilities in relevant time periods, interest rate risk can be limited.

As a financial institution, the Company s potential interest rate volatility is a primary component of its market risk. Fluctuations in interest rates will ultimately impact the level of income and expense recorded on a large portion of the Company s assets and liabilities, and the market value of all interest-earning assets, other than those which possess a short term to maturity. Based upon the Company s nature of operations, the Company is not subject to foreign currency exchange or commodity price risk. The Company does not own any trading assets and does not have any hedging transactions in place, such as interest rate swaps and caps.

The Company s Board of Directors has adopted an Asset/Liability Policy designed to stabilize net interest income and preserve capital over a broad range of interest rate movements. This policy outlines guidelines and ratios dealing with, among others, liquidity, volatile liability dependence, investment portfolio composition, loan portfolio composition, loan-to-deposit ratio and gap analysis ratio. The Company s performance as compared to the

Asset/Liability Policy is monitored by its Board of Directors. In addition, to effectively administer the Asset/Liability Policy and to monitor exposure to fluctuations in interest rates, the Company maintains an Asset/Liability Committee, consisting of the Chief Executive Officer, Chief Financial Officer, Chief Lending Officer, Chief Retail Officer, Chief Credit Officer, certain other senior officers and certain directors. This committee meets quarterly to review the Company s financial results and to develop strategies to implement the Asset/Liability Policy and to respond to market conditions.

The Company monitors and controls interest rate risk through a variety of techniques, including use of traditional interest rate sensitivity analysis (also known as gap analysis) and an interest rate risk management model. With the interest rate risk management model, the Company projects future net interest income, and then estimates the effect of various changes in interest rates and balance sheet growth rates on that projected net interest income. The Company also uses the interest rate risk management model to calculate the change in net portfolio value over a range of interest rate change scenarios. Traditional gap analysis involves arranging the Company s interest-earning assets and interest-bearing liabilities by repricing periods and then computing the difference (or interest rate sensitivity gap) between the assets and liabilities that are estimated to reprice during each time period and cumulatively through the end of each time period.

Both interest rate sensitivity modeling and gap analysis are done at a specific point in time and involve a variety of significant estimates and assumptions. Interest rate sensitivity modeling requires, among other things, estimates of how much and when yields and costs on individual categories of interest-earning assets and interest-bearing liabilities will respond to general changes in market rates, future cash flows and discount rates.

Gap analysis requires estimates as to when individual categories of interest-sensitive assets and liabilities will reprice, and assumes that assets and liabilities assigned to the same repricing period will reprice at the same time and in the same amount. Gap analysis does not account for the fact that repricing of assets and liabilities is discretionary and subject to competitive and other pressures.

The following table sets forth the estimated maturity/repricing structure of the Company s interest-earning assets and interest-bearing liabilities at December 31, 2006. Except as stated below, the amounts of assets or liabilities shown which reprice or mature during a particular period were determined in accordance with the contractual terms of each asset or liability. The majority of interest-bearing demand deposits and savings deposits are assumed to be core deposits, or deposits that will generally remain at the Company regardless of market interest rates. Therefore, 13% of the core interest-bearing deposits, 20% of core savings deposits and 35% of money market deposit accounts are shown as maturing or repricing within three months. The remainder is divided between the after 1 but within 5 years column and the after 5 years column. Interest-bearing transaction accounts held by states and municipalities are seen to be more sensitive than personal interest-bearing transaction accounts. Therefore, 75% of public interest-bearing transaction accounts are shown as repricing within three months. The table does not assume any prepayment of fixed-rate loans.

The table does not necessarily indicate the impact of general interest rate movements on the Company s net interest income because the repricing of certain categories of assets and liabilities, for example, prepayments of loans and withdrawal of deposits, is beyond the Company s control. As a result, certain assets and liabilities indicated as repricing within a stated period may in fact reprice at different times and at different rate levels.

December 31, 2006	Maturing or Repricing Within three months	After 3 months but within 1 year	After 1 but within 5 years	After 5 Years	Total
			(dollars in thousands)		
Interest-earning assets:					
Loans	$ 306,508	$ 154,685	$ 719,345	$ 411,106	$ 1,591,644
Investment securities	44,815	63,863	212,781	101,888	423,347
Interest-bearing cash accounts	32,076				32,076
Total interest-earning assets	383,399	218,548	932,126	512,994	2,047,067
Interest-bearing liabilities:					
Deposits:					
Interest-bearing demand	283,579		273,321	174,898	731,798
Savings accounts	64,478		114,628	143,286	322,392
Time deposits	197,041	271,579	33,155	1,104	502,879
Total interest-bearing deposits	545,098	271,579	421,104	319,288	1,557,069
Borrowings:					
Fed funds purchased and securities sold under agreements to repurchase	41,061				41,061
Long-term debt	405	50,450	40,855		91,710
Subordinated debentures			30,000	26,703	56,703
Total borrowings	41,466	50,450	70,855	26,703	189,474
Total interest-bearing liabilities	586,564	322,029	491,959	345,991	1,746,543
Interest rate sensitivity gap	$ (203,165)	$ (103,481)	$ 440,167	$ 167,003	$ 300,524
Cumulative rate sensitivity gap	$ (203,165)	$ (306,646)	$ 133,521	$ 300,524	

Changes in estimates and assumptions made for interest rate sensitivity modeling and gap analysis could have a significant impact on projected results and conclusions. Therefore, these techniques may not accurately reflect the impact of general interest rate movements on the Company s net interest income or net portfolio value.

Because of the limitations in the gap analysis discussed above, members of the Company s Asset/Liability Committee believe that the interest sensitivity modeling more accurately reflects the effects and exposure to changes in interest rates. Net interest income simulation considers the relative sensitivities of the balance sheet including the effects of interest rate caps on adjustable rate mortgages and the relatively stable aspects of core deposits. As such, net interest income simulation is designed to address the probability of interest rate changes and the behavioral response of the balance sheet to those changes. Market Value of Portfolio Equity represents the fair value of the net present value of assets, liabilities and off-balance-sheet items.

The starting point (or base case) for the following table is an estimate of the Company s net portfolio value at December 31, 2006 using current discount rates, and an estimate of net interest income for 2007 assuming that both interest rates and the Company s interest-sensitive assets and liabilities remain at December 31, 2006 levels. The information provided for the net portfolio value assumes fluctuations or rate shocks of plus 200 basis points and minus 200 basis points. Rate shocks assume that current interest rates change immediately. The information provided for net interest income for 2007 assumes that changes in interest rates of plus 200 basis points and minus 200 basis points change gradually in equal increments over the twelve month period. The information set forth in the following table is based on significant estimates and assumptions, and constitutes a forward-looking statement under the Private Securities Litigation Reform Act of 1995.

Rate Scenario	Net Portfolio Value at December 31, 2006 Amount	Net Portfolio Value at December 31, 2006 Percent Change From Base Case	Net interest income for 2007 Amount	Net interest income for 2007 Percent Change From Base Case
	(dollars in thousands)			
+200 basis points	$ 273,907	(12.8)%	$ 66,035	(4.9)%
Base Case	314,189	%	69,403	%
-200 basis points	329,554	4.9%	72,665	4.7%

Capital Resources

Stockholders equity increased $7.7 million to $199.5 million at December 31, 2006, from $191.8 million at December 31, 2005, reflecting net income during the year of $17.0 million, cash dividends to stockholders of $8.5 million, other comprehensive income of $1.8 million, purchases of treasury stock of $3.1 million and a net change from the exercise of stock options of $622,000.

Book value per share (total stockholders equity divided by the number of shares outstanding) increased from $8.65 on December 31, 2005 to $9.04 on December 31, 2006 as a result of increased income and a decrease in shares outstanding resulting from the buyback of shares under the stock repurchase program. Book value per share was $8.53 on December 31, 2004.

The FDIC s risk-based capital policy statement imposes a minimum capital standard on insured banks. The minimum ratio of risk-based capital to risk-weighted assets (including certain off-balance sheet items, such as standby letters of credit) is 8%. At least half of the total capital is to be comprised of common stock equity and qualifying perpetual preferred stock, less goodwill (Tier I capital). The remainder (Tier II capital) may consist of mandatory convertible debt securities, qualifying subordinated debt, other preferred stock and a portion of the allowance for loan and lease losses. The Federal Reserve Board has adopted a similar risk-based capital guideline for the Company which is computed on a consolidated basis.

In addition, the bank regulators have adopted minimum leverage ratio guidelines (Tier I capital to average quarterly assets, less goodwill) for financial institutions. These guidelines provide for a minimum leverage ratio of 3% for financial institutions that meet certain specified criteria, including that they have the highest regulatory rating. All other holding companies are required to maintain a leverage ratio of 3% plus an additional cushion of at least 100 to 200 basis points.

The following table reflects capital ratios of the Company and Lakeland as of December 31, 2006 and 2005:

Capital Ratios:	Tier 1 Capital to Total Average Assets Ratio December 31, 2006	Tier 1 Capital to Total Average Assets Ratio December 31, 2005	Tier 1 Capital to Risk-Weighted Assets Ratio December 31, 2006	Tier 1 Capital to Risk-Weighted Assets Ratio December 31, 2005	Total Capital to Risk-Weighted Assets Ratio December 31, 2006	Total Capital to Risk-Weighted Assets Ratio December 31, 2005
The Company	**7.51%**	7.49%	**10.13%**	11.51%	**10.96%**	12.47%
Lakeland Bank	**6.85%**	6.86%	**9.24%**	10.57%	**10.07%**	11.53%
Well capitalized institution under FDIC Regulations	**5.00%**	5.00%	**6.00%**	6.00%	**10.00%**	10.00%

Recent Accounting Pronouncements

As further discussed in Note 1 Stock Based Compensation, the Company adopted SFAS No. 123(R), Share-Based Payments on January 1, 2006. SFAS No. 123(R) requires the Company to recognize compensation expense for all share-based payments made to employees based on the fair value of the share-based payment on the date of the grant. The Company elected to use a modified method of prospective application. Prior to adopting SFAS No. 123(R), the Company followed the provisions of SFAS No. 123, Accounting for Stock-Based Compensation. SFAS No. 123 permitted entities to account for employee stock options and similar equity instruments under Accounting Principles Board (APB) Opinion No. 25, Accounting for Stock Issued for Employees. Under SFAS No. 123, entities were required to make pro forma disclosures of net income and earnings per share, as if the fair-value based method of accounting defined in SFAS No. 123 had been applied.

On May 13, 2005, the Company accelerated the vesting of 483,812 stock options, representing all unvested stock options on such date which had exercise prices in excess of the market value of the Company s common stock on May 13, 2005. The Company s decision to accelerate the vesting of these options was part of a review by the Board of Directors of the Company s incentive compensation program and upcoming changes in the accounting for stock options. Compensation expense that would have been recorded absent the accelerated vesting was approximately $1.3 million net of taxes, $644,000 of which would have been recorded in 2006. In December 2005, the Company granted options to purchase 164,308 shares of common stock to key employees at an exercise price of $14.94 per share. These options vested immediately. Compensation expense that would have been recorded net of taxes was approximately $774,000.

Because the Company s options are fully vested, there was no impact on compensation expense or net income for 2006.

In December 2006, the Company issued 36,028 shares of restricted stock at a market value of $14.65 per share. These shares vest over a four year period. The expected compensation expense will be $124,000 a year for the next four years.

In July 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes (FIN 48). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise s financial statements in accordance with Statement of Financial Accounting Standards No. 109, Accounting for Income Taxes. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006. The Company is currently evaluating the impact the adoption of FIN 48 will have on its consolidated financial statements.

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

In September 2006, 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) . This statement requires balance sheet recognition of the overfunded or underfunded status of pension and postretirement benefit plans. Under SFAS No. 158, actuarial gains and losses, prior service costs or credits, and any remaining transition assets or obligations that have not been recognized under previous accounting standards must be recognized in Accumulated Other Comprehensive Income, net of tax effects, until they are amortized as a component of net periodic benefit cost. In addition, the measurement date, the date at which plan assets and benefit obligations are measured, must be a company s fiscal year end. The Company adopted SFAS No. 158 on December 31, 2006 and recorded a liability of $526,000, a deferred tax asset of $184,000, and an other comprehensive loss of $342,000 upon adoption.

In September 2006, the SEC staff issued Staff Accounting Bulletin No. 108, Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements. SAB 108 was issued to provide consistency between how registrants quantify financial statement misstatements.

SAB 108 established an approach that requires quantification of financial statement misstatements based on the effects of the misstatement on each of a company s financial statements and the related financial statement disclosures. This approach is commonly referred to as the dual approach because it requires quantification of errors under both the roll-over and iron curtain methods.

The Company evaluated the impact that the adoption of SAB 108 had on its financial statements using both the iron curtain method and the rollover method to evaluate misstatements and did not find any items requiring an adjustment.

In September 2006, the Financial Accounting Standards Board ratified a consensus opinion reached by the Emerging Issues Task Force on Issue 06-4, Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements, (EITF 06-4) which requires employers that enter into endorsement split-dollar life insurance arrangements that provide an employee with a postretirement benefit to recognize a liability for the future benefits promised based on the substantive agreement made with the employee. Whether the accrual is based on a death benefit or on the future cost of maintaining the insurance would depend on what the employer has effectively agreed to provide during the employee s retirement. The purchase of an endorsement-type life insurance policy does not qualify as a settlement of the liability.

The consensus in EITF 06-4 is effective for fiscal years beginning after December 15, 2007. The Company intends to adopt EITF 06-4 effective January 1, 2008. The Company is currently evaluating the impact this guidance will have on the Company s financial position and results of operations.

In September 2006, the FASB ratified the consensus reached by the Emerging Issues Task Force in Issue 06-5, Accounting for Purchases of Life Insurance Determining the Amount That Could Be Realized in Accordance with FASB Technical Bulletin No. 85-4, Accounting for Purchases of Life Insurance (EITF 06-5). EITF 06-5 is effective for the fiscal years beginning after December 15, 2006. The Company adopted this EITF effective January 1, 2007. EITF 06-5 pertains to companies with life insurance policies, including Bank Owned Life Insurance, and further defines the amount that could be realized under an insurance contract that should be booked as an asset on a company s balance sheet. The Company is currently evaluating the impact this guidance will have on the Company s financial position and results of operations.

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159, The Fair Value Option for Financial Assets and Financial Liabilities-Including an amendment of FASB Statement No. 115. SFAS No. 159 permits entities to choose to measure many financial instruments and certain other items at fair value. SFAS No. 159 is effective as of the beginning of an entity s first fiscal year that begins after November 15, 2007 but earlier adoption is permitted provided the entity also elects to apply the provisions of SFAS No. 157 during the same time period.

Effects of Inflation

The impact of inflation, as it affects banks, differs substantially from the impact on non-financial institutions. Banks have assets which are primarily monetary in nature and which tend to move with inflation. This is especially true for banks with a high percentage of rate sensitive interest-earning assets and interest-bearing liabilities. A bank can further reduce the impact of inflation with proper management of its rate sensitivity gap. This gap represents the difference between interest rate sensitive assets and interest rate sensitive liabilities. Lakeland attempts to structure its assets and liabilities and manages its gap to protect against substantial changes in interest rate scenarios, in order to minimize the potential effects of inflation.

ITEM 7A - Quantitative and Qualitative Disclosures About Market Risk

See Management s Discussion and Analysis of Financial Condition and Results of Operations.

ITEM 8 Financial Statements and Supplementary Data

Lakeland Bancorp, Inc. and Subsidiaries

CONSOLIDATED BALANCE SHEETS

	December 31, 2006	2005
	(dollars in thousands)	
ASSETS		
Cash	**$ 47,888**	$ 42,639
Interest-bearing deposits due from banks	**32,076**	10,176
Total cash and cash equivalents	**79,964**	52,815
Investment securities available for sale	**280,509**	515,903
Investment securities held to maturity; fair value of $140,564 in 2006 and $151,637 in 2005	**142,838**	154,569
Loans, net of deferred fees	**1,591,644**	1,312,767
Less: allowance for loan and lease losses	**13,454**	13,173
Net loans	**1,578,190**	1,299,594
Premises and equipment net	**32,072**	32,428
Accrued interest receivable	**8,509**	8,851
Goodwill	**87,111**	87,111
Other identifiable intangible assets	**4,942**	6,284
Bank owned life insurance	**36,774**	35,479
Other assets	**12,664**	12,999
TOTAL ASSETS	**$ 2,263,573**	$ 2,206,033
LIABILITIES AND STOCKHOLDERS EQUITY		
LIABILITIES:		
Deposits:		
Noninterest bearing	**$ 303,558**	$ 312,529
Savings and interest-bearing transaction accounts	**1,054,190**	1,038,038
Time deposits under $100 thousand	**293,308**	293,293
Time deposits $100 thousand and over	**209,571**	154,300
Total deposits	**1,860,627**	1,798,160
Federal funds purchased and securities sold under agreements to repurchase	**41,061**	103,199
Long-term debt	**91,710**	45,061
Subordinated debentures	**56,703**	56,703
Other liabilities	**13,972**	11,129
TOTAL LIABILITIES	**2,064,073**	2,014,252
Commitments and contingencies		
Stockholders equity:		
Common stock, no par value; authorized shares, 40,000,000; issued shares, 23,563,463 at December 31, 2006 and 23,564,454 at December 31, 2005; outstanding shares, 22,057,322 at December 31, 2006 and 22,178,020 at December 31, 2005	**242,661**	226,322
Accumulated Deficit	**(17,526)**	(9,514)
Treasury stock, at cost, 1,506,141 in 2006 and 1,386,434 in 2005	**(22,565)**	(20,176)
Accumulated other comprehensive loss	**(3,070)**	(4,851)
TOTAL STOCKHOLDERS EQUITY	**199,500**	191,781

TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	**$ 2,263,573**	$ 2,206,033

See accompanying notes to consolidated financial statements

Lakeland Bancorp, Inc. and Subsidiaries

CONSOLIDATED INCOME STATEMENTS

	Years Ended December 31,		
	2006	2005	2004
	(In thousands, except per share data)		
INTEREST INCOME			
Loans and fees	**$ 94,909**	$ 76,388	$ 58,952
Federal funds sold and interest-bearing deposits with banks	**1,060**	764	286
Taxable investment securities	**20,115**	23,027	20,835
Tax-exempt investment securities	**3,724**	3,660	3,246
TOTAL INTEREST INCOME	**119,808**	103,839	83,319
INTEREST EXPENSE			
Deposits	**41,546**	24,832	15,527
Federal funds purchased and securities sold under agreements to repurchase	**4,297**	3,026	589
Long-term debt	**7,261**	5,774	5,701
TOTAL INTEREST EXPENSE	**53,104**	33,632	21,817
NET INTEREST INCOME	**66,704**	70,207	61,502
Provision for loan and lease losses	**1,726**	1,555	3,602
NET INTEREST INCOME AFTER PROVISION FOR LOAN AND LEASE LOSSES	**64,978**	68,652	57,900
NONINTEREST INCOME			
Service charges on deposit accounts	**10,792**	9,633	7,823
Commissions and fees	**3,595**	3,074	3,001
Gains (losses) on the sales of investment securities	**(2,995)**	(583)	638
Income on bank owned life insurance	**1,237**	1,210	1,134
Other income	**1,551**	1,211	803
TOTAL NONINTEREST INCOME	**14,180**	14,545	13,399
NONINTEREST EXPENSE			
Salaries and employee benefits	**30,839**	28,511	25,128
Net occupancy expense	**5,386**	5,416	4,365
Furniture and equipment	**4,657**	4,453	4,080
Stationery, supplies and postage	**1,631**	1,806	1,552
Legal fees	**618**	811	1,655
Marketing expense	**1,573**	1,625	1,473
Core deposit intangible amortization	**1,196**	1,212	810
Other expenses	**8,821**	9,558	8,122
TOTAL NONINTEREST EXPENSE	**54,721**	53,392	47,185
Income before provision for income taxes	**24,437**	29,805	24,114
Provision for income taxes	**7,460**	9,584	7,619
NET INCOME	**$ 16,977**	$ 20,221	$ 16,495
PER SHARE OF COMMON STOCK:			
Basic earnings	**$ 0.77**	$ 0.90	$ 0.81

Diluted earnings	**$ 0.77**	$ 0.89	$ 0.80
Cash dividends	**$ 0.39**	$ 0.37	$ 0.36

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

	Years Ended December 31,		
	2006	**2005**	**2004**
		(in thousands)	
NET INCOME	**$ 16,977**	$ 20,221	$ 16,495
OTHER COMPREHENSIVE INCOME NET OF TAX:			
Unrealized securities gains (losses) arising during period	**247**	(5,587)	678
Less: reclassification for gains (losses) included in net income	**(2,073)**	(396)	436
Change in pension liabilities, net	**(539)**		
Other Comprehensive Income (Loss)	**1,781**	(5,191)	242
TOTAL COMPREHENSIVE INCOME	**$ 18,758**	$ 15,030	$ 16,737

See accompanying notes to consolidated financial statements

Lakeland Bancorp, Inc. and Subsidiaries

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS EQUITY

For the years ended December 31, 2006, 2005 and 2004

	Common stock				Accumulated Other Comprehensive	
	Number of Shares	Amount	Accumulated Deficit	Treasury Stock	Income (Loss)	Total
			(dollars in thousands)			
BALANCE DECEMBER 31, 2003	16,483,551	$ 131,116	($ 12,980)	($ 7,283)	$ 98	$ 110,951
Net Income 2004			16,495			16,495
Other comprehensive income, net of tax					242	242
Exercise of stock options		264		818		1,082
Shares issued for the purchase of Newton Financial Corp.	4,891,019	77,553				77,553
Cash dividends			(7,362)			(7,362)
Purchase of treasury stock				(4,413)		(4,413)
BALANCE DECEMBER 31, 2004	21,374,570	208,933	(3,847)	(10,878)	340	194,548
Net Income 2005			20,221			20,221
Other comprehensive loss, net of tax					(5,191)	(5,191)
Exercise of stock options		(192)		800		608
Stock dividend	1,067,767	17,581	(17,581)			
Cash dividends			(8,307)			(8,307)
Purchase of treasury stock				(10,098)		(10,098)
BALANCE DECEMBER 31, 2005	22,442,337	226,322	(9,514)	(20,176)	(4,851)	191,781
Net Income 2006			16,977			16,977
Other comprehensive income, net of tax and reclassification adjustments					1,781	1,781
Exercise of stock options		(133)		755		622
Stock dividend	1,121,126	16,472	(16,472)			
Cash dividends			(8,517)			(8,517)
Purchase of treasury stock				(3,144)		(3,144)
BALANCE DECEMBER 31, 2006	23,563,463	$ 242,661	$ (17,526)	$ (22,565)	$ (3,070)	$ 199,500

See accompanying notes to consolidated financial statements

Lakeland Bancorp, Inc. and Subsidiaries

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Years Ended December 31,		
	2006	**2005**	**2004**
		(in thousands)	
CASH FLOWS FROM OPERATING ACTIVITIES			
Net income	**$ 16,977**	$ 20,221	$ 16,495
Adjustments to reconcile net income to net cash provided by operating activities:			
Net amortization of premiums, discounts and deferred loan fees and costs	**594**	1,281	3,166
Depreciation and amortization	**3,512**	3,532	3,189
Amortization of intangible assets	**1,196**	1,212	810
Provision for loan and lease losses	**1,726**	1,555	3,602
Provision for losses on other real estate			200
(Gains) losses on sales of securities	**2,995**	583	(637)
Gain on sale of branch	**(361)**		
Deferred income tax (benefit)	**(740)**	1,524	1,330
(Increase) decrease in other assets	**(641)**	(1,851)	39
Increase in other liabilities	**2,084**	1,428	661
NET CASH PROVIDED BY OPERATING ACTIVITIES	**27,342**	29,485	28,855
CASH FLOWS FROM INVESTING ACTIVITIES			
Cash equivalents in excess of cash paid for business acquired			1,067
Proceeds from repayments on and maturity of securities:			
Available for sale	**86,977**	122,326	153,537
Held to maturity	**29,910**	32,326	43,244
Proceeds from sales of securities:			
Available for sale	**178,124**	80,380	32,708
Held to maturity		715	
Purchase of securities:			
Available for sale	**(29,908)**	(146,359)	(171,400)
Held to maturity	**(18,378)**	(25,058)	(122,965)
Purchase of Asset Based Lending portfolio			(25,524)
Net increase in loans	**(280,137)**	(141,340)	(103,618)
Proceeds from sale of branch, net	**(7,326)**		
Proceeds from dispositions of premises and equipment	**51**	135	44
Capital expenditures	**(3,400)**	(4,345)	(3,682)
Net decrease in other real estate owned		650	
NET CASH USED IN INVESTING ACTIVITIES	**(44,087)**	(80,570)	(196,589)
CASH FLOWS FROM FINANCING ACTIVITIES			
Net increase in deposits	**70,459**	71,356	134,229
Increase (decrease) in federal funds purchased and securities sold under agreements to repurchase	**(62,138)**	(7,631)	59,407
Proceeds from long-term debt	**50,000**	10,000	
Repayments of long-term debt	**(3,351)**	(7,227)	(5,521)
Purchase of treasury stock	**(3,144)**	(10,098)	(4,413)
Exercise of stock options	**519**	461	656
Excess tax benefits	**66**		
Dividends paid	**(8,517)**	(8,307)	(7,362)
NET CASH PROVIDED BY FINANCING ACTIVITIES	**43,894**	48,554	176,996
Net increase (decrease) in cash and cash equivalents	**27,149**	(2,531)	9,262

Cash and cash equivalents, beginning of year	**52,815**	55,346	46,084
CASH AND CASH EQUIVALENTS, END OF YEAR	**$ 79,964**	$ 52,815	$ 55,346

See accompanying notes to consolidated financial statements

Lakeland Bancorp, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - SUMMARY OF ACCOUNTING POLICIES

Lakeland Bancorp, Inc. (the Company) is a bank holding company whose principal activity is the ownership and management of its wholly owned subsidiary, Lakeland Bank (Lakeland). The Newton Trust Company (Newton), was merged into Lakeland on November 4, 2005 and Community State Bank (CSB) was merged into Lakeland on August 25, 2003. Lakeland operates under a state bank charter and provides full banking services and, as a state bank, is subject to regulation by the New Jersey Department of Banking and Insurance. Lakeland generates commercial, mortgage and consumer loans and receives deposits from customers located primarily in Northern New Jersey. Lakeland also provides securities brokerage services, including mutual funds and variable annuities.

Lakeland operates as a commercial bank offering a wide variety of commercial loans and leases and, to a lesser degree, consumer credits. Its primary future strategic aim is to establish a reputation and market presence as the small and middle market business bank in its principal markets. Lakeland funds its loans primarily by offering time, savings and money market, and demand deposit accounts to both commercial enterprises and individuals. Additionally, it originates residential mortgage loans, and services such loans which are owned by other investors. Lakeland also has a leasing division which provides equipment lease financing primarily to small and medium sized business clients and an asset based lending department which specializes in utilizing particular assets to fund the working capital needs of borrowers.

The Company and Lakeland are subject to regulations of certain state and federal agencies and, accordingly, are periodically examined by those regulatory authorities. As a consequence of the extensive regulation of commercial banking activities, Lakeland s business is particularly susceptible to being affected by state and federal legislation and regulations.

Basis of Financial Statement Presentation

The accounting and reporting policies of the Company and Lakeland and its subsidiaries conform with accounting principles generally accepted in the United States of America and predominant practices within the banking industry. The consolidated financial statements include the accounts of the Company, Lakeland, Lakeland Investment Corp. and Lakeland NJ Investment Corp. All intercompany balances and transactions have been eliminated.

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements. These estimates and assumptions also affect reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates. Significant estimates implicit in these financial statements are as follows.

The principal estimates that are particularly susceptible to significant change in the near term relate to the allowance for loan and lease losses and the evaluation of goodwill impairment.

The evaluation of the adequacy of the allowance for loan and lease losses includes, among other factors, an analysis of historical loss rates, by category, applied to current loan totals. However, actual losses may be higher or lower than historical trends, which vary. Actual losses on specified problem loans, which also are provided for in the evaluation, may vary from estimated loss percentages, which are established based upon a limited number of potential loss classifications.

The Company provides disclosures under Statement of Financial Accounting Standards (SFAS) No. 131, Disclosures about Segments of an Enterprise and Related Information. Operating segments are components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and assess performance.

The Company has one operating segment and accordingly one reportable segment, Community Banking. All of the Company s activities are interrelated, and each activity is dependent and assessed based on how each of the activities of the Company supports the others. For example, commercial lending is dependent upon the ability of Lakeland to fund itself with retail deposits and other borrowings and to manage interest rate and credit risk. This situation is also similar for consumer and residential mortgage lending. Accordingly, all significant operating decisions are based upon analysis of the Company as one operating segment or unit.

In September 2006, the SEC staff issued Staff Accounting Bulletin No. 108, Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements. SAB 108 was issued to provide consistency between how registrants quantify financial statement misstatements.

SAB 108 established an approach that requires quantification of financial statement misstatements based on the effects of the misstatement on each of a company s financial statements and the related financial statement disclosures. This approach is commonly referred to as the dual approach because it requires quantification of errors under both the roll-over and iron curtain methods.

The Company evaluated the impact that the adoption of SAB 108 had on its financial statements using both the iron curtain method and the rollover method to evaluate misstatements and did not find any items requiring an adjustment.

Investment Securities

The Company accounts for its investment securities in accordance with SFAS No. 115, Accounting for Certain Investments in Debt and Equity Securities. Investments in securities are classified in one of three categories: held to maturity, trading, or available for sale. Investments in debt and equity securities, for which management has both the ability and intent to hold to maturity, are carried at cost, adjusted for the amortization of premiums and accretion of discounts computed by the interest method. Investments in debt and equity securities, which management believes may be sold prior to maturity due to changes in interest rates, prepayment risk, liquidity requirements, or other factors, are classified as available for sale. Net unrealized gains and losses for such securities, net of tax effect, are reported as other comprehensive income (loss) and excluded from the determination of net income. The Company does not engage in security trading. Gains or losses on disposition of investment securities are based on the net proceeds and the adjusted carrying amount of the securities sold using the specific identification method.

In November 2005, FASB Staff Position 115-1 and 124-1, The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments (FSP 115-1) was issued. FSP 115-1 replaced the guidance in paragraphs 10 18 of EITF Issue 03-1 with references to existing other-than-temporary impairment guidance, such as SFAS No. 115, Accounting for Certain Investments in Debt and Equity Securities, Staff Accounting Bulletin 59, Accounting for Noncurrent Marketable Equity Securities, and APB Opinion 18, The Equity Method of Accounting for Investments in Common Stock. FSP 115-1 codified the guidance set forth in EITF Topic D-44 and clarified that an investor should recognize an impairment loss no later than when the impairment is considered other-than-temporary, even if a decision to sell has not been made. FSP 115-1 also includes language from EITF Issue 03-1 regarding the accounting for debt securities subsequent to an other-than-temporary impairment.

The Company has evaluated its investments under FSP 115-1. Because it has concluded that none of its securities have impairments that are other-than-temporary, the impact of these pronouncements have not had a material impact on the Company s financial statements.

Loans and Allowance for Loan and Lease Losses

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are stated at the amount of unpaid principal and are net of unearned discount, unearned loan fees and an allowance for loan and lease losses. The allowance for loan and lease losses is established through a provision for loan and lease losses charged to expense. Loan principal considered to be uncollectible by management is charged against the allowance for loan and lease losses. The allowance is an amount that management believes will be adequate to absorb losses on existing loans that may become uncollectible based upon an evaluation of known and inherent risks in the loan portfolio. The evaluation takes into consideration such factors as changes in the nature and size of the loan portfolio, overall portfolio quality, specific problem loans, and current economic conditions which may affect the borrowers ability to pay. The evaluation also details historical losses by loan category, the resulting loss rates for which are projected at current loan total amounts. Loss estimates for specified problem loans are also detailed.

Interest income is accrued as earned on a simple interest basis. Accrual of interest is discontinued on a loan when management believes, after considering economic and business conditions and collection efforts, that the borrower s financial condition is such that collection of interest is doubtful. When a loan is placed on such non-accrual status, all accumulated accrued interest receivable is reversed out of current period income. Commercial loans 90 days or more past due and still accruing interest must have both principal and accruing interest adequately secured and must be in the process of collection. Residential mortgage loans are placed on non-accrual status at the time when foreclosure proceedings are commenced except where there exists sufficient collateral to cover the defaulted principal and interest payments, and management s knowledge of the specific circumstances warrant continued accrual. Consumer loans are generally charged off when principal and interest payments are four months in arrears unless the obligations

are well secured and in the process of collection. Interest thereafter on such charged-off consumer loans is taken into income when received only after full recovery of principal.

Impairment of loans is measured based on the present value of expected future cash flows discounted at the loan s effective interest rate, except that as a practical expedient, Lakeland may measure impairment based on a loan s observable market price, or the fair value of the collateral if the loan is collateral-dependent. Regardless of the measurement method, a creditor must measure impairment based on the fair value of the collateral when the creditor determines that foreclosure is probable.

Bank Premises and Equipment

Bank premises and equipment, including leasehold improvements, are stated at cost less accumulated depreciation. Depreciation expense is computed on the straight-line method over the estimated useful lives of the assets. Leasehold improvements are depreciated over the shorter of the estimated useful lives of the improvements or the terms of the related leases.

Other Real Estate Owned

Other real estate owned (OREO), representing property acquired through foreclosure, is carried at the lower of the principal balance of the secured loan or fair value less estimated disposal costs of the acquired property. Costs relating to holding the assets are charged to expense. An allowance for OREO has been established, through charges to OREO expense, to maintain properties at the lower of cost or fair value less estimated costs to sell. Operating results of OREO, including rental income, operating expenses and gains and losses realized from the sale of properties owned, are included in other expenses.

Mortgage Servicing

The Company performs various servicing functions on loans owned by others. A fee, usually based on a percentage of the outstanding principal balance of the loan, is received for these services. At December 31, 2006 and 2005, Lakeland was servicing approximately $15.4 million and $17.1 million, respectively, of loans for others.

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

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

In March 2006, the FASB issued SFAS No 156, Accounting for Servicing of Financial Assets an amendment of FASB Statement No. 140. (SFAS No. 156). This statements amends SFAS No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities with respect to the accounting for separately recognized servicing assets and servicing liabilities. Among other requirements, SFAS No. 156 requires an entity to recognize a servicing asset or servicing liability each time it undertakes an obligation to service a financial asset by entering into a servicing contract in certain situations. SFAS No. 156 is effective for a company s first fiscal year beginning after September 15, 2006. The Company adopted SFAS No. 156 effective January 1, 2007. The adoption of this statement did not have a material impact on the Company s financial position or results of operations.

Restrictions On Cash And Due From Banks

Lakeland is required to maintain reserves against customer demand deposits by keeping cash on hand or balances with the Federal Reserve Bank of New York in a noninterest bearing account. The amounts of those reserves and cash balances at December 31, 2006 and 2005 were approximately $2.6 million and $2.9 million, respectively.

Earnings Per Share

The Company follows the provisions of SFAS No. 128, Earnings Per Share, which requires presentation of basic and diluted earnings per share in conjunction with the disclosure of the methodology used in computing such earnings per share. Basic earnings per share excludes dilution and is computed by dividing income available to common shareholders by the weighted average common shares outstanding during the period. Diluted earnings per share takes into account the potential dilution that could occur if securities or other contracts to issue common stock were exercised and converted into common stock. Unless otherwise indicated, all weighted average, actual shares or per share information in the financial statements have been adjusted retroactively for the effect of stock dividends.

Employee Benefit Plans

The Company has certain employee benefit plans covering substantially all employees. The Company accrues such costs as incurred.

The Company adopted SFAS No. 158, Employers Accounting for Defined Benefit Pension and Other Post Retirement Plans-an amendment of FASB Statements No. 87, 88, 106 and 132(R), as of December 31, 2006. This statement requires balance sheet recognition of the overfunded or underfunded status of pension and postretirement benefit plans. Under SFAS No. 158, actuarial gains and losses, prior service costs or credits, and any remaining transition assets or obligations that have not been recognized under previous accounting standards must be recognized in Accumulated Other Comprehensive Income, net of tax effects, until they are amortized as a component of net periodic benefit cost. In addition, the measurement date, the date at which plan assets and benefit obligations are measured, must be a company s fiscal year end as of December 31, 2007. The Company adopted SFAS No. 158 on December 31, 2006 for the Newton pension plan and the Director s Retirement Plan and recorded a liability of $526,000, a deferred tax asset of $184,000 and an other comprehensive loss of $342,000 upon adoption.

Stock-Based Compensation

The Company established the 2000 Equity Compensation Program which authorizes the granting of incentive stock options and supplemental stock options to employees of the Company which includes those employees serving as officers and directors of the Company. The plan authorized options to purchase up to 2,149,875 shares of common stock of the Company. All of the Company s stock option grants expire 10 years from the date of grant, thirty days after termination of service other than for cause, or one year after death or disability of the grantee. The Company s stock option program also allows for the grant of restricted shares. The Company has no option or restricted stock awards with market or performance conditions attached to them. The Company generally issues shares for option exercises from its treasury stock. The Company s stock-based employee compensation plans are more fully described in Note 14.

Prior to 2006, the Company followed the disclosure provisions of SFAS No. 123, Accounting for Stock-Based Compensation. SFAS No. 123 permitted entities to account for employee stock options and similar equity instruments under Accounting Principles Board (APB) Opinion No. 25, Accounting for Stock Issued for Employees. Under SFAS No. 123, entities were required to make pro forma disclosures of net income and earnings per share, as if the fair-value based method of accounting defined in SFAS No. 123 had been applied.

On May 13, 2005, the Company accelerated the vesting of 483,812 stock options, representing all unvested stock options on such date which had exercise prices in excess of the market value of the Company s common stock on May 13, 2005. The Company s decision to accelerate the vesting of these options was part of a review by the Board of Directors of the Company s incentive compensation program and upcoming changes in the accounting for stock options. Compensation expense that would have been recorded absent the accelerated vesting was approximately $2.1 million net of taxes, $644,000 of which would have been recorded in 2006. In December 2005, the Company granted options to purchase 164,308 shares of common stock to key employees at an exercise price of $14.94 per share. These options vested immediately. Compensation expense that would have been recorded net of taxes was approximately $774,000.

The following table illustrates the effect on net income and earnings per share if the Company had applied the fair value recognition method to stock-based employee compensation (in thousands, except per share amounts).

	Years Ended December 31, 2005	2004
Net income, as reported	$ 20,221	$ 16,495
Deduct: Stock-based compensation costs determined under fair value based method for all awards	2,888	769
Pro forma net income	$ 17,333	$ 15,726
Earnings per share:		
Basic, as reported	$ 0.90	$ 0.81
Basic, pro forma	$ 0.77	$ 0.77
Diluted, as reported	$ 0.89	$ 0.80
Diluted, pro forma	$ 0.76	$ 0.77

Statement Of Cash Flows

Cash and cash equivalents are defined as cash on hand, cash items in the process of collection, amounts due from banks and federal funds sold with an original maturity of three months or less. Cash paid for income taxes was $10.6 million, $7.8 million and $6.7 million in 2006, 2005 and 2004, respectively. Cash paid for interest was $51.9 million, $32.6 million and $21.4 million in 2006, 2005 and 2004, respectively.

Comprehensive Income

The Company follows the disclosure provisions of SFAS No. 130, Reporting Comprehensive Income. SFAS No. 130 requires the reporting of comprehensive income in addition to net income from operations. Comprehensive income is a more inclusive financial reporting methodology that includes disclosure of certain financial information that historically has not been recognized in the calculation of net income.

	Year ended December 31, 2006		
	Before tax amount	Tax Benefit (Expense)	Net of tax amount
		(dollars in thousands)	
Unrealized gains on available for sale securities			
Unrealized holding gains arising during period	$ 378	$ (131)	$ 247
Less reclassification adjustment for net losses realized in net income	(2,995)	922	(2,073)
Net unrealized gains on available for sale securities	3,373	(1,053)	2,320
Change in pension liabilities	(829)	290	(539)
Other comprehensive income, net	$ 2,544	$ (763)	$ 1,781

	Year ended December 31, 2005		
	Before tax amount	Tax Benefit (Expense)	Net of tax amount
		(dollars in thousands)	
Unrealized losses on available for sale securities			
Unrealized holding gains arising during period	$ (8,503)	$ 2,916	$ (5,587)
Less reclassification adjustment for net losses realized in net income	(583)	187	(396)
Other comprehensive loss, net	$ (7,920)	$ 2,729	$ (5,191)

	Year ended December 31, 2004		
	Before tax amount	Tax Benefit (Expense)	Net of tax amount
		(dollars in thousands)	
Unrealized gains on available for sale securities			
Unrealized holding gains arising during period	$ 991	$ (313)	$ 678
Less reclassification adjustment for net gains realized in net income	638	(202)	436
Other comprehensive income, net	$ 353	$ (111)	$ 242

Goodwill and Other Identifiable Intangible Assets

The Company accounts for goodwill and other identifiable intangible assets in accordance with SFAS No. 142, Goodwill and Intangible Assets. The Company tests goodwill for impairment annually at the reporting unit level using various market valuation methodologies. The Company has tested the goodwill and other identifiable intangible assets as of December 31, 2006 and has determined that they are not impaired.

Goodwill and core deposit intangible resulting from the Newton and CSB acquisitions totaled $84.9 million and $7.9 million, respectively, and is included in goodwill and other identifiable intangible assets. Total goodwill was $87.1 million for each of the years ended December 31, 2006 and 2005. Core deposit intangible was $4.9 million and $6.3 million for the years ended

December 31, 2006 and 2005, respectively. Amortization expense of core deposit intangible was $1.2 million, $1.2 million and $810,000 for the years ended December 31, 2006, 2005 and 2004, respectively.

Bank Owned Life Insurance

The Company invests in bank owned life insurance (BOLI). BOLI involves the purchasing of life insurance by the Company on a chosen group of employees. The Company is owner and beneficiary of the policies. At December 31, 2006 and 2005, Lakeland had $36.8 million and $35.5 million, respectively, in BOLI. Income earned on BOLI was

$1.2 million, $1.2 million and $1.1 million for the years ended December 31, 2006, 2005 and 2004, respectively.

In September 2006, the Financial Accounting Standards Board ratified a consensus opinion reached by the Emerging Issues Task Force on Issue 06-4, Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements, (EITF 06-4) which requires employers that enter into endorsement split-dollar life insurance arrangements that provide an employee with a postretirement benefit to recognize a liability for the future benefits promised based on the substantive agreement made with the employee. Whether the accrual is based on a death benefit or on the future cost of maintaining the insurance would depend on what the employer has effectively agreed to provide during the employee s retirement. The purchase of an endorsement-type life insurance policy does not qualify as a settlement of the liability.

The consensus in EITF 06-4 is effective for fiscal years beginning after December 15, 2007. The Company intends to adopt EITF 06-4 effective January 1, 2008. The Company is currently evaluating the impact this guidance will have on the Company s financial position and results of operations.

In September 2006, the FASB ratified the consensus reached by the Emerging Issues Task Force in Issue 06-5, Accounting for Purchases of Life Insurance Determining the Amount That Could Be Realized in Accordance with FASB Technical Bulletin No. 85-4, Accounting for Purchases of Life Insurance (EITF 06-5). EITF 06-5 is effective for the fiscal years beginning after December 15, 2006. The Company adopted this EITF effective January 1, 2007. EITF 06-5 pertains to companies with life insurance policies, including Bank-Owned Life Insurance, and further defines the amount that could be realized under an insurance contract that should be booked as an asset on a company s balance sheet. The Company is currently evaluating the impact this guidance will have on the Company s financial position and results of operations.

Income Taxes

The Company accounts for income taxes under the liability method of accounting for income taxes. Deferred tax assets and liabilities are determined based on the difference between the financial statement and tax bases of assets and liabilities as measured by the enacted tax rates that will be in effect when these differences reverse. Deferred tax expense is the result of changes in deferred tax assets and liabilities. The principal types of differences between assets and liabilities for financial statement and tax return purposes are allowance for loan and lease losses, core deposit intangible, deferred loan fees, deferred compensation and securities available for sale.

In July 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes (FIN 48). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise s financial statements in accordance with Statement of Financial Accounting Standards No. 109, Accounting for Income Taxes. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006. The Company is currently evaluating the impact the adoption of FIN 48 will have on its consolidated financial statements.

Variable Interest Entities

Management has determined that Lakeland Bancorp Capital Trust I, Lakeland Bancorp Capital Trust II and Lakeland Bancorp Capital Trust III (collectively, the Trusts) qualify as a variable interest entities under FIN 46. The Trusts issued mandatorily redeemable preferred stock to investors and loaned the proceeds to the Company. The Trusts hold, as their sole asset, subordinated debentures issued by the Company.

The Federal Reserve has issued guidance on the regulatory capital treatment for the trust preferred securities issued by the Trusts as a result of the adoption of FIN 46(R). The rule retains the current maximum percentage of total capital permitted for trust preferred securities at 25%, but enacts other changes to the rules governing trust preferred securities that affect their use as part of the collection of entities known as restricted core capital elements. The rule took effect April 11, 2005; however, a five year transition period starting March 31, 2004 and leading up to March 31, 2009 allows bank holding companies to continue to count trust preferred securities as Tier 1 Capital after applying FIN 46(R). Management will continue to evaluate the effects of this rule through the transition period.

New Accounting Pronouncements

In September 2006, the FASB issued Statement of Financial Accounting Standards (SFAS) No. 157, Fair Value Measurements which is effective for fiscal years beginning after November 15, 2007 and for interim periods within those years. This statement

defines fair value, establishes a framework for measuring fair value and expands the related disclosure requirements. The Company is currently evaluating the impact the adoption of SFAS No. 157 will have on its consolidated financial statements.

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159, The Fair Value Option for Financial Assets and Financial Liabilities-Including an amendment of FASB Statement No. 115. SFAS No. 159 permits entities to choose to measure many financial instruments and certain other items at fair value. SFAS No. 159 is effective as of the beginning of an entity s first fiscal year that begins after November 15, 2007 but earlier adoption is permitted provided the entity also elects to apply the provisions of SFAS No. 157 during the same time period.

NOTE 2 - ACQUISITIONS

On July 1, 2004, the Company completed the acquisition of Newton Financial Corp. (NFC) pursuant to which NFC was merged into the Company. NFC shareholders had the right to elect stock and/or cash in the merger subject to certain allocation provisions. NFC shareholders who received stock received 4.5 shares (4.961 restated*) of the Company s stock for each of their NFC shares. NFC shareholders who received cash received $72.08 per share. Under the terms of the merger, 1,086,922 shares of NFC stock were exchanged for a total issuance of 4,891,119 shares (5,392,457 restated*) of Lakeland Bancorp stock. The remaining 270,526 shares of NFC stock were exchanged for a total of $19.5 million. NFC stock options of 13,591 were exchanged for Company stock options of 61,160 (67,428 restated*) and were fully vested at the time of the merger. As a result of the acquisition, the Company recorded $67.0 million in goodwill and other intangible assets. In 2005, an unasserted legal claim was identified related to loan payments previously made to Newton prior to Lakeland s acquisition. The unasserted legal claim of approximately $460,000 was recorded in goodwill during the first quarter of 2005 and was settled in the second quarter of 2005. The transaction was accounted for under the purchase method of accounting. The results of operations include Newton s results of operations from July 1, 2004 forward.

*Restated for the 5% stock dividend payable on August 16, 2005 to shareholders of record on July 29, 2005 and for the 5% stock dividend paid on August 16, 2006 to shareholders of record on July 31, 2006.

The following represents the unaudited pro forma financial information of Lakeland Bancorp as if the acquisition occurred on the first date of the period indicated. The pro forma financial information should be read in conjunction with the related historical information and is not necessarily indicative of the results that would have been attained had the transaction actually taken place.

	For the year ended December 31, 2004 (in thousands)
Interest income	$ 90,826
Interest expense	23,300
Net interest income	67,526
Provision for loan losses	4,038
Non-interest income	14,065
Non-interest expense	51,959
Net Income	$ 17,592

NOTE 3 - INVESTMENT SECURITIES

The amortized cost, gross unrealized gains and losses, and the fair value of the Company s available for sale and held to maturity securities are as follows:

AVAILABLE FOR SALE

	December 31, 2006				December 31, 2005			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(in thousands)				(in thousands)			
U.S. government agencies	**$ 43,346**	**$**	**$ (967)**	**$ 42,379**	$ 160,421	$ 0	$ (3,039)	$ 157,382
Mortgage-backed securities	**179,734**	**7**	**(5,365)**	**174,376**	293,179	27	(7,402)	285,804
Obligations of states and political subdivisions	**29,183**	**166**	**(139)**	**29,210**	45,396	549	(226)	45,719
Other debt securities	**13,128**	**35**	**(644)**	**12,519**	8,084	13	(166)	7,931
Equity securities	**19,153**	**3,007**	**(135)**	**22,025**	16,231	3,069	(233)	19,067

$ 284,544	**$ 3,215**	**$ (7,250)**	**$ 280,509**	$ 523,311	$ 3,658	$ (11,066)	$ 515,903

HELD TO MATURITY

	December 31, 2006				December 31, 2005			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(in thousands)				(in thousands)			
U.S. government agencies	**$ 39,256**	**$**	**$ (808)**	**$ 38,448**	$ 38,532	$	$ (834)	$ 37,698
Mortgage-backed securities	**44,993**	**7**	**(1,008)**	**43,992**	49,277	13	(1,111)	48,179
Obligations of states and political subdivisions	**56,983**	**125**	**(550)**	**56,558**	64,143	142	(1,116)	63,169
Other debt securities	**1,606**		**(40)**	**1,566**	2,617		(26)	2,591
	$ 142,838	**$ 132**	**$ (2,406)**	**$ 140,564**	$ 154,569	$ 155	$ (3,087)	$ 151,637

The following table lists contractual maturities of investment securities classified as available for sale and held to maturity. 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.

	December 31, 2006			
	Available for Sale		Held to Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
	(in thousands)			
Due in one year or less	$ 17,415	$ 17,382	$ 14,194	$ 14,162
Due after one year through five years	30,990	30,566	45,900	45,014
Due after five years through ten years	29,899	28,988	28,634	28,294
Due after ten years	7,353	7,172	9,117	9,102
	85,657	84,108	97,845	96,572
Mortgage-backed securities	179,734	174,376	44,993	43,992
Equity securities	19,153	22,025		
Total securities	$ 284,544	$ 280,509	$ 142,838	$ 140,564

	Years ended December 31,		
	2006	2005	2004
		(in thousands)	
Sale proceeds	**$ 178,124**	$ 81,095	$ 32,708
Gross gains	**1,204**	343	678
Gross losses	**(4,199)**	(926)	(440)

In 2005, the Company sold approximately $715,000 in investment securities classified as held to maturity for a gain of $23,000 because over 85% of the original principal acquired on these securities had been paid by the sale date.

Securities with a carrying value of approximately $332.8 million and $255.3 million at December 31, 2006 and 2005, respectively, were pledged to secure public deposits and for other purposes required by applicable laws and regulations.

The following table indicates the length of time individual securities have been in a continuous unrealized loss position at December 31, 2006 and 2005:

	Less than 12 months		12 months or longer			Total	
	Fair value	Unrealized Losses	Fair value	Unrealized Losses	Number of securities	Fair value	Unrealized Losses
			(dollars in thousands)				
December 31, 2006							
AVAILABLE FOR SALE							
U.S. government agencies	**$**	**$**	**$ 39,382**	**$ 967**	**12**	**$ 39,382**	**$ 967**
Mortgage-backed securities	**17,557**	**190**	**152,883**	**5,175**	**97**	**170,440**	**5,365**
Obligations of states and political subdivisions	**2,155**	**18**	**12,680**	**121**	**31**	**14,835**	**139**
Other debt securities	**5,032**	**22**	**5,548**	**622**	**5**	**10,580**	**644**
Equity securities			**8,291**	**135**	**3**	**8,291**	**135**
	$ 24,744	**$ 230**	**$ 218,784**	**$ 7,020**	**148**	**$ 243,528**	**$ 7,250**
HELD TO MATURITY							
U.S. government agencies	**$ 983**	**$ 16**	**37,465**	**$ 792**	**16**	**$ 38,448**	**$ 808**
Mortgage-backed securities	**5,508**	**48**	**38,090**	**960**	**27**	**43,598**	**1,008**
Obligations of states and political subdivisions	**11,181**	**22**	**30,729**	**528**	**106**	**41,910**	**550**
Other debt securities			**1,566**	**40**	**3**	**1,566**	**40**
	$ 17,672	**$ 86**	**$ 107,850**	**$ 2,320**	**152**	**$ 125,522**	**$ 2,406**

	Less than 12 months		12 months or longer			Total	
	Fair value	Unrealized Losses	Fair value	Unrealized Losses	Number of securities	Fair value	Unrealized Losses
			(dollars in thousands)				
December 31, 2005							
AVAILABLE FOR SALE							
U.S. government agencies	$ 53,718	$ 340	$ 103,664	$ 2,699	55	$ 157,382	$ 3,039
Mortgage-backed securities	101,212	1,720	168,724	5,682	136	269,936	7,402
Obligations of states and political subdivisions	16,923	204	767	22	38	17,690	226
Other debt securities	5,452	149	568	17	4	6,020	166
Equity securities	7,862	233			6	7,862	233
	$ 185,167	$ 2,646	$ 273,723	$ 8,420	239	$ 458,890	$ 11,066
HELD TO MATURITY							
U.S. government agencies	$ 14,830	$ 252	22,868	$ 582	16	$ 37,698	$ 834
Mortgage-backed securities	18,904	277	27,388	834	22	46,292	1,111
Obligations of states and political subdivisions	38,825	649	2,523	467	131	41,348	1,116
Other debt securities	2,038	24	553	2	4	2,591	26
	$ 74,597	$ 1,202	$ 53,332	$ 1,885	173	$ 127,929	$ 3,087

Management has evaluated the securities in the above table and has concluded that none of these securities has impairments that are other-than-temporary. In its evaluation, management considered the types of securities including if the securities were US government issued, and what the credit rating was on the securities. Most of the securities that are in an unrealized loss position are in a loss position because of changes in interest rates since the securities were purchased. The securities that have been in an unrealized loss position for 12 months or longer include US government agency securities and mortgage backed securities whose market values are sensitive to interest rates. The corporate securities and the obligations of state and political subdivisions listed in the above table all are investment grade securities.

NOTE 4 - LOANS

	December 31, 2006	2005
	(in thousands)	
Commercial	**$ 714,496**	$ 589,646
Leases	**196,518**	90,194
Real estate-mortgage	**272,102**	256,621
Real estate-construction	**87,562**	68,325
Home Equity and Consumer	**315,038**	302,236
Total loans	**1,585,716**	1,307,022
Plus deferred costs	**5,928**	5,745
Loans net of deferred fees	**$ 1,591,644**	$ 1,312,767

The maturities of minimum lease receivables are as follows (in thousands):

2007	$ 7,928
2008	24,313
2009	45,411
2010	42,348
2011	53,743
2012 and therafter	22,775
	$ 196,518

Changes in the allowance for loan and lease losses are as follows:

	Years ended December 31, 2006	2005	2004
		(in thousands)	
Balance at beginning of year	**$ 13,173**	$ 16,638	$ 16,899
Provision for loan and lease losses	**1,726**	1,555	3,602
Addition related to acquisitions			2,301
Loans charged off	**(2,790)**	(6,273)	(6,682)
Recoveries	**1,345**	1,253	518
Balance at end of year	**$ 13,454**	$ 13,173	$ 16,638

The balance of impaired loans was $4.1 million and $3.7 million at December 31, 2006 and 2005, respectively. Lakeland identifies a loan as impaired when it is probable that interest and principal will not be collected according to the contractual terms of the loan agreements. The allowance for loan and lease losses associated with impaired loans was $1,351,000 and $953,000 at December 31, 2006 and 2005, respectively. The average recorded investment on impaired loans was $3.7 million, $8.2 million and $15.3 million during 2006, 2005 and 2004, respectively, and the income recognized, primarily on the cash basis, on impaired loans was $315,000, $323,000 and $190,000 during 2006, 2005 and 2004, respectively. Interest which would have been accrued on impaired loans during 2006, 2005 and 2004 was $299,000, $661,000 and $1.5 million, respectively. Lakeland s policy for interest income recognition on impaired loans is to recognize income on restructured loans under the accrual method. Lakeland recognizes income on non-accrual loans under the cash basis when the loans are both current and the collateral on the loan is sufficient to cover the outstanding obligation to Lakeland; if these factors do not exist, Lakeland will not recognize income until all loan principal has been recovered.

Loans past due 90 days or more and still accruing are those loans as to which payment of interest or principal is in arrears for a period of 90 days or more but is adequately collateralized as to interest and principal or is in the process of collection. Non-performing loans consist of non-accrual loans and renegotiated loans. Non-accrual loans are those on which income under the accrual method has been discontinued with subsequent interest payments credited to interest income when received, or if ultimate collectibility of principal is in doubt, applied as principal reductions. Renegotiated loans are loans whose contractual interest rates have been reduced or where other significant modifications have been made due to borrowers financial difficulties. Interest on these loans is either accrued or credited directly to interest income. Loans past due 90 days or more and non-accrual loans were as follows:

	December 31,		
	2006	2005	2004
	(in thousands)		
Loans past due 90 days or more and still accruing	**$ 876**	$ 5,127	$ 2,347
Non-accrual loans	**$ 4,437**	$ 3,907	$ 13,017

The impact of the above non-performing loans on interest income is as follows:

December 31,	**2006**	**2005**	**2004**
	(in thousands)		
Interest income if performing in accordance with original terms	**$ 299**	$ 661	$ 1,476
Interest income actually recorded	**315**	323	217
	$ (16)	$ 338	$ 1,259

Lakeland has entered into lending transactions in the ordinary course of business with directors, executive officers, principal stockholders and affiliates of such persons on similar terms as those prevailing for comparable transactions with other borrowers. These loans at December 31, 2006, were current as to principal and interest payments, and do not involve more than normal risk of collectibility. At December 31, 2006, loans to these related parties amounted to $32.6 million. There were new loans of $15.8 million to related parties and repayments of $13.0 million from related parties in 2006.

NOTE 5 - PREMISES AND EQUIPMENT

	Estimated	**December 31,**	
	useful lives	**2006**	**2005**
		(in thousands)	
Land	Indefinite	**$ 5,604**	$ 5,698
Buildings and building improvements	10 to 50 years	**30,079**	29,615
Leasehold improvements	10 to 25 years	**1,976**	1,855
Furniture, fixtures and equipment	2 to 30 years	**23,280**	21,823
		60,939	58,991
Less accumulated depreciation and amortization		**28,867**	26,563
		$ 32,072	$ 32,428

NOTE 6 - DEPOSITS

At December 31, 2006, the schedule of maturities of certificates of deposit is as follows (in thousands):

2007	$ 468,526
2008	27,192
2009	2,775
2010	2,688
2011	594
Thereafter	1,104
	$ 502,879

NOTE 7 - Debt

Lines of Credit

As of December 31, 2006, the Company had approved lines of credit with the Federal Home Loan Bank (FHLB) of New York of $200.0 million. Borrowings under this arrangement have an interest rate that fluctuates based on market conditions and customer demand. As of December 31, 2006 there were no outstanding borrowings against these lines. As of December 31, 2006, the Company also had overnight federal funds lines available for it to borrow $110.0 million. The Company had not borrowed against these lines as of December 31, 2006.

Securities Sold Under Agreements to Repurchase and Federal Funds Purchased

Borrowed money at December 31, 2006 and 2005 consisted of short-term securities sold under agreements to repurchase and federal funds purchased. Securities underlying the agreements were under Lakeland s control. The following tables summarize information relating to securities sold under agreements to repurchase and federal funds purchased for 2006, 2005 and 2004. For purposes of the tables, the average amount outstanding was calculated based on a daily average.

	2006	2005 (in thousands)	2004
Federal funds purchased:			
Balance at December 31	**$**	$ 36,275	$ 55,000
Interest rate at December 31	**0.00%**	4.32%	2.50%
Maximum amount outstanding at any month-end during the year	**$ 95,150**	$ 80,825	$ 55,000
Average amount outstanding during the year	**$ 32,614**	$ 15,233	$ 12,370
Weighted average interest rate during the year	**5.07%**	3.08%	1.55%

	2006	2005 (in thousands)	2004
Securities sold under agreements to repurchase:			
Balance at December 31	**$ 41,061**	$ 66,294	$ 55,830
Interest rate at December 31	**4.19%**	3.79%	2.10%
Maximum amount outstanding at any month-end during the year .	**$ 74,336**	$ 111,737	$ 60,057
Average amount outstanding during the year	**$ 59,866**	$ 80,206	$ 26,524
Weighted average interest rate during the year	**4.42%**	3.19%	1.51%

Long-Term Debt

FHLB Debt

At December 31, 2006, advances from the FHLB totaling $91.7 million will mature within one to seven years and are reported as long-term borrowings. These advances are collateralized by certain securities and first mortgage loans. The advances had a weighted average interest rate of 5.08%.

Outstanding borrowings mature as follows (in thousands):

Year	
2007	$ 30,855
2008	30,855
2009	
2010	10,000
2011	10,000
Thereafter	10,000

	$ 91,710

Subordinated Debentures

On December 15, 2003, the Company issued $25.8 million of junior subordinated debentures due January 7, 2034 to Lakeland Bancorp Capital Trust III, a Delaware business trust, which is a wholly-owned subsidiary of the Company. The distribution rate on these securities is 7.535% for 10 years and float at LIBOR plus 285 basis points thereafter. The debentures are the sole asset of the Trust. The Trust issued 25,000 shares of trust preferred securities, $1,000 face value, for total proceeds of $25.0 million. The Company s obligations under the debentures and related documents, taken together, constitute a full, irrevocable and unconditional guarantee on a subordinated basis by the Company of the Trust s obligations under the preferred securities. The preferred securities are callable by the

Company on or after January 7, 2009, or earlier if the deduction of related interest for federal income taxes is prohibited, treatment as Tier I capital is no longer permitted, or certain other contingencies arise. The preferred securities must be redeemed upon maturity of the debentures in 2034.

On June 18, 2003, the Company issued $10.3 million of junior subordinated debentures due July 7, 2033 to Lakeland Bancorp Capital Trust I, a Delaware business trust, which is a wholly-owned subsidiary of the Company. The distribution rate on these securities is 6.20% for 7 years and float at LIBOR plus 310 basis points thereafter. The debentures are the sole asset of the Trust. The Trust issued 10,000 shares of trust preferred securities, $1,000 face value, for total proceeds of $10.0 million. The Company s obligations under the debentures and related documents, taken together, constitute a full, irrevocable and unconditional guarantee on a subordinated basis by the Company of the Trust s obligations under the preferred securities. The preferred securities are callable by the Company on or after July 7, 2010, or earlier if the deduction of related interest for federal income taxes is prohibited, treatment as Tier I capital is no longer permitted, or certain other contingencies arise. The preferred securities must be redeemed upon maturity of the debentures in 2033.

On June 18, 2003, the Company also issued $20.6 million of junior subordinated debentures due June 30, 2033 to Lakeland Bancorp Capital Trust II, a Delaware business trust, which is a wholly-owned subsidiary of the Company. The distribution rate on these securities is 5.71% for 5 years and float at LIBOR plus 310 basis points thereafter. The debentures are the sole asset of the Trust. The Trust issued 20,000 shares of trust preferred securities, $1,000 face value, for total proceeds of $20.0 million. The Company s obligations under the debentures and related documents, taken together, constitute a full, irrevocable and unconditional guarantee on a subordinated basis by the Company of the Trust s obligations under the preferred securities. The preferred securities are callable by the Company on or after June 30, 2008, or earlier if the deduction of related interest for federal income taxes is prohibited, treatment as Tier I capital is no longer permitted, or certain other contingencies arise. The preferred securities must be redeemed upon maturity of the debentures in 2033.

NOTE 8 - STOCKHOLDERS EQUITY

On July 12, 2006, the Company announced a stock repurchase program for the purchase of up to 500,000 shares of the Company s common stock over the next year. The Company has purchased no shares of its common stock under this repurchase program.

On July 12, 2006, the Company s Board of Directors authorized a 5% stock dividend which was distributed on August 16, 2006.

On June 10, 2005, the Company announced a stock repurchase program for the purchase of up to 826,875 shares of the Company s common stock over the next year. During 2005, the Company purchased 421,157 shares of its outstanding common stock in the 2005 plan at an average price of $14.46 per share for an aggregate cost of $6.1 million. During 2006, the Company purchased 220,657 shares of its common stock in the 2005 plan at an average price of $14.25 per share for an aggregate cost of $3.1 million. In July 2006, the 2005 plan expired and was replaced by the 2006 plan.

On July 13, 2005, the Company s Board of Directors authorized a 5% stock dividend which was distributed on August 15, 2005.

In January 2004, the Company announced a stock repurchase program for the purchase of up to 275,625 shares of the Company s common stock over the next year. On July 15, 2004, the amount of shares purchasable in the stock buyback plan was increased to 551,250 shares to be purchased over the following year. During 2004, the Company purchased 278,932 shares of its outstanding common stock at an average price of $15.82 per share for an aggregate cost of $4.4 million. During 2005, the Company completed purchasing the shares purchasable in the 2004 plan by purchasing 284,432 shares of its outstanding common stock at an average price of $14.10 per share for an aggregate price of $4.0 million.

NOTE 9 - SHAREHOLDER PROTECTION RIGHTS PLAN

The Company adopted a Shareholder Rights Plan (the Rights Plan) in 2001 to protect shareholders from attempts to acquire control of the Company at an inadequate price. Under the Rights Plan, the Company distributed a dividend of one right to purchase a unit of common stock on each outstanding common share of the Company. The rights are not currently exercisable or transferable, and no separate certificates evidencing such rights will be distributed, unless certain events occur. The rights have an expiration date of September 4, 2011.

After the rights become exercisable, under certain circumstances, the rights (other than rights held by a 15.0% beneficial owner or an adverse person) will entitle the holders to purchase the Company s common shares at a substantially reduced price.

The Company is generally entitled to redeem the rights at $0.001 per right at any time before the Rights become exercisable. Rights are not redeemable following an adverse person determination.

The Rights Plan was not adopted in response to any specific effort to acquire control of the Company. The issuance of rights had no dilutive effect, did not affect the Company s reported earnings per share, and was not taxable to the Company or its shareholders.

NOTE 10 - INCOME TAXES

The components of income taxes are as follows:

	Years Ended December 31,		
	2006	2005	2004
		(in thousands)	
Current tax provision	**$ 8,200**	$ 8,060	$ 6,289
Deferred tax provision (benefit)	**(740)**	1,524	1,330
Total provision for income taxes	**$ 7,460**	$ 9,584	$ 7,619

The income tax provision reconciled to the income taxes that would have been computed at the statutory federal rate of 35% is as follows:

	Years Ended December 31,		
	2006	2005	2004
		(in thousands)	
Federal income tax, at statutory rates	**$ 8,553**	$ 10,432	$ 8,442
Increase (deduction) in taxes resulting from:			
Non-taxable interest income	**(1,781)**	(1,730)	(1,507)
State income tax, net of federal income tax effect	**704**	823	622
Other, net	**(16)**	59	62
Provision for income taxes	**$ 7,460**	$ 9,584	$ 7,619

The net deferred tax asset consisted of the following:

	December 31,	
	2006	2005
Deferred tax assets:	(in thousands)	
Allowance for loan and lease losses	$ 5,736	$ 5,382
Valuation reserves for land held for sale and other real estate	679	679
Non-accrued interest	292	243
Depreciation	164	68
Deferred compensation	1,140	974
Unfunded pension benefits	290	0
Unrealized loss on securities available for sale	1,504	2,557
Other, net	6	240
Deferred tax assets	9,811	10,143
Deferred tax liabilities:		
Core deposit intangible from acquired companies	2,030	2,466
Deferred loan costs	1,161	963
Prepaid expenses	290	264
Fair market value adjustments	131	217
Other	563	574
Deferred tax liabilities	4,175	4,484
Net deferred tax assets, included in other assets	$ 5,636	$ 5,659

NOTE 11 EARNINGS PER SHARE

The Company s calculation of earnings per share in accordance with SFAS No. 128 is as follows:

	Year ended December 31, 2006		
	Income (numerator)	Shares (denominator)	Per share amount
	(in thousands, except per share amounts)		
Basic earnings per share			
Net income available to common shareholders	**$ 16,977**	**22,039**	**$ 0.77**
Effect of dilutive securities			
Stock Options		**144**	
Diluted earnings per share			
Net income available to common shareholders plus assumed conversions	**$ 16,977**	**22,183**	**$ 0.77**

Options to purchase 535,691 shares of common stock and 36,028 shares of restricted stock at a weighted average of $15.39 and $14.65 per share, respectively, were outstanding during 2006. The options and restricted stock were not included in the computation of diluted earnings per share because the option exercise price and the grant-date price were greater than the average market price during the period.

	Year ended December 31, 2005		
	Income (numerator)	Shares (denominator)	Per share amount
	(in thousands, except per share amounts)		
Basic earnings per share			
Net income available to common shareholders	$ 20,221	22,511	$ 0.90
Effect of dilutive securities			
Stock Options		170	(0.01)
Diluted earnings per share			
Net income available to common shareholders plus assumed conversions	$ 20,221	22,681	$ 0.89

Options to purchase 547,576 shares of common stock at a weighted average of $15.39 per share were outstanding during 2005. They were not included in the computation of diluted earnings per share because the option exercise price was greater than the average market price.

	Year ended December 31, 2004		
	Income (numerator)	Shares (denominator)	Per share amount
	(in thousands, except per share amounts)		
Basic earnings per share			
Net income available to common shareholders	$ 16,495	20,295	$ 0.81
Effect of dilutive securities			
Stock Options		250	(0.01)
Diluted earnings per share			
Net income available to common shareholders plus assumed conversions	$ 16,495	20,545	$ 0.80

Options to purchase 238,523 shares of common stock at $15.91 per share were outstanding during 2004. They were not included in the computation of diluted earnings per share because the option exercise price was greater than the average market price.

NOTE 12 - EMPLOYEE BENEFIT PLANS

Profit Sharing Plan

The Company s annual contribution to the plan is determined by its Board of Directors. Annual contributions are allocated to participants on a point basis with accumulated benefits payable at retirement, or, at the discretion of the plan committee, upon termination of employment. Contributions made by the Company were approximately $743,000 for 2006, $755,000 for 2005 and $625,000 for 2004.

Salary Continuation Agreements

The National Bank of Sussex County (NBSC) entered into a salary continuation agreement during 1996 with its former Chief Executive Officer and its President which entitle them to certain payments upon their retirement. As part of the merger of the Company and NBSC s parent (High Point Financial Corp.) in July 1999, Lakeland placed in trusts amounts equal to the present value of the amounts that would be owed to them in their retirement. These amounts were $722,000 for the Chief Executive Officer and $381,000 for the President. Lakeland has no further obligation to pay additional amounts pursuant to these agreements.

Former CEO Retirement Benefits

Metropolitan State Bank entered into an agreement in January 1997 with its former Chief Executive Officer (CEO), which provides for an annual retirement benefit of $35,000 for a fifteen year period. In February 1999, the Company entered into an additional agreement with this CEO. Such agreement provides for an additional retirement benefit of $35,000 per annum for a fifteen year period as well as certain retiree medical benefits. During 2006, 2005 and 2004, $11,000, $9,000 and $15,000 respectively, was charged to operations related to these obligations.

Retirement Savings Plans (401K plans)

Beginning in January 2002, the Company began contributing to its 401(k) plan. All eligible employees can contribute a portion of their annual salary with the Company matching up to 40% of the employee s contributions. The Company s contributions in 2006, 2005 and 2004 totaled $361,000, $321,000 and $240,000, respectively.

Pension Plan

Newton had a defined benefit pension plan. As of March 31, 2004, Newton s Board of Directors elected to freeze the benefits of the pension plan. All participants of the plan ceased accruing benefits as of that date.

The investment policy and strategy of the Plan and its advisors includes target portfolio allocations of approximately 60% in equities and 40% in debt securities. Based on historical performance, the Plan assumes that the long term equity securities have earned a rate of return of approximately 10% and fixed income securities have earned a return of between 1% and 5%. The composition of plan assets at December 31, 2006 was as follows:

Asset Category	
Equity securities	**67%**
Debt securities	**32%**
Other securities	**1%**

The accumulated benefit obligation as of December 31, 2006 and 2005, is as follows:

(in thousands)	2006	2005
Accumulated postretirement benefit obligation	**$ 1,500**	$ 1,481
Interest Cost	**95**	105
Actuarial loss	**286**	237
Estimated benefit payments	**(305)**	(323)
Total accumulated postretirement benefit obligation	**1,576**	1,500
Fair value of plan assets beginning of period	**1,360**	1,619
Return on plan assets	**121**	64
Benefits paid	**(305)**	(323)
Asset gain	**0**	0
Fair value of plan assets at end of year	**1,176**	1,360
Funded status	**(400)**	(140)
Unrecognized net actuarial loss	**530**	304
Prepaid benefit	**$ 130**	$ 164
Accumulated benefit obligation	**$ 1,576**	$ 1,500
Amount not recognized as component of net postretirement cost		
Recognized in accumulated other comprehensive income Net actuarial loss	**$ 344**	$

The components of net periodic pension cost are as follows:

(in thousands)	2006	2005
Amortization of actuarial loss	$ 25	$ 4
Interest cost on APBO	95	105
Expected return on plan assets	(87)	(117)
Net periodic postretirement cost	$ 33	$ (8)

The benefits expected to be paid in each of the next five years and the aggregate for the five fiscal years thereafter are as follows (in thousands):

2007	$ 2
2008	50
2009	53
2010	63
2011	62
2012 - 2016	506

The assumptions used to determine the pension obligation and the net periodic pension cost were as follows:

	2006	2005
Discounted rate	**6.00%**	6.00%
Expected return on plan assets	**7.25%**	7.25%
Rate of compensation	**0.00%**	0.00%

The Company adopted SFAS No. 158 on December 31, 2006 and recorded a liability of $226,000, a deferred tax asset of $79,000 and an other comprehensive loss of $147,000 upon adoption.

The amount in accumulated other comprehensive loss expected to be recognized as a component of net periodic benefit cost in 2007 is $31,000.

Employee Stock Ownership Plan

NBSC had an Employee Stock Ownership Plan (ESOP). No contributions have been made to this plan for the years ended December 31, 2006, 2005 and 2004.

Postretirement Health Care Benefits

In 2000, the Company instituted postretirement health care benefits and life insurance coverage to its employees who meet certain predefined criteria. The expected cost of these benefits is charged to expense during the years that eligible employees render service. In December 2005, the Company terminated this plan recording a curtailment gain of $675,000 and a settlement gain of $197,000.

The accumulated postretirement benefit obligation (APBO) as of December 31, 2005 was as follows:

(in thousands)	**2005**
Accumulated postretirement benefit obligation, January 1	**$ 660**
Service cost	**62**
Interest Cost	**41**
Amendments	**(204)**
Effect of Settlement	**(30)**
Effect of Curtailment	**(512)**
Actuarial (gain) loss	**15**
Estimated benefit payments	**(32)**
Total accumulated postretirement benefit obligation	0
Unrecognized net gain due to past experience different from that assumed and effects of changes in assumptions made	
Unrecognized prior service cost	
Unamortized transition obligation	
Accrued accumulated postretirement benefit obligation	$

The measurement date for the APBO was December 31, 2005.

The components of net periodic postretirement benefit cost are as follows:

(in thousands)	**2005**	**2004**
Service cost, benefits attributed to employee service during the year	**$ 62**	$ 66
Interest cost on APBO	**41**	36
Amortization of prior service cost	**26**	47
Amortization of transition obligation	**6**	6
Amortization of gains	**(9)**	(7)
Net periodic postretirement cost before accounting for settlement and curtailment	**$ 126**	$ 148
Curtailment gain	**(675)**	
Settlement gain	**(197)**	

Net periodic postretirement benefit cost	**($ 746)**	$

Because the Company terminated the postretirement benefit plan, there will be no contribution in 2007.

The discount rate used to determine the Company s APBO was 6.0% for 2005.

Deferred Compensation Arrangements

High Point Financial Corp. had established deferred compensation arrangements for certain directors and executives

of High Point Financial Corp. and NBSC. The deferred compensation plans differ, but generally provide for annual payments for ten to fifteen years following retirement. The Company s liabilities under these arrangements are being accrued from the commencement of the plans over the participants remaining periods of service. The Company intends to fund its obligations under the deferred compensation arrangements with the increase in cash surrender value of life insurance policies that it has purchased on the respective participants. The deferred compensation plans do not hold any assets. For the years ended December 31, 2006, 2005 and 2004, $12,000, $25,000 and $3,000, respectively, was charged to operations related to these obligations. As of December 31, 2006 and 2005, the accrued liability for these plans was $190,000 and $208,000, respectively.

Supplemental Executive Retirement Plan

In 2003, the Company entered into a supplemental executive retirement plan (SERP) agreement with its Chief Executive Officer that provides annual retirement benefits of $150,000 a year for a 15 year period when the Chief Executive Officer reaches the age of 65. The Company intends to fund its obligations under the deferred compensation arrangements with the increase in cash surrender value of bank owned life insurance policies purchased in 2003. In 2006, 2005 and 2004, the Company expensed $355,000, $331,000 and $308,000, respectively, for this plan.

NOTE 13 - DIRECTORS RETIREMENT PLAN

The Company provides a plan that any director who completes five years of service may retire and continue to be paid for a period of ten years at a rate ranging from $5,000 through $17,500 per annum, depending upon years of credited service. This plan is unfunded. The following tables present the status of the plan and the components of net periodic plan cost for the years then ended. The measurement date for the accumulated benefit obligation is December 31 of the years presented.

	December 31,	
	2006	**2005**
	(in thousands)	
Actuarial present value of benefit obligation		
Vested	**$ 594**	$ 543
Nonvested	**56**	86
Accumulated benefit obligation	**$ 650**	$ 629
Projected benefit obligation	**833**	825
Unrecognized net loss		(113)
Unrecognized prior service cost being amortized over fifteen years		(258)
Accrued plan cost included in other liabilities	**$ 833**	$ 454
Amount not recognized as component of net postretirement benefit cost		
Recognized in accumulated other comprehensive income		
Net actuarial loss	**$ 86**	$
Unrecognized prior service cost	**$ 213**	
Not recognized in accumulated other comprehensive income		
Net actuarial loss		113
Unrecognized prior service cost		258
Amounts not recognized as a component of net postretirement benefit cost	**$ 299**	$ 371

	Years ended December 31, 2006	2005	2004
	(in thousands)		
Net periodic plan cost included the following components:			
Service cost	**$ 24**	$ 21	$ 18
Interest cost	**47**	48	49
Amortization of prior service cost	**46**	47	46
	$ 117	$ 116	$ 113

A discount rate of 6.00% was assumed in the plan valuation for both 2006 and 2005. As the benefit amount is not dependent upon compensation levels, a rate of increase in compensation assumption was not utilized in the plan valuation.

The director s retirement plan holds no plan assets. The benefits expected to be paid in each of the next five years and in aggregate for the five years thereafter are as follows (in thousands):

2007	$ 47
2008	55
2009	55
2010	72
2011	72
2012 - 2016	357

The Company expects its contribution to the director s retirement plan to be $47,000 in 2007.

On December 31, 2006, the Company adopted SFAS No. 158 and recorded a liability of $299,000 to recognize the underfunded status of the Director s Retirement Plan. It also recorded a deferred tax asset of $105,000 and an other comprehensive loss of $194,000.

The amount in accumulated other comprehensive loss expected to be recognized as a component of net periodic benefit cost in 2007 is $35,000.

NOTE 14 - STOCK-BASED COMPENSATION

Employee Stock Option Plans

The Company established the 2000 Equity Compensation Program which authorizes the granting of incentive stock options and supplemental stock options to employees of the Company which includes those employees serving as officers and directors of the Company. The plan originally authorized options to purchase up to 1,273,089 shares of common stock of the Company. At the 2005 Annual Shareholders Meeting, the shareholders voted to increase the authorized shares by an additional 876,786 shares.

During 2004 the Company granted options to purchase 110,250 shares to new non-employee directors of the Company. The directors options were exercisable in five equal installments beginning on the date of grant and continuing on the next four anniversaries of the date of grant. The vesting of these shares was accelerated in 2005 as further discussed below. As of December 31, 2006 and 2005, 272,115 and 295,162 options granted to directors were outstanding, respectively.

During 2005, the Company granted options to purchase 164,308 shares of common stock to key employees at an exercise price of $14.94 per share. These options vested immediately. During 2004, the Company granted options to purchase 166,070 shares of common stock to key employees at an exercise price of $15.61, 64,640 of which were subject to shareholder approval of the increase of authorized shares. As of December 31, 2006 and 2005, outstanding options to purchase common stock granted to key employees were 813,643 and 868,246, respectively.

On May 13, 2005, the Company accelerated 483,812 stock options representing all unvested stock options on such date which had exercise prices in excess of the market value of the Company s common stock on that date.

In addition to the 2000 Equity Compensation program, the Company has assumed the outstanding options granted under three employee stock option plans established by High Point (the High Point Plans). As of December 31,

2006 and 2005, 1,609 options were outstanding under the High Point Plans. The Company has also assumed outstanding options granted under Newton Financial Corp. s 1999 Stock Option Plan (the Newton Plan). As of December 31, 2006 and 2005, 53,233 options were outstanding under the Newton Plan.

On December 13, 2006, the Company granted 36,028 shares of restricted stock at a market value of $14.65. These shares vest over a four year period. The expected compensation expense will be $124,000 a year for the next four years.

Prior to the adoption of SFAS No. 123(R), the Company presented all tax benefits of deductions resulting from the exercise of stock options as operating cash flows in the Statement of Cash Flows. Statement 123(R) requires the cash flows resulting from the tax benefits resulting from tax deductions in excess of the compensation cost recognized for those options (excess tax benefits) to be classified as financing cash flows. A $66,000 excess tax benefit classified as a financing cash inflow would have been classified as an operating cash inflow had the Company not adopted SFAS No. 123(R).

For the years ended December 31, 2005 and 2004, the Company estimated the fair value of each option grant on the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions:

	2005	2004
Risk-free interest rates	4.28%	3.98%
Expected dividend yield	2.00%	2.00%
Expected volatility	30.00%	31.00%
Expected lives (years)	7.00	7.00
Weighted average fair value of options granted	$ 4.50	$ 4.76

There were no options granted in 2006.

A summary of the status of the Company s option plans as of December 31, 2006 and the changes during the year ending on that date is represented below.

	Number of shares	Weighted average exercise price	Weighted average remaining contractual term (in years)	Aggregate Intrinsic Value
Outstanding, beginning of year	**1,218,249**	**$ 12.82**		
Options granted in acquisition				
Exercised	**(64,922)**	**8.00**		
Forfeited	**(12,727)**	**15.41**		
Outstanding, end of year	**1,140,600**	**$ 13.07**	**6.22**	**$ 2,383,151**
Options exercisable at year-end	**1,140,600**		**6.22**	**$ 2,383,151**
Vested and expected to vest at December, 31, 2006	**1,140,600**		**6.22**	**$ 2,383,151**

The aggregate intrinsic value of options exercised in 2006, 2005 and 2004 were $363,000, $749,000 and $888,000, respectively. Exercise of stock options during 2006, 2005 and 2004 resulted in cash receipts of $519,000, $624,000 and $743,000, respectively. The total fair value of options that vested in 2005 and 2004 were $3.0 million and $846,000, respectively.

NOTE 15 - COMMITMENTS AND CONTINGENCIES

Lease Obligations

Rentals under long-term operating leases amounted to approximately $1,197,000, $1,186,000 and $878,000 for the years ended December 31, 2006, 2005 and 2004, respectively, including rent expense to related parties of $197,000 in 2006 and 2005 and $183,000 in 2004. At December 31, 2006, the minimum commitments, which include rental, real estate tax and other related amounts, under all noncancellable leases with remaining terms of more than one year and expiring through 2024 are as follows (in thousands):

2007	$ 1,118
2008	946
2009	852
2010	759
2011	581
Thereafter	3,591
	$ 7,847

Litigation

As the Company has disclosed in its periodic reports filed with the SEC, the Company was involved in legal proceedings concerning four separate portfolios of predominately commercial leases which Lakeland purchased from Commercial Money Center, Inc. (CMC). CMC obtained surety bonds from three surety companies to guarantee each lessee s performance. Relying on these bonds, Lakeland and other investors purchased the leases and CMC s right to payment under the various surety bonds. CMC (and a related entity, Commercial Servicing Corp. (CSC)) eventually stopped forwarding to the Company the required amounts.

On July 20, 2005, Lakeland entered into a settlement agreement with RLI Insurance Company and one remaining party in Lakeland s claims related to the CMC matter. Pursuant to the settlement agreements Lakeland was paid an aggregate of $3,315,000 and the parties executed mutual releases. As a result of the settlements, Lakeland s nonperforming assets were reduced by $6.4 million and no additional loan loss provision was required. A charge-off of $3.0 million was recorded.

In 2001, a complaint captioned Ronnie Clayton dba Clayton Trucking, et al v. Ronald Fisher, et al was filed in the Los Angeles County Superior Court against Lakeland and others. Plaintiffs are certain of the lessees who had entered into leases with CMC. Plaintiffs allege, among other things, that these leases are not true leases but are instead loans which charge usurious interest rates. They further allege that because of various California Financial Code violations by CMC, the lease instruments are either void or must be reformed and all amounts paid by the lessees must be returned to them. The action against Lakeland has been stayed while an appeal by plaintiffs is pending concerning the dismissal of certain of plaintiffs claims against defendants.

From time to time, the Company and its subsidiaries are defendants in legal proceedings relating to their respective businesses. While the ultimate outcome of these matters cannot be determined at this time, management does not believe that the outcome of any pending legal proceeding will materially affect the consolidated financial position of the Company, but could possibly be material to the results of operations of any one period.

NOTE 16 - FINANCIAL INSTRUMENTS WITH OFF-BALANCE-SHEET RISK AND CONCENTRATIONS OF CREDIT RISK

Lakeland is party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit and standby letters of credit. Such financial instruments are recorded in the financial statements when they become payable. Those instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the consolidated balance sheets. The contract or notional amounts of those instruments reflect the extent of involvement Lakeland has in particular classes of financial instruments.

Lakeland s exposure to credit loss in the event of non-performance by the other party to the financial instrument for commitments to extend credit and standby letters of credit is represented by the contractual or notional amount of those instruments. Lakeland uses

the same credit policies in making commitments and conditional obligations as it

does for on-balance-sheet instruments.

Lakeland generally requires collateral or other security to support financial instruments with credit risk. The approximate contract amounts are as follows:

	December 31, 2006	2005
	(in thousands)	
Financial instruments whose contract amounts represent credit risk		
Commitments to extend credit	**$ 385,789**	$ 351,418
Standby letters of credit and financial guarantees written	**9,754**	11,842

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. Lakeland evaluates each customer s creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by Lakeland upon extension of credit, is based on management s credit evaluation.

Standby letters of credit are conditional commitments issued by Lakeland to guarantee the payment by or performance of a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. Lakeland holds deposit accounts, residential or commercial real estate, accounts receivable, inventory and equipment as collateral to support those commitments for which collateral is deemed necessary. The extent of collateral held for those commitments at December 31, 2006 and 2005 varies based on Lakeland s credit evaluation.

The Company has financial and performance letters of credit. Financial letters of credit require the Company to make payment if the customer fails to make payment, as defined in the agreements. Performance letters of credit require the Company to make payments if the customer fails to perform certain non-financial contractual obligations. The Company defines the initial fair value of these letters of credit as the fees received from the customer. The Company records these fees as a liability when issuing the letters of credit and amortizes the fee over the life of the letter of credit.

The maximum potential undiscounted amount of future payments of these letters of credit as of December 31, 2006 is $9.8 million and they expire through 2009. Lakeland s exposure under these letters of credit would be reduced by actual performance, subsequent termination by the beneficiaries and by any proceeds that the Company obtained in liquidating the collateral for the loans, which varies depending on the customer.

As of December 31, 2006, the Company had $385.8 million in loan commitments, with $335.4 million maturing within one year, $12.8 million maturing after one year but within three years, $2.8 million maturing after three years but within five years, and $34.8 million maturing after five years. As of December 31, 2006, the Company had $9.8 million in standby letters of credit, with $8.0 million maturing within one year and $1.8 million maturing after one year but within three years.

Lakeland grants loans primarily to customers in its immediately adjacent suburban counties which include Bergen, Morris, Passaic, Sussex, Warren and Essex counties in Northern New Jersey and surrounding areas. Certain of Lakeland s consumer loans and lease customers are more diversified nationally. Although Lakeland has a diversified loan portfolio, a large portion of its loans are secured by commercial or residential real property. Although Lakeland has a diversified loan portfolio, a substantial portion of its debtors ability to honor their contracts is dependent upon the economy. Commercial and standby letters of credit were granted primarily to commercial borrowers.

NOTE 17 - ESTIMATED FAIR VALUE OF FINANCIAL INSTRUMENTS

SFAS No. 107 requires disclosure of the estimated fair value of an entity s assets and liabilities considered to be financial instruments. For the Company, as for most financial institutions, the majority of its assets and liabilities are considered financial instruments as defined in SFAS No. 107. However, many such instruments lack an available trading market, as characterized by a willing buyer and seller engaging in an exchange transaction. Also, it is the Company s general practice and intent to hold its financial instruments to maturity and not to engage in trading or

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sales activities, except for certain loans. Therefore, the Company had to use significant estimations and present value calculations to prepare this disclosure.

Changes in the assumptions or methodologies used to estimate fair values may materially affect the estimated amounts. Also, management is concerned that there may not be reasonable comparability between institutions due to the wide range of permitted assumptions and methodologies in the absence of active markets. This lack of uniformity gives rise to a high degree of subjectivity in estimating financial instrument fair values.

Estimated fair values have been determined by the Company using the best available data and an estimation methodology suitable for each category of financial instruments. The estimation methodologies used, the estimated fair values, and recorded book balances at December 31, 2006 and 2005 are outlined below.

For cash and cash equivalents and interest-bearing deposits with banks, the recorded book values approximate fair values. The estimated fair values of investment securities are based on quoted market prices, if available. Estimated fair values are based on quoted market prices of comparable instruments if quoted market prices are not available.

The net loan portfolio at December 31, 2006 and 2005 has been valued using a present value discounted cash flow where market prices were not available. The discount rate used in these calculations is the estimated current market rate adjusted for credit risk. The carrying value of accrued interest approximates fair value.

The estimated fair values of demand deposits (i.e. interest (checking) and non-interest bearing demand accounts, savings and certain types of money market accounts) are, by definition, equal to the amount payable on demand at the reporting date (i.e. their carrying amounts). The carrying amounts of variable rate accounts approximate their fair values at the reporting date. For fixed maturity certificates of deposit, fair value was estimated using the rates currently offered for deposits of similar remaining maturities. The carrying amount of accrued interest payable approximates its fair value.

The fair value of securities sold under agreements to repurchase and long-term debt are based upon discounted value of contractual cash flows. The Company estimates the discount rate using the rates currently offered for similar borrowing arrangements.

The fair values of commitments to extend credit and standby letters of credit are estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present creditworthiness of the counter parties. For fixed-rate loan commitments, fair value also considers the difference between current levels of interest rates and the committed rates. The fair value of guarantees and letters of credit is based on fees currently charged for similar agreements or on the estimated cost to terminate them or otherwise settle the obligations with the counter parties at the reporting date.

The carrying values and estimated fair values of the Company s financial instruments are as follows:

	December 31,			
	2006		2005	
	Carrying Value	Estimated fair value	Carrying Value	Estimated fair value
	(in thousands)			
Financial Assets:				
Cash and cash equivalents	**$ 79,964**	**$ 79,964**	$ 52,815	$ 52,815
Investment securities available for sale	**280,509**	**280,509**	515,903	515,903
Investment securities held to maturity	**142,838**	**140,564**	154,569	151,637
Loans	**1,591,644**	**1,580,824**	1,312,767	1,314,884
Financial Liabilities:				
Deposits	**1,860,627**	**1,858,196**	$ 1,798,160	1,794,444
Federal funds purchased and securities sold under agreements to repurchase	**41,061**	**41,061**	103,199	103,139
Long-term debt	**91,710**	**91,638**	45,061	45,822
Subordinated debentures	**56,703**	**51,483**	56,703	51,838
Commitments:				
Standby letters of credit		**27**		23

NOTE 18 - REGULATORY MATTERS

The Bank Holding Company Act of 1956 restricts the amount of dividends the Company can pay. Accordingly, dividends should generally only be paid out of current earnings, as defined.

The New Jersey Banking Act of 1948 restricts the amount of dividends paid on the capital stock of New Jersey chartered banks. Accordingly, no dividends shall be paid by such banks on their capital stock unless, following the payment of such dividends, the capital stock of Lakeland will be unimpaired, and: (1) Lakeland will have a surplus, as defined, of not less than 50% of its capital, or, if not, (2) the payment of such dividend will not reduce the surplus, as defined, of Lakeland. Under these limitations, approximately $141.3 million was available for payment of dividends from Lakeland to the Company as of December 31, 2006.

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

Quantitative measures established by regulations to ensure capital adequacy require the Company and Lakeland to maintain minimum amounts and ratios (set forth in the table below) of total and Tier 1 capital (as defined in the regulations) to risk-weighted assets, and of Tier 1 capital to average assets. Management believes, as of December 31, 2006, that the Company and Lakeland met all capital adequacy requirements to which they are subject.

As of December 31, 2006, the most recent notification from the Federal Reserve Bank of New York and the FDIC categorized the Company and Lakeland as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, the Company and Lakeland must maintain minimum total risk-based, Tier 1 risk-based and Tier 1 leverage ratios as set forth in the table. There are no conditions or events since that notification that management believes have changed the institutions category.

As of December 31, 2006 and 2005, the Company and Lakeland have the following capital ratios:

	Actual			For capital adequacy purposes			To be well capitalized under prompt corrective action provisions	
	Amount	Ratio		Amount	Ratio		Amount	Ratio
				(dollars in thousands)				
As of December 31, 2006								
Total capital (to risk-weighted assets)								
Company	**$ 178,856**	**10.96%**	**≥**	**$ 130,597**	**≥ 8.00%**		**N/A**	**N/A**
Lakeland	**163,867**	**10.07**		**130,183**	**8.00**	**≥**	**$ 162,729**	**≥ 10.00%**
Tier 1 capital (to risk-weighted assets)								
Company	**$ 165,402**	**10.13%**	**≥**	**$ 65,299**	**≥ 4.00%**		**N/A**	**N/A**
Lakeland	**150,413**	**9.24**		**65,092**	**4.00**	**≥**	**$ 97,637**	**≥ 6.00%**
Tier 1 capital (to average assets)								
Company	**$ 165,402**	**7.51%**	**≥**	**$ 88,089**	**≥ 4.00%**		**N/A**	**N/A**
Lakeland	**150,413**	**6.85**		**87,866**	**4.00**	**≥**	**$ 109,832**	**≥ 5.00%**

	Actual			For capital adequacy purposes			To be well capitalized under prompt corrective action provisions	
	Amount	Ratio		Amount	Ratio		Amount	Ratio
				(dollars in thousands)				
As of December 31, 2005								
Total capital (to risk-weighted assets)								
Company	$ 171,409	12.47%	≥	$ 109,970	≥ 8.00%		N/A	N/A
Lakeland	157,805	11.53		109,489	8.00	≥	$ 136,862	≥ 10.00%
Tier 1 capital (to risk-weighted assets)								
Company	$ 158,236	11.51%	≥	$ 54,984	≥ 4.00%		N/A	N/A
Lakeland	144,632	10.57		54,745	4.00	≥	$ 82,117	≥ 6.00%
Tier 1 capital (to average assets)								
Company	$ 158,236	7.49%	≥	$ 84,542	≥ 4.00%		N/A	N/A
Lakeland	144,632	6.86		84,274	4.00	≥	$ 105,342	≥ 5.00%

NOTE 19 - QUARTERLY FINANCIAL DATA (UNAUDITED)

The following represents summarized quarterly financial data of the Company, which in the opinion of management reflected all adjustments, consisting only of nonrecurring adjustments, necessary for a fair presentation of the Company s results of operations.

	Quarter ended			
	March 31, 2006	June 30, 2006	September 30, 2006	December 31, 2006
	(in thousands, except per share amounts)			
Total interest income	**$ 27,953**	**$ 28,932**	**$ 30,789**	**$ 32,134**
Total interest expense	**11,405**	**12,211**	**14,159**	**15,329**
Net interest income	**16,548**	**16,721**	**16,630**	**16,805**
Provision for loan and lease losses	**332**	**319**	**337**	**738**
Noninterest income	**4,399**	**4,324**	**4,301**	**4,115**
Gains (losses) on sales of investment securities	**78**	**0**	**271**	**(3,344)**
Noninterest expense	**13,793**	**13,417**	**13,379**	**14,096**
Income before taxes	**6,900**	**7,309**	**7,486**	**2,742**
Income taxes	**2,208**	**2,254**	**2,379**	**619**
Net income	**$ 4,692**	**$ 5,055**	**$ 5,107**	**$ 2,123**
Earnings per share				
Basic	**$ 0.21**	**$ 0.23**	**$ 0.23**	**$ 0.10**
Diluted	**$ 0.21**	**$ 0.23**	**$ 0.23**	**$ 0.10**

In fourth quarter of 2006, the Company sold $97.3 million in securities at a loss of $3.3 million and wrote-off $300,000 in costs related to a stock offering which the Company elected not to complete.

	Quarter ended			
	March 31, 2005	June 30, 2005	September 30, 2005	December 31, 2005
	(in thousands, except per share amounts)			
Total interest income	$ 24,640	$ 25,064	$ 26,486	$ 27,649
Total interest expense	7,032	7,637	8,759	10,204
Net interest income	17,608	17,427	17,727	17,445
Provision for loan and lease losses	783	327	304	141
Noninterest income	3,501	3,624	3,978	4,025
Gains (losses) on sales of investment securities	28	100	4	(715)
Noninterest expense	13,673	13,233	13,410	13,076
Income before taxes	6,681	7,591	7,995	7,538
Income taxes	2,113	2,454	2,637	2,380
Net income	$ 4,568	$ 5,137	$ 5,358	$ 5,158
Earnings per share				
Basic	$ 0.20	$ 0.23	$ 0.24	$ 0.23
Diluted	$ 0.20	$ 0.22	$ 0.24	$ 0.23

During the fourth quarter of 2005, the Company recorded a $750,000 reduction of benefit expense related to the termination of its post-retirement benefit plan.

NOTE 20 - CONDENSED FINANCIAL INFORMATION PARENT COMPANY ONLY:

BALANCE SHEETS

CONDENSED BALANCE SHEETS

	December 31,	
	2006	2005
	(in thousands)	
ASSETS		
Cash and due from banks	**$ 8,665**	$ 4,288
Investment securities available for sale	**5,802**	5,378
Investment in bank subsidiaries	**238,799**	231,326
Land held for sale	**1,327**	1,402
Other assets	**3,330**	7,523
TOTAL ASSETS	**$ 257,923**	$ 249,917
LIABILITIES AND STOCKHOLDERS' EQUITY		
Other liabilities	**$ 1,720**	$ 1,433
Subordinated debentures	**56,703**	56,703
Stockholders equity	**199,500**	191,781
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	**$ 257,923**	$ 249,917

CONDENSED STATEMENTS OF OPERATIONS

	Years Ended December 31,		
	2006	2005	2004
		(in thousands)	
INCOME			
Dividends from subsidiaries	**$ 20,325**	$ 14,850	$ 12,635
Other income	**420**	241	748
TOTAL INCOME	**20,745**	15,091	13,383
EXPENSE			
Interest on subordinated debentures	**3,842**	3,842	3,845
Noninterest expenses	**1,034**	724	641
TOTAL EXPENSE	**4,876**	4,566	4,486
Income before benefit for income taxes	**15,869**	10,525	8,897
Benefit for income taxes	**(1,554)**	(1,514)	(1,438)
Income before equity in undistributed income of subsidiaries	**17,423**	12,039	10,335
Equity in undistributed income (loss) of subsidiaries	**(446)**	8,182	6,160

NET INCOME	**$ 16,977**	$ 20,221	$ 16,495

CONDENSED STATEMENTS OF CASH FLOWS

	Years Ended December 31,		
	2006	**2005**	**2004**
		(in thousands)	
CASH FLOWS FROM OPERATING ACTIVITIES			
Net income	**$ 16,977**	$ 20,221	$ 16,495
Adjustments to reconcile net income to net cash provided by (used in) operating activities:			
Gain on sale of securities	**(243)**		(576)
(Increase) decrease in other assets	**2,668**	(1,095)	(1,619)
Increase (decrease) in other liabilities	**(49)**	(52)	747
Equity in undistributed (income) loss of subsidiaries	**446**	(8,182)	(6,160)
NET CASH PROVIDED BY OPERATING ACTIVITIES	**19,799**	10,892	8,887
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchases of securities	**(17)**	(118)	(12)
Proceeds from sale of securities available for sale	**671**		954
Purchase of banks			(19,342)
Contribution to subsidiary	**(5,000)**		
NET CASH USED IN INVESTING ACTIVITIES	**(4,346)**	(118)	(18,400)
CASH FLOWS FROM FINANCING ACTIVITIES			
Cash dividends paid on common stock	**(8,517)**	(8,307)	(7,362)
Purchase of treasury stock	**(3,144)**	(10,098)	(4,413)
Excess tax benefits	**66**		
Exercise of stock options	**519**	461	656
NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES	**(11,076)**	(17,944)	(11,119)
Net increase (decrease) in cash and cash equivalents	**4,377**	(7,170)	(20,632)
Cash and cash equivalents, beginning of year	**4,288**	11,458	32,090
CASH AND CASH EQUIVALENTS, END OF YEAR	**$ 8,665**	$ 4,288	$ 11,458

Report of Independent Registered Public Accounting Firm

Board of Directors

Lakeland Bancorp, Inc

We have audited the accompanying consolidated balance sheets of Lakeland Bancorp, Inc. and subsidiaries (a New Jersey corporation) as of December 31, 2006 and 2005, and the related consolidated statements of income, stockholders equity, and cash flows for each of the three years in the period ended December 31, 2006. These financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these financial statements based on our 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 audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

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

As discussed in Note 12, 13 and 14 to the consolidated financial statements, the Company has adopted Financial Accounting Standards Board Statement (FASB) No. 158, *Employers Accounting for Defined Benefit Pension and Other Post Retirement Plans - an amendment of FASB Statements No. 87, 88, 106 and 132(R)* and FASB No. 123(R) *Share Based Payments* in 2006.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of Lakeland Bancorp, Inc. s 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) and our report dated March 2, 2007 expressed an unqualified opinion on management s assessment of the effectiveness of internal control over financial reporting and an unqualified opinion on the effectiveness of internal control over financial reporting.

/s/ Grant Thornton LLP

Philadelphia, Pennsylvania

March 2, 2007

ITEM 9 Changes in and Disagreements with Accountants on

Accounting and Financial Disclosure

Not Applicable

ITEM 9A Controls and Procedures

Evaluation of Disclosure Controls and Procedures

As of the end of the period covered by this Annual Report on Form 10-K, the Company s management, including the Chief Executive Officer and Chief Financial Officer, evaluated the Company s disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) related to the recording, processing, summarization, and reporting of information in the Company s periodic reports that the Company files with the SEC.

Based on their evaluation as of December 31, 2006, the Company s Chief Executive Officer and Chief Financial Officer have concluded that the Company s disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) are effective to ensure that the information required to be disclosed by the Company in the reports that the Company files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms.

Changes in Internal Controls Over Financial Reporting

There have been no changes in the Company s internal control over financial reporting that occurred during the last fiscal quarter to which this Annual Report on Form 10-K relates that have materially affected, or are reasonably likely to materially affect, the Company s internal control over financial reporting.

Management s Report on Internal Control Over Financial Reporting

The management of Lakeland Bancorp, Inc. and its subsidiaries (the Company) is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rule 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934.

The 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 and includes those policies and procedures that:

Pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the Company;

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 the board of directors of the Company; and

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 risk that controls may become inadequate because of changes in conditions or because of declines in the degree of compliance with policies or procedures.

The Company s management assessed the effectiveness of the Company s internal control over financial reporting as of December 31, 2006. In making this assessment, the Company s management used the criteria set forth by the Committee of

Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control-Integrated Framework.

As of December 31, 2006, based on management s assessment, the Company s internal control over financial reporting was effective.

Grant Thornton LLP, the Company s independent registered public accounting firm, has issued an audit report on our assessment of the Company s internal control over financial reporting. See Report of Independent Registered Public Accounting Firm on Internal Control Over Financial Reporting below.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors

Lakeland Bancorp, Inc.

We have audited management s assessment, included in the accompanying Management s Report on Internal Control Over Financial Reporting, that Lakeland Bancorp, Inc. (a New Jersey corporation) and its subsidiaries 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). Lakeland Bancorp, Inc. s management is responsible 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 management s assessment and an opinion on the effectiveness of the company s internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit 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 audit provides 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, management s assessment that Lakeland 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). Also in our opinion, Lakeland 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).

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Lakeland Bancorp, Inc. and its subsidiaries as of December 31, 2006 and 2005, and the related consolidated statements of income, shareholders equity, and cash flows for each of the three years in the period ended December 31, 2006 and our report dated March 2, 2007 expressed an unqualified opinion on those financial statements.

/s/ GRANT THORNTON LLP

Philadelphia, Pennsylvania

March 2, 2007

ITEM 9B Other Information

None.

PART III

ITEM 10 - Directors and Executive Officers of the Registrant

The Company responds to this Item by incorporating by reference the material responsive to this Item in the Company s definitive proxy statement for its 2007 Annual Meeting of Shareholders.

ITEM 11 - Executive Compensation

The Company responds to this Item by incorporating by reference the material responsive to this Item in the Company s definitive proxy statement for its 2007 Annual Meeting of Shareholders.

ITEM 12 - Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

The Company responds to this Item by incorporating by reference the material responsive to this Item in the Company s definitive proxy statement for its 2007 Annual Meeting of Shareholders.

ITEM 13 - Certain Relationships and Related Transactions

The Company responds to this Item by incorporating by reference the material responsive to this Item in the Company s definitive proxy statement for its 2007 Annual Meeting of Shareholders.

ITEM 14 - Principal Accountant Fees and Services

The Company responds to this Item by incorporating by reference the material responsive to this Item in the Company s definitive proxy statement for its 2007 Annual Meeting of Shareholders.

PART IV

ITEM 15 - Exhibits and Financial Statement Schedules

(a) 1. The following portions of the Company s consolidated financial statements are set forth in Item 8 of this Annual Report:

(i) Consolidated Balance Sheets as of December 31, 2006 and 2005.
(ii) Consolidated Statements of Income for each of the three years in the period ended December 31, 2006.
(iii) Consolidated Statements of Changes in Stockholders Equity for each of the three years in the period ended December 31, 2006.
(iv) Consolidated Statements of Cash Flows for each of the three years in the period ended December 31, 2006.
(v) Notes to Consolidated Financial Statements.
(vi) Report of Independent Registered Public Accounting Firm.

(a) 2. Financial Statement Schedules

All financial statement schedules are omitted as the information, if applicable, is presented in the consolidated financial statements or notes thereto.

(a) 3. Exhibits

2.1 Agreement and Plan of Merger, dated as of March 31, 2003, among the Registrant, Lakeland

	Bank, CSB Financial Corp. and Community State Bank, is incorporated by referenced to Exhibit 2.1 to the Registrant s Current Report on Form 8-K filed with the SEC on April 3, 2003.
2.2	Agreement and Plan of Merger, dated as of October 24, 2003, between the Registrant and Newton Financial Corporation, is incorporated by reference to Exhibit 2.1 to the Registrant s Current Report on Form 8-K filed with the SEC on October 29, 2003.
3.1	Certificate of Incorporation of the Registrant, as amended, is incorporated by reference to Exhibit 4.1 to Registrant s Registration Statement on Form S-8 (No. 333-125616) filed with the SEC on June 8, 2005.
3.2	By-Laws of the Registrant, as amended, are incorporated by reference to Exhibit 3.2 to Registrant s Annual Report on Form 10-K for the year ended December 31, 2003.
4.1	Registrant s Shareholder Protection Rights Plan, dated as of August 24, 2001, is incorporated by reference to Exhibit 4.1 to Registrant s Current Report on Form 8-K filed with the SEC on August 24, 2001.
10.1	Lakeland Bancorp, Inc. Amended and Restated 2000 Equity Compensation Program is incorporated by reference to Appendix A to the Registrant s definitive proxy materials for its 2005 Annual Meeting of Shareholders.
10.2	Employment Agreement Change in Control, Severance and Employment Agreement for Roger Bosma, dated as of January 1, 2000, among Lakeland Bancorp, Inc., Lakeland Bank and Roger Bosma, is incorporated by reference to Exhibit 10.6 to the Registrant s Annual Report on Form 10-K for the year ended December 31, 1999.
10.3	Change of Control Agreement dated March 1, 2001, among Lakeland Bancorp, Inc., Lakeland Bank and Joseph F. Hurley is incorporated by reference to Exhibit 10.8 to the Registrant s Annual Report on Form 10-K for the year ended December 31, 2000.
10.4	Change of Control Agreement dated March 1, 2001, among Lakeland Bancorp, Inc., Lakeland Bank and Robert A. Vandenbergh is incorporated by reference to Exhibit 10.9 to the Registrant s Annual Report on Form 10-K for the year ended December 31, 2000.
10.5	Change of Control Agreement dated March 6, 2001, among Lakeland Bancorp, Inc., Lakeland Bank and Louis E. Luddecke is incorporated by reference to Exhibit 10.10 to the Registrant s Annual Report on Form 10-K for the year ended December 31, 2000.
10.6	Change of Control Agreement dated March 7, 2001, among Lakeland Bancorp, Inc. Lakeland Bank and Jeffrey J. Buonforte is incorporated by reference to Exhibit 10.11 to the Registrant s Annual Report on Form 10-K for the year ended December 31, 2000.
10.7	Amendments to Change of Control Agreements, dated March 10, 2003, among Lakeland Bancorp, Inc., Lakeland Bank and each of Joseph F. Hurley, Robert A. Vandenbergh, Louis E. Luddecke and Jeffrey J. Buonforte are incorporated by reference to Exhibit 10.13 to the Registrant s Annual Report on Form 10-K for the year ended December 31, 2002.
10.8	Change of Control Agreement dated April 7, 2004, among Lakeland Bancorp, Inc., Lakeland Bank and James R. Noonan is incorporated by reference to Exhibit 10.11 to the Registrant s Annual Report on Form 10-K for the year ended December 31, 2004.
10.9	Lakeland Bancorp, Inc. Directors Deferred Compensation Plan, as amended June 9, 2004, is incorporated by reference to Exhibit 10.10 to the Registrant s Annual Report on Form 10-K for the year ended December 31, 2004.
10.10	Change in Control, Severance and Employment Agreement, dated August 2, 2006, among Lakeland Bancorp, Inc., Lakeland Bank and Steven Schachtel, is incorporated by referenced to Exhibit 10.1 to the Registrant s Quarterly Report on Form 10-Q for the period ended June 30, 2006.
10.11	Supplemental Executive Retirement Plan Agreement for Roger Bosma, dated August 21, 2003, and First Amendment to the Supplemental Executive Retirement Plan Agreement, adopted December 13, 2006.
21.1	Subsidiaries of Registrant.
23.1	Consent of Grant Thornton LLP.
24.1	Power of Attorney.
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

SIGNATURES

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

LAKELAND BANCORP, INC.

Dated: March 15, 2007

By: /s/Roger Bosma
Roger Bosma
President and Chief Executive Officer

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

Signature	Capacity	Date
/s/ Roger Bosma Roger Bosma	Director, Chief Executive Officer, and President	March 15, 2007
/s/ Bruce G. Bohuny* Bruce G. Bohuny	Director	March 15, 2007
/s/ Mary Ann Deacon* Mary Ann Deacon	Director	March 15, 2007
/s/ John W. Fredericks* John W. Fredericks	Director	March 15, 2007
/s/ Mark J. Fredericks* Mark J. Fredericks	Director	March 15, 2007
/s/ George H. Guptill, Jr.* George H. Guptill, Jr.	Director	March 15, 2007
/s/ Janeth C. Hendershot* Janeth C. Hendershot	Director	March 15, 2007

/s/ Robert E. McCracken*		March 15, 2007
	Director	
Robert E. McCracken		

/s/ Robert B. Nicholson, III*	Director	March 15, 2007
Robert B. Nicholson, III		
/s/ Joseph P. O Dowd*	Director	March 15, 2007
Joseph P. O Dowd		
/s/ Stephen R. Tilton, Sr.*	Director	March 15, 2007
Stephen R. Tilton, Sr.		
/s/ Paul G. Viall, Jr.*	Director	March 15, 2007
Paul. G. Viall, Jr.		
/s/ Arthur L. Zande*	Director	March 15, 2007
Arthur L. Zande		
/s/Joseph F. Hurley	Executive Vice President and	March 15, 2007
Joseph F. Hurley	Chief Financial Officer	

*By: /s/Roger Bosma
Roger Bosma
Attorney-in-Fact