

SOUTHERN CONNECTICUT BANCORP INC
Form 10KSB
March 27, 2008

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10 - KSB

ANNUAL REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the Fiscal Year Ended December 31, 2007.

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 333-59824

SOUTHERN CONNECTICUT BANCORP, INC.
(Name of Small Business Issuer in Its Charter)

06-1609692

Connecticut
(State or other jurisdiction of incorporation or
organization)

(I.R.S. Employer Identification
Number)

215 Church Street

New Haven, Connecticut

06510

(Address of Principal Executive Offices)

(Zip Code)

Issuer's telephone number

(203) 782-1100

Securities registered under Section 12(b) of the Exchange Act:

Common Stock, par value \$.01 per share

American Stock Exchange

(Title of Class)

(Name of each exchange on which
registered)

Securities registered under Section 12(g) of the Exchange Act:

None

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Check if there is no disclosure of delinquent filers in response to Item 405 of Regulation S-B contained in this form, and no disclosure will 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-KSB or any amendment to this Form 10-KSB. [X]

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

State issuer's revenue for its most recent fiscal year: \$10,103,876

Aggregate market value of the voting and non-voting common equity held by non-affiliates (assumes all directors, executive officers and 10% or greater holders are affiliates) of the registrant as of March 10, 2008: \$18,195,291.

State the number of shares outstanding of each of the issuer's classes of common equity: Common Stock, par value \$.01 per share, outstanding as of March 10, 2008: 2,969,714

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive Proxy Statement for its 2008 Annual Meeting of Shareholders which is expected to be filed with the Securities and Exchange Commission within 120 days after the close of the fiscal year covered by this Form 10-KSB, are incorporated by reference into Part III of this report on Form 10-KSB.

Transitional Small Business Disclosure Format (check one):

Yes _____; No X

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PART I

Item 1. Description of Business.

Background

Southern Connecticut Bancorp, Inc. (the “Company”) is a bank holding company headquartered in New Haven, Connecticut that was incorporated on November 8, 2000. The Company’s strategic objective is to serve as a bank holding company for The Bank of Southern Connecticut, a community-based commercial bank serving New Haven, Connecticut and the surrounding communities (the “Greater New Haven Market”). As of December 31, 2007, the Company had consolidated total assets of \$130.6 million, net loans of \$86.0 million, and total deposits of \$107.4 million. Net interest margin for the year ended December 31, 2007 was 4.89%.

Southern Connecticut Bancorp, Inc. owns 100% of the capital stock of The Bank of Southern Connecticut (the “Bank”), a Connecticut-chartered bank with its headquarters in New Haven, Connecticut. The Bank commenced operations on October 1, 2001. The Bank of Southern Connecticut is headquartered in New Haven, Connecticut with branch offices in the Amity/Westville section of New Haven and in Branford, Connecticut, just east of New Haven. The Bank of North Haven, a division of The Bank of Southern Connecticut, operates in North Haven, Connecticut as a branch of the Bank.

The Bank sold its branch in New London, Connecticut at the close of business February 29, 2008, to the Savings Institute Bank & Trust. The sale of the New London branch reflects a change in strategy with respect to the Bank’s primary market area. The sale of the New London branch allows the Bank to concentrate its resources in the Greater New Haven Market.

The Bank focuses on serving the banking needs of small to medium-sized businesses, professionals and professional corporations, and their owners and employees in greater New Haven. The Bank’s target commercial customer has between \$1.0 and \$30.0 million in revenues, 15 to 150 employees, and borrowing needs of up to \$3.0 million. The primary focus on this commercial market makes the Bank uniquely qualified to move deftly in responding to the needs of its clients. The Bank has been successful in winning business by offering a combination of competitive pricing for its services, quick decision making processes and a high level of personalized, “high touch” customer service.

The Greater New Haven Market

The Bank serves the Greater New Haven Market, which is comprised of the communities located in and around New Haven County in Southern Central Connecticut. The Greater New Haven Market is located in the center of, and is a critical component of, the commercial activity of the northeast corridor in New England. The market focus resides in the busy transportation and commercial area between New York City to the south, Hartford to the north, Providence to the east, and Boston to the northeast. The diversified economic base of this market region includes pharmaceutical, advanced manufacturing, healthcare, defense, technology, service and energy companies. The region is also one of New England’s most popular tourist destinations, featuring popular shoreline and heritage sites. In addition, the Bank’s headquarters is located in downtown New Haven, in the area of Yale University’s campus.

Growth and Operating Strategy

The Bank seeks to differentiate itself by offering prompt, personal “high touch” service and quality banking products. The Bank’s target customers are small to medium-sized businesses, professionals and professional corporations, and their owners and employees. The Bank emphasizes personal relationships with customers, community involvement by employees and the board of directors, and responsive lending decisions by an accessible and experienced local management team.

The key elements of the Bank’s business strategy include:

- Provision of individualized attention with local underwriting and credit decision-making authority. As the only commercial bank based in and wholly focused on the greater New Haven area, the Bank is better able to provide the individualized customer service, combined with prompt local underwriting and credit decision-making authority that management believes small to medium-sized businesses desire.
- Employing qualified and experienced banking professionals. The Company and the Bank seek to continue to hire and retain highly experienced and qualified local commercial lenders and other banking professionals with successful track records and established relationships with small to medium-sized businesses in targeted market areas. The experience and expertise of these individuals serves to enhance the Bank’s image within the communities it serves, thereby increasing the Bank’s business.
- Leveraging personal relationships and community involvement. The directors, officers and senior employees of the Company and the Bank have extensive personal contacts, business relationships and involvement in communities in which they live and work and which the Bank serves. By building on and leveraging these relationships and community involvement, management believes that the Bank has generated and will continue to generate enthusiasm and interest from small to medium-sized businesses and professionals in the targeted market areas.
- Offering a suite of products attractive to our core customer base. The Bank seeks to offer competitive basic, popular products to its commercial and consumer customer base. The Bank offers internet banking services to its customers through a partnership with Digital Insight, a subsidiary of Intel. The Bank offers remote deposit capture, a system that allows our customers to deposit checks from their places of business, rather than having to make a trip to the Bank. The Bank offers a full complement of banking services utilized by small business customers.

- Maintaining high credit quality. The success of the Bank's business plan depends to a significant extent on the quality of the Bank's assets, particularly loans. The Bank has built a strong internal emphasis on credit quality and has established stringent underwriting standards and loan approval processes. The Bank actively manages past-due and non-performing loans in an effort to minimize credit loss and related expenses and to ensure that the allowance for loan losses is adequate.
- Taking market share from large, non-local competitors. The Greater New Haven Market is dominated by large, non-locally owned financial institutions with headquarters typically located outside of Connecticut. Management believes that the Bank has attracted and can continue to attract small to medium-sized businesses and professionals that prefer local decision-making authority and interaction with banking professionals who can provide prompt personalized and knowledgeable service.
- Optimizing net interest margin. The Bank's focus on commercial customers helps to support a strong net interest margin. The high percentage of assets concentrated in loans to commercial entities that typically provide higher yield than consumer loans, particularly residential mortgages and home equity related loans. The Bank maintains a high percentage of commercial transaction accounts and money market deposit accounts to fund its operations. These deposits typically have a lower interest rate expense than certificates of deposits. The combination of the higher yielding assets and lower expense deposits produces a strong margin for the Company.

Lending, Depository and Other Products

Lending Products. The Bank offers a broad range of loans to businesses and individuals in its service area, including commercial and business loans, industrial loans, personal loans, commercial and home mortgage loans, home equity loans and automobile loans. The Bank has received lending approval status from the Small Business Administration ("SBA") to enable it to make SBA loans in communities located throughout the State of Connecticut. The Bank holds certified lending status ("CLP") from the SBA.

Loans are made on a variable or fixed rate basis, with fixed rate loans typically limited to three to five year terms. All loans are approved pursuant to lending policies and procedures authorized by the Bank's board of directors. The Bank, at times, participates in multi-bank loans to companies in its market area. Commercial loans and commercial real estate loans may be written for maturities of up to twenty years. Loans to purchase or refinance commercial real estate are typically supported by personal guarantees of the principal owners and related parties, and are collateralized by the subject real estate, which may in certain cases be supplemented by additional collateral in the form of liquid assets. Loans to local businesses are generally supported by the personal guarantees of the principal owners and are carefully underwritten to determine appropriate collateral and covenant requirements.

Depository Products. The Bank has attracted a base of core deposits, including interest bearing and non-interest bearing checking accounts, money market accounts, savings accounts, sweep accounts, NOW accounts, repurchase agreements, and a variety of certificates of deposits and IRA accounts. To continue to attract deposits, the Bank employs an aggressive marketing plan in its service area and features a broad product line and rates and services competitive with those offered in the Greater New Haven Market. The primary sources of deposits have been and are expected to continue to be small to medium-sized businesses, professionals (lawyers, doctors, accountants, etc.) and professional corporations, and their owners and employees. The Bank obtains these deposits through personal solicitation by its officers and directors, outside programs and advertisements published and/or broadcasted in the local media. The Bank offers internet banking services to its customers, including commercial cash management services and personal banking services. The Bank offers remote deposit capture, which offers check deposit capabilities for customers from their place of business. The Bank also offers drive-in teller services, automated teller services, wire transfer, lock box and safe deposit services.

Other Services. The Bank provides a broad range of other services and products, including cashier's checks, money orders, travelers' checks, bank-by-mail, direct deposit and U. S. Savings Bonds. The Bank is associated with a shared network of automated teller machines that its customers are able to use throughout Connecticut and other regions. The Bank does not expect to offer trust services directly in the near future, but may offer trust services in the future independently or possibly through a joint venture with a larger institution. To directly offer trust services, the Bank would need the approval of the Connecticut Banking Commissioner and the FDIC.

Investment Services

The Company does not engage in investment services.

Investment Securities

Investment securities are held by the Company and the Bank with the objective of maximizing the long-term rate of return for shareholders. Investments are overseen by the Board of Directors and a committee of officers who take into account returns, liquidity needs, and the overall asset/liability management of the Company and the Bank. Permissible investments include debt securities such as U.S. Government securities, government sponsored agency securities, municipal bonds, domestic certificates of deposit that are insured by the FDIC, mortgage-backed securities and collateralized mortgage obligations. The Bank's current investment portfolio is limited to U.S. Government sponsored agency obligations and sponsored agency issued collateralized mortgage obligations, which have been classified as available for sale. Accordingly, the principal risk associated with the Bank's current investing activities is market risk (variations in value resulting from general changes in interest rates) rather than credit risk. The Bank does not take credit risk for the purposes of increasing interest income. Management continually reviews its portfolio and prevailing market conditions, and under certain market conditions, the Company's strategy may be reviewed and revised by management and the board of directors.

Asset and Liability Management

Interest rate risk measures the impact that changing interest rates have on current and future earnings. The Company's goal is to optimize long-term profitability while minimizing exposure to interest rate fluctuations. Interest rate risk exposure, including, among other things, the Company's exposure to changes in interest income and equity value based on fluctuations in interest rates, is monitored by senior management and reported to the Bank's Asset Liability Committee (ALCO) and the board of directors on a quarterly basis. The Bank employs the services of a national service provider for monitoring, analyzing and managing interest rate risk.

Regulatory Compliance

The Company operates in a heavily regulated industry and is subject to increasing regulatory review and scrutiny from the Federal Reserve Board, the Connecticut Banking Commissioner, and the FDIC. The Company and the Bank have invested and continue to invest significant time and resources to ensure compliance and conformity with applicable regulations (see "REGULATION AND SUPERVISION"). The Bank is committed to meeting its obligations under the Bank Secrecy Act, the Gramm-Leach-Bliley Act and the USA PATRIOT Act, as well as various other regulations. Management meets and reports to the board of directors on a regular basis regarding new developments in compliance and the Bank's efforts to comply therewith.

Competition

There are numerous banks and other financial institutions serving the Greater New Haven Market posing significant competition to attract deposits and loans. The Bank competes for loans and deposits with other commercial banks, savings and loan associations, finance companies, money market funds, insurance companies, credit unions and other financial institutions, a number of which are much larger and have substantially greater resources. To increase its business, the Bank will have to win existing customers away from existing banks and financial institutions as well as successfully compete for new customers from growth in the target markets.

The greater New Haven market is currently served by approximately 80 offices of 14 commercial and savings banks. The majority of these banks are substantially larger than the Bank expects to be in the near future, and are able to offer products and services which may be impractical for the Bank to provide at this time. There are numerous banks and other financial institutions serving the communities surrounding New Haven, which also draw customers from New Haven, posing significant competition for the Bank to attract deposits and loans. The Bank also experiences competition from out-of-state financial institutions with little or no traditional bank branches in New Haven. Many of these banks and financial institutions are well established and better capitalized than the Bank, allowing them to provide a greater range of services.

Intense market demands, economic pressures, and significant legislative and regulatory actions have eroded traditional banking industry classifications and have increased competition among banks and other financial institutions. Market dynamics as well as legislative and regulatory changes have resulted in a number of new competitors offering services historically offered only by commercial banks. Increased customer awareness of product and service differences among competitors has also increased competition among banks.

Employees

As of December 31, 2007, the Bank had 39 full-time equivalent employees. Relationships with all employees are believed to be excellent.

REGULATION AND SUPERVISION

Banks and bank holding companies are extensively regulated under both federal and state law. The Company and the Bank have set forth below brief summaries of various aspects of supervision and regulation to which they are subject. These summaries do not purport to be complete and are qualified in their entirety by reference to applicable laws, rules and regulations.

Laws and Regulations to which The Company is Subject

General. As a bank holding company registered in accordance with the Bank Holding Company Act of 1956 (the “BHC Act”), the Company is regulated by and subject to the supervision of the Federal Reserve Board and is required to file with the Federal Reserve Board an annual report and such other information as may be required. The Federal Reserve Board has the authority to conduct examinations of the Company as well. The Federal Reserve Board has the authority to issue orders to bank holding companies to cease and desist from unsound banking practices and violations of conditions imposed by, or violations of agreements with, the Federal Reserve Board. The Federal Reserve Board is also empowered to assess civil money penalties against companies or individuals who violate the BHC Act or orders or regulations thereunder, to order termination of non-banking activities of non-banking subsidiaries of bank holding companies, and to order termination of ownership and control of a non-banking subsidiary by a bank holding company.

The BHC Act—Acquisitions and Permissible Activities. The BHC Act requires the prior approval of the Federal Reserve Board for a bank holding company to acquire substantially all the assets of a bank or acquire direct or indirect ownership or control of more than 5% of any class of the voting shares of any bank, bank holding company or savings association, or increase any such non-majority ownership or control of any bank, bank holding company or savings association, or merge or consolidate with any bank holding company. Federal law generally authorizes bank holding companies to acquire banks located in any state, subject to certain state-imposed age and deposit concentration limits, and also generally authorizes interstate bank holding company and bank mergers and to a lesser extent, interstate branching.

Unless a bank holding company becomes a financial holding company under the Gramm-Leach-Bliley Act of 1999 (“GLBA”) (as discussed below), the BHC Act prohibits a bank holding company from acquiring a direct or indirect interest in or control of more than 5% of any class of the voting shares of a company that is not a bank or a bank holding company and from engaging directly or indirectly in activities other than those of banking, managing or controlling banks or furnishing services to its subsidiary banks, except that it may engage in and may own shares of companies engaged in certain activities the Federal Reserve Board has determined to be so closely related to banking or managing or controlling banks as to be a proper incident thereto.

The GLBA permits a qualifying bank holding company to become a “financial holding company” and thereby engage in a broader range of activities than is permissible for a traditional bank holding company. In order to qualify for this election, all of the depository institution subsidiaries of the bank holding company must be well capitalized and well managed, as defined under Federal Reserve Board regulations, and all such subsidiaries must have achieved a rating of “satisfactory” or better with respect to meeting community credit needs. Pursuant to the GLBA, financial holding companies are permitted to engage in activities that are “financial in nature” or incidental or complementary thereto, as determined by the Federal Reserve Board. The GLBA identifies several activities as “financial in nature,” including, among others, insurance underwriting and agency activities, investment advisory services, merchant banking and underwriting, and dealing in or making a market in securities. At this time, the Company has not elected to become a financial holding company and has no immediate plans to do so.

Capital Requirements. The Federal Reserve Board has adopted capital adequacy guidelines pursuant to which it assesses the adequacy of capital in examining and supervising a bank holding company and in analyzing applications submitted to it under the BHC Act. These capital adequacy guidelines generally require bank holding companies to maintain total capital equal to at least 8% of total risk-adjusted assets and off-balance sheet items (the "Total Risk-Based Capital Ratio"), with at least one-half of that amount consisting of Tier I or core capital and the remaining amount consisting of Tier II or supplementary capital. Tier I capital for bank holding companies generally consists of the sum of common shareholders' equity and perpetual preferred stock (subject in the case of the latter to limitations on the kind and amount of such stocks which may be included as Tier I capital), less goodwill and other non-qualifying intangible assets. Tier II capital generally consists of: hybrid capital instruments; perpetual preferred stock, which is not eligible to be included as Tier I capital; term subordinated debt and intermediate-term preferred stock; and, subject to limitations, general allowances for loan losses. Assets are adjusted under the risk-based guidelines to take into account different risk characteristics.

In addition to the risk-based capital requirements, the Federal Reserve Board requires bank holding companies to maintain a minimum leverage capital ratio of Tier I capital (defined by reference to the risk-based capital guidelines) to total average assets (the "Leverage Ratio") of 3.0%. Total average assets for this purpose do not include goodwill and any other intangible assets and investments that the Federal Reserve Board determines should be deducted from Tier I capital. The Federal Reserve Board has announced that the 3.0% Leverage Ratio requirement is the minimum for the top-rated bank holding companies without any supervisory, financial or operational weaknesses, deficiencies, or those that are not experiencing or anticipating significant growth. For all other bank holding companies, the minimum leverage ratio is 4%, and bank holding companies with supervisory, financial, managerial or operational weaknesses or organizations expecting significant growth are expected to maintain capital ratios well above minimum levels.

The Company is currently in compliance with the Total Risk-Based Capital Ratio, Tier I Capital and the Leverage Ratio requirements. As of December 31, 2007, the Company had a Tier I Risk-Based Capital Ratio and a Total Risk-Based Capital Ratio equal to 18.80% and 19.97%, respectively, and a Leverage Ratio equal to 15.08%. U.S. bank regulatory authorities and international bank supervisory organizations, principally the Basel Committee on Banking Supervision, currently are considering changes to the risk-based capital adequacy framework, including emphasis on credit, market and operational risk components, which ultimately could affect the appropriate capital guidelines.

Limitations on Acquisitions of Common Stock. The federal Change in Bank Control Act prohibits a person or group of persons from acquiring "control" of a depository institution or a depository institution holding company unless the appropriate federal banking agency has been given at least 60 days to review the proposal and public notice has been provided. "Control" is generally defined under this act as ownership of 25% or more of any class of voting stock. In addition, under a rebuttable presumption established by the Federal Reserve Board, the acquisition of 10% or more of a class of voting stock of a depository institution or a depository institution holding company with a class of securities registered under Section 12 of the Exchange Act would, under the circumstances set forth in the presumption, constitute the acquisition of control. Furthermore, any company, as that term is broadly defined in the BHC Act, would be required to obtain the approval of the Federal Reserve Board under BHC Act before acquiring 25% (5% in the case of an acquirer that is a bank holding company) or more of any class of voting securities of a depository institution or a depository institution holding company, or such lesser percentage as the Federal Reserve Board deems to constitute a "controlling influence."

Bank Holding Company Dividends. The Federal Reserve Board has authority to prohibit bank holding companies from paying cash dividends if such payment is deemed to be an unsafe or unsound practice. The Federal Reserve Board has indicated generally that it may be an unsafe or unsound practice for bank holding companies to pay dividends unless the bank holding company's net income over the preceding year is sufficient to fund the dividends and the expected rate of earnings retention is consistent with the organization's capital needs, asset quality, and overall financial condition. The Company's ability to pay dividends is also subject to laws and regulations of the Connecticut Department of Banking.

Bank Holding Company Support of Subsidiary Banks. Under Federal Reserve Board policy, a bank holding company is expected to act as a source of financial and managerial strength to each of its subsidiary banks and to commit resources to their support. This support may be required at times when the bank holding company may not have the resources to provide it. Similarly, under the cross-guarantee provisions of the Federal Deposit Insurance Act ("FDIA"), the FDIC can hold any FDIC-insured depository institution liable for any loss suffered or anticipated by the FDIC in connection with (1) the "default" of a commonly controlled FDIC-insured depository institution; or (2) any assistance provided by the FDIC to a commonly controlled FDIC-insured depository institution "in danger of default."

The Sarbanes-Oxley Act. The Sarbanes-Oxley Act of 2002 ("Sarbanes-Oxley") implements a broad range of corporate governance and accounting measures for public companies (including publicly-held bank holding companies such as the Company) designed to promote honesty and transparency in corporate America. Sarbanes-Oxley's principal provisions, many of which have been interpreted through regulations of the Securities and Exchange Commission, provide for and include, among other things: (i) the creation of an independent accounting oversight board; (ii) auditor independence provisions that restrict non-audit services that accountants may provide to their audit clients; (iii) additional corporate governance and responsibility measures, including the requirement that the chief executive officer and chief financial officer of a public company certify financial statements; (iv) 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; (v) an increase in the oversight of, and enhancement of certain requirements relating to, audit committees of public companies and how they interact with the company's independent auditors; (vi) requirements that audit committee members must be independent and are barred from accepting consulting, advisory or other compensatory fees from the issuer; (vii) requirements that companies disclose whether at least one member of the audit committee is a "financial expert" (as such term is defined by the SEC); (viii) expanded disclosure requirements for corporate insiders, including accelerated reporting of stock transactions by insiders and a prohibition on insider trading during pension blackout periods; (ix) a prohibition on personal loans to directors and officers, except certain loans made by insured financial institutions on non-preferential terms and in compliance with other bank regulatory requirements; (x) disclosure of a code of ethics and filing a Form 8-K for a change or waiver of such code; and (xi) a range of enhanced penalties for fraud and other violations. On December 15, 2006, the Securities and Exchange Commission delayed the internal control reporting requirements under Section 404 of the Sarbanes-Oxley Act for non-accelerated filers to periods ending after December 15, 2007. In accordance with the requirements of Section 404(a), Management's report on internal controls is included herein at Item 8A. On January 31, 2008, the SEC proposed a further one-year delay from fiscal years ending after December 15, 2008 to fiscal years ending after December 15, 2009 for the auditors attestation report on internal controls over financial reporting.

USA PATRIOT ACT. The Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (the “Patriot Act”), designed to deny terrorists and others the ability to obtain access to the United States financial system, has significant implications for depository institutions, broker-dealers and other businesses involved in the transfer of money. The Patriot Act, as implemented by various federal regulatory agencies, requires financial institutions, including the Company and the Bank, to implement new policies and procedures or amend existing policies and procedures with respect to, among other matters, anti-money laundering, compliance, suspicious activity and currency transaction reporting, and due diligence on customers. The Patriot Act and its underlying regulations also permits information sharing for counter-terrorist purposes between federal law enforcement agencies and financial institutions, as well as among financial institutions, subject to certain conditions, and require the Federal Reserve Board (and other federal banking agencies) to evaluate the effectiveness of an applicant in combating money laundering activities when considering applications filed under the BHC Act or the Bank Merger Act.

Significant Laws and Regulations to which the Bank is Subject

General. The Bank is organized under the Banking Law of the State of Connecticut. Its operations are subject to federal and state laws applicable to commercial banks and to extensive regulation, supervision and examination by the Connecticut Banking Commissioner, as well as by the FDIC, as its primary federal regulator and insurer of deposits. While the Bank is not a member of the Federal Reserve System, it is subject to certain regulations of the Federal Reserve Board. In addition to banking laws, regulations and regulatory agencies, the Bank is subject to various other laws, regulations and regulatory agencies, all of which directly or indirectly affect the Bank’s operations. The Connecticut Banking Commissioner and the FDIC examine the affairs of the Bank for the purpose of determining its financial condition and compliance with laws and regulations. The Connecticut Banking Commissioner and the FDIC have the authority to limit the Bank’s payment of cash dividends based on such factors as the maintenance of adequate capital, which could reduce the amount of dividends otherwise payable.

The Connecticut Banking Commissioner and the FDIC have significant discretion in connection with their supervisory and enforcement activities and examination policies, including policies with respect to the classification of assets and the establishment of adequate loan loss reserves for regulatory purposes. Any change in such policies, whether by the FDIC, Congress, the Connecticut Banking Commissioner, or the Connecticut General Assembly, could have a material adverse impact on the Bank.

Activities and Investments of Insured State-Chartered Banks. Section 24 of the FDIA generally limits the activities of principal and equity investments of FDIC-insured, state-chartered banks to those that are permissible for national banks. The Company does not expect such provisions to have a material adverse effect on the Company or the Bank.

Capital Requirements. The FDIC has issued regulations and adopted a statement of policy regarding the capital adequacy of state-chartered banks, such as the Bank. Under the regulations, a bank generally is deemed to be (i) “well-capitalized” if it has a Total Risk-Based Capital Ratio of 10.0% or more, a Tier I Risk-Based Capital Ratio of 6.0% or more, a Leverage Ratio of 5.0% or more and is not subject to any written capital order or directive; or (ii) “adequately capitalized” if it has a Total Risk-Based Capital Ratio of 8.0% or more, a Tier I Risk-Based Capital Ratio of 4.0% or more, and a Leverage Ratio of 4.0% or more (3.0% under certain circumstances) and does not meet the definition of “well-capitalized;” or (iii) “undercapitalized” if it has a Total Risk-Based Capital Ratio that is less than 8.0%, a Tier I Risk-Based Capital Ratio that is less than 4.0% or a Leverage Ratio that is less than 4.0% (3.0% under certain circumstances); or (iv) “significantly undercapitalized” if it has a Total Risk-Based Capital Ratio that is less than 6.0%, a Tier I Risk-Based Capital Ratio that is less than 3.0% or a Leverage Ratio that is less than 3.0%, and (v) “critically undercapitalized” if it has a ratio of tangible equity to total assets that is equal to or less than 2.0%. If an institution becomes undercapitalized, it would become subject to significant additional oversight and regulation, as mandated by the FDIA.

The following table illustrates the Company's and the Bank's regulatory capital ratios at:

	Company			Bank		
	December 31, 2007	December 31, 2006	Capital Adequacy Target Ratio	December 31, 2007	December 31, 2006	Capital Adequacy Target Ratio
Total Capital to Risk Weighted Assets	19.97%	22.96%	8.00%	17.34%	19.72%	8.00%
Tier 1 Capital to Risk Weighted Assets	18.80%	21.80%	4.00%	16.13%	18.52%	4.00%
Tier 1 (Leverage) Capital Ratio to Average Assets	15.08%	17.56%	4.00%	12.88%	14.82%	4.00%

As of December 31, 2007, the Bank and the Company were deemed to be well-capitalized institutions.

Prompt Corrective Action and Other Enforcement Mechanisms. Federal law requires each federal banking agency to take prompt corrective action to resolve the problems of insured depository institutions, including but not limited to those that fall below one or more prescribed minimum capital ratios. An institution that, based upon its capital levels, is classified as “well capitalized,” “adequately capitalized” or “undercapitalized” may be treated as though it were in the next lower capital category if the appropriate federal banking agency, after notice and opportunity for hearing, determines that an unsafe or unsound condition or an unsafe or unsound practice warrants such treatment. At each successive lower capital category, an insured depository institution is subject to more restrictions. The federal banking agencies, however, may not treat an institution as “critically undercapitalized” unless its capital ratio actually warrants such treatment.

In addition to restrictions and sanctions imposed under the prompt corrective action provisions, commercial banking organizations may be subject to potential enforcement actions by the federal regulators for unsafe or unsound practices in conducting their businesses or for violations of any law, rule, regulation or any condition imposed in writing by the agency or any written agreement with the agency. Enforcement actions may include the imposition of a conservator or receiver, the issuance of a cease and desist order that can be judicially enforced, the termination of insurance of deposits (in the case of a depository institution), the imposition of civil money penalties, the issuance of directives to increase capital, the issuance of formal and informal agreements, the issuance of removal and prohibition orders against institution-affiliated parties and the enforcement of such actions through injunctions or restraining orders based upon a judicial determination that the agency would be harmed if such equitable relief was not granted.

Premiums for Deposit Insurance. The FDIC has implemented a risk-based assessment system, under which an institution's deposit insurance premium assessment is based on the probability that the deposit insurance fund will incur a loss with respect to the institution, the likely amount of any such loss, and the revenue needs of the deposit insurance fund.

Under this risk-based assessment system, banks are categorized into one of three capital categories (well capitalized, adequately capitalized, and undercapitalized) and one of three categories based on supervisory evaluations by its primary federal regulator. The three supervisory categories are: financially sound with only a few minor weaknesses (Group A); demonstrates weaknesses that could result in significant deterioration (Group B); and poses a substantial probability of loss (Group C). The capital ratios used by the FDIC to define well capitalized, adequately capitalized and undercapitalized are the same in the FDIC's prompt corrective action regulations.

FDIC insurance of deposits may be terminated by the FDIC, after notice and hearing, upon finding by the FDIC that the insured institution has engaged in unsafe or unsound practices, or is in an unsafe or unsound condition to continue operations, or has violated any applicable law, regulation, rule or order of, or conditions imposed by, the FDIC.

Safety and Soundness Standards. Federal law requires each federal banking agency to prescribe for depository institutions under its jurisdiction standards relating to, among other things: internal controls; information systems and audit systems; loan documentation; credit underwriting; interest rate risk; asset growth; compensation; fees and benefits; and such other operational and managerial standards as the agency deems appropriate. The federal banking agencies have promulgated regulations and Interagency Guidelines Establishing Standards for Safety and Soundness (the "Guidelines") to implement these safety and soundness standards. The Guidelines set forth the safety and soundness standards that the federal banking agencies use to identify and address problems at insured depository institutions before capital becomes impaired. The Guidelines address internal controls and information systems; internal audit system; credit underwriting; loan documentation; interest rate risk exposure; asset quality; earnings and compensation; and fees and benefits. If the appropriate federal banking agency determines that an institution fails to meet any standards prescribed by the Guidelines, the agency may require the institution to submit to the agency an acceptable plan to achieve compliance with the standard set by the FDIC.

The federal banking agencies also have adopted regulations for real estate lending prescribing uniform guidelines for real estate lending. The regulations require insured depository institutions to adopt written policies establishing standards, consistent with such guidelines, for extensions of credit secured by real estate. The policies must address loan portfolio management, underwriting standards and loan to value limits that do not exceed the supervisory limits prescribed by the regulations.

Community Reinvestment Act. Under the Community Reinvestment Act (“CRA”), as implemented by FDIC regulations, the 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 prescribe specific lending requirements or programs for financial institutions nor does it limit an institution’s discretion to develop the types of products and services that it believes are best suited to its particular community, consistent with the CRA. The CRA requires the FDIC, in connection with its examination of a depository institution, to assess the institution’s record of meeting the credit needs of its community and to take such record into account in its evaluation of certain applications by such institution. The FDIC is required to provide a written evaluation and make public disclosure of an institution’s CRA performance utilizing a four-tiered descriptive rating system. Institutions are evaluated and rated by the FDIC as “Outstanding,” “Satisfactory,” “Needs to Improve,” or “Substantial Non Compliance.” Failure to receive at least a “Satisfactory” rating may inhibit an institution from undertaking certain activities, including acquisitions of other financial institutions, which require regulatory approval based, in part, on CRA compliance considerations. In its most recent CRA evaluation, dated July 31, 2003, the Bank was rated as “Satisfactory.”

Transactions with Affiliates. Sections 23A and 23B of the Federal Reserve Act restrict transactions between a bank and an affiliated company, including a parent bank holding company. The Bank is subject to certain restrictions on loans to affiliated companies, on investments in the stock or securities thereof, on the taking of such stock or securities as collateral for loans to any borrower, and on the issuance of a guarantee or letter of credit on their behalf. Among other things, these restrictions limit the amount of such transactions, require collateral in prescribed amounts for extensions of credit, prohibit the purchase of low quality assets and require that the terms of such transactions be substantially equivalent to terms of similar transactions with nonaffiliates. Generally, the Bank is limited in its extensions of credit to any affiliate to 10% of the Bank’s capital and in its extensions of credit to all affiliates to 20% of the Bank’s capital.

Customer Information Security. The FDIC and other bank regulatory agencies have adopted guidelines (the “Security Guidelines”) for safeguarding confidential, personal customer information. The Security Guidelines require each financial institution, under the supervision and ongoing oversight of its board of directors or an appropriate committee thereof, to create, implement and maintain a comprehensive written information security program designed to ensure the security and confidentiality of customer information, protect against any anticipated threats or hazards to the security or integrity of such information, and protect against unauthorized access to or use of such information, and ensure the proper disposal of information that could result in substantial harm or inconvenience to any customer.

Privacy. Financial institutions are required to implement policies and procedures regarding their information collection practices and the disclosure of nonpublic personal information about consumers to nonaffiliated third parties. In general, the statute requires explanations to consumers on policies and procedures regarding the disclosure of such nonpublic personal information, and, except as otherwise required by law, prohibits disclosing such information except as provided in the financial institution's policies and procedures.

Item 2. Description of Property.

The table below sets forth information about properties the Bank uses for its branch offices. The Company also owns property located in Clinton, Connecticut.

Office	Location	Square Feet	Status
Main Office	215 Church Street, New Haven, Connecticut	11,306	Leased
Branford Office	445 West Main Street, Branford, Connecticut	3,714	Leased
Amity Office	1475 Whalley Avenue, New Haven, Connecticut	2,822	Owned
New London Office	15 Masonic Street, New London, Connecticut	4,341	Leased*
North Haven Office	24 Washington Avenue, North Haven, Connecticut	2,430	Leased

*Note: The lease for the Bank's New London office was assigned to Savings Institute Bank and Trust Company at the close of business February 29, 2008. See below.

Property at 215 Church Street, New Haven, Connecticut. The Bank leases a free-standing building located at 215 Church Street, New Haven, Connecticut, in the central business and financial district of New Haven. The headquarters of the Bank and the Company are located within this building. The building has a drive-up teller, an automated teller machine, two vaults and a night deposit drop.

The lease term ended in 2006, however, the Bank exercised its option to extend the lease for an additional five years. The Bank has a right of first refusal to purchase the building. The Bank's annual rent, which is fixed in the terms of the lease, including during the option periods, is currently \$137,933. The Bank is responsible for all costs to maintain the interior of the building, other than structural repairs, and for all real estate taxes.

When practical, the Bank seeks to sublease space within the building that is not needed for operations. The Bank of Southern Connecticut had two tenants in 2007, including the rental of approximately 1,045 square feet to Laydon and Company, LLC, an entity owned by Elmer A. Laydon, the son of Elmer F. Laydon, the Chairman of the board of directors of the Company.

Property at 445 West Main Street, Branford, Connecticut. The Bank of Southern Connecticut leases space at 445 West Main Street, Branford, Connecticut, the site of the Branford branch, which opened for business on October 7, 2002.

The current term of the Branford branch lease expires in 2012. The Bank of Southern Connecticut has option to extend the lease for two additional terms. The base rent payable for the current term is \$40,631 until September 30, 2012. The base rent for the option periods increases and is fixed in the lease. The Bank is responsible for all costs to maintain the building, other than structural repairs, and for all real estate taxes.

Property at 1475 Whalley Avenue, New Haven, Connecticut. The Bank owns a one-acre site with a single story, stucco facility of approximately 2,822 square feet that is located at 1475 Whalley Avenue, New Haven, Connecticut. The Bank operates its Amity branch from this location.

Property at 15 Masonic Street, New London, Connecticut. The Bank formerly leased a facility at 15 Masonic Street, New London, Connecticut, which is used as the main office for The Bank of Southeastern Connecticut, a division of the Bank. The Bank transferred the assets and liabilities of this branch to Savings Institute Bank and Trust Company at the close of business February 29, 2008. In connection with this transfer, the Bank assigned the lease to Savings Institute Bank and Trust Company.

Property at 24 Washington Avenue, North Haven, Connecticut. On February 16, 2006, the Company entered into a lease agreement to lease the facility at 24 Washington Avenue, North Haven, Connecticut, the site of The Bank of North Haven, a division of The Bank of Southern Connecticut. The facility was improved to accommodate the new branch, and \$295,000 was expended for improvements, furnishings and equipment. The Bank of North Haven, a division of The Bank of Southern Connecticut, opened for operations on July 10, 2006. The Lease is for an initial term of five years, with three successive five-year option periods. Base rent is \$38,880 annually until April 30, 2011. The base rent for the option periods increases and is fixed in the lease. The Bank is responsible for the pro rata share of operating expenses.

Property in Clinton, Connecticut. In June 2005, the Company purchased a one acre improved site with two buildings in Clinton, Connecticut for the primary purpose of establishing a branch office of the Bank. The net purchase price of the property was \$495,000. During 2007, the Bank determined that it would not establish a branch at this location and subsequently retained a commercial real estate broker to represent the Company in the sale of the property, and the property is classified as held for sale at December 31, 2007.

Item 3. Legal Proceedings.

There are no legal proceedings currently pending or threatened against the Company, its subsidiaries or their property. The Company is not aware of any proceeding contemplated by a governmental entity involving the Company or a subsidiary.

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

No matter was submitted to a vote of shareholders of the Company during the fourth quarter of the fiscal year covered by this Form 10-KSB.

PART II

Item 5. Market for Common Equity and Related Stockholder Matters.

The Company's Common Stock is quoted on the American Stock Exchange under the symbol "SSE."

The following table sets forth the high and low sales price per share of the Company's Common Stock for the last two years:

Quarter Ended	High	Low
March 31, 2007	\$ 8.12	\$ 7.10
June 30, 2007	\$ 7.66	\$ 7.10
September 30, 2007	\$ 7.65	\$ 7.00
December 31, 2007	\$ 7.62	\$ 6.85
March 31, 2006	\$ 7.55	\$ 6.95
June 30, 2006	\$ 7.55	\$ 6.96
September 30, 2006	\$ 7.19	\$ 6.80
December 31, 2006	\$ 7.29	\$ 6.89

Holdings

There were approximately 107 registered shareholders of record of the Company's Common Stock as of March 10, 2008.

Dividends

No cash dividends have been declared to date by the Company. Management expects that earnings, if any, will be retained and that no cash dividends will be paid in the near future. The Company may, however, declare stock dividends at the discretion of its Board of Directors. No stock dividends were declared in 2007 and 2006.

The Company's sole operating subsidiary is the Bank. The Company is dependent upon the ability of the Bank to declare and pay dividends to the Company. The Bank's ability to declare cash dividends is dependent upon the Bank's ability to earn profits and to maintain acceptable capital ratios, as well as meet regulatory requirements and remain compliant with banking law.

The policy of the Connecticut Banking Commissioner is to prohibit payment of any cash dividends prior to recapture of organization and pre-operating expenses from operating profits. In addition, the Bank is prohibited by Connecticut law from declaring a cash dividend on its Common Stock without prior approval of the Connecticut Banking Commissioner except from its net profits for that year and any retained net profits of the preceding two years. "Net profits" is defined as the remainder of all earnings from current operations. In some instances, further restrictions on dividends may be imposed by the FDIC. At December 31, 2007 and 2006, no cash dividends may be declared by the Bank without regulatory approval.

The payment of cash dividends by the Bank may also be affected by other factors, such as the requirement to maintain capital in accordance with regulatory guidelines. If, in the opinion of the Connecticut Banking Commissioner, the Bank were engaged in or was about to engage in an unsafe or unsound practice, the Commissioner could require, after notice and a hearing, the Bank to cease and desist from the practice. The federal banking agencies have indicated that paying dividends that deplete a depository institution's capital base to an inadequate level would be an unsafe and unsound banking practice. Under the Federal Deposit Insurance Corporation Improvements Act of 1991, a depository institution may not pay any cash dividend if payment would cause it to become undercapitalized or if it already is undercapitalized. Moreover, the federal banking agencies have issued policy statements that provide that bank holding companies and insured banks should generally only pay dividends out of current operating earnings.

Equity Compensation Plan Information

The following schedule provides information with respect to the compensation plans (including individual compensation arrangements) under which equity securities of the Company are authorized for issuance as of December 31, 2007:

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)	Weighted-average exercise price of outstanding options, warrants and rights (b)	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))
Equity Compensation Plans approved by security holders	319,075	\$7.69	142,944
Equity Compensation Plan not approved by security holders (1)	77,184	\$10.39	0
Total	396,259	\$8.22	142,944

(1) The Company adopted a 2001 Warrant Plan and 2001 Supplemental Warrant Plan (collectively, the "Warrant Plans") on April 11, 2001 and October 16, 2001, respectively. The Warrant Plans were not approved by security holders. Under the Warrant Plans, each director of the Company, other than Mr. Joseph V. Ciaburri (who served as the Chairman of the board of directors of the Company at the time), and each director of the Bank who is not a director of the Company, as of the initial public offering of the Company in July 2001, received a warrant to purchase one share of the Company common stock for each four shares purchased in the offering by such director or members of such director's immediate family. Under the 2001 Supplemental Warrant Plan, certain organizers of the Company who are not directors, officers or employees of the Company or the Bank but who made contributions to the

Company's enterprise received a warrant to purchase one share of the Company common stock for each five shares purchased in the offering by such person or member of such person's immediate family. The warrants have a term of ten years. The exercise price of the warrants is \$10.39, the price at which the Company's common stock was sold in the initial public offering, as adjusted for subsequent stock dividends. As of December 31, 2007, the warrants are fully exercisable.

Recent Sales of Unregistered Securities

The Company has not sold unregistered securities.

Repurchase of Securities

In December 2005, the Board of Directors of the Company authorized the repurchase of up to 146,879 shares of the Company common stock. No shares of the Company's common stock were purchased through December 31, 2007. As of March 10, 2008, the Company has repurchased 2,900 of its shares.

Item 6. Management's Discussion and Analysis or Plan of Operation.

The following discussion is intended to assist you in understanding the financial condition and results of operations of the Company and the Bank, and should be read in conjunction with the consolidated financial statements and related notes beginning on page F-3.

Overview

Southern Connecticut Bancorp, Inc. is a bank holding company headquartered in New Haven, Connecticut that was incorporated on November 8, 2000. The Company's strategic objective is to serve as a bank holding company for The Bank of Southern Connecticut, a commercial bank serving New Haven, Connecticut and the surrounding communities. The Bank of Southern Connecticut commenced operations on October 1, 2001.

The Company's net loss for fiscal year 2007 was \$574,000, an increase of \$456,000 from the net loss of \$118,000 in fiscal year 2006. In comparison to 2006, the 2007 operating results reflect increased net interest income due to increased average earning assets and higher interest rates. Additionally, non-interest income (from fees and other income) increased during 2007 due to an increase in service charges and fees, resulting from increases in deposit account balances, deposit account activity and deposit account charges. The increases in non-interest expenses in 2007 in comparison to 2006 were partially due to the opening of the two new branches during 2006, The Bank of Southeastern Connecticut, and The Bank of North Haven, both of which are divisions of The Bank of Southern Connecticut, which contributed to an increase in salaries and benefits associated with the staffing of such branches. In addition, the increase in operating expense is attributable to postretirement benefits, increases in professional services and a write-down of the Clinton office offset by a reduction in advertising and promotional expense.

The Bank offers a wide range of services to businesses, professionals, and individuals. The Bank focuses on serving the banking needs of small to medium-sized businesses in its geographic areas. The Bank makes commercial loans, industrial loans, real estate loans, construction loans and consumer loans, accepts demand, savings, and time deposits and provides a broad range of other services to its customers, either directly or through third parties. The Bank derives revenues principally from interest earned on loans and fees from other banking-related services. The operations of the Bank are influenced significantly by general economic conditions and by policies of financial institution regulatory agencies, primarily the Connecticut Banking Commissioner and the FDIC. The Bank's cost of funds is influenced by interest rates on competing investments and general market interest rates. Lending activities are affected by the demand for financing of real estate and other types of loans, which in turn is affected by the interest rates at which such financings may be offered.

Selected Financial Data –
Years Ended December 31, 2007 and December 31, 2006

Operating Data	2007	2006
Interest income	\$ 9,143,381	\$ 7,080,124
Interest expense	3,377,776	2,223,065
Net interest income	5,765,605	4,857,059
Provision for loan losses	538,480	253,495
Noninterest income	960,495	804,066
Noninterest expenses	6,761,301	5,525,424
Net loss	(573,681)	(117,794)
Basic and diluted loss per share	(0.19)	(0.04)
Balance sheet data		
Cash and due from banks	\$ 3,891,258	\$ 5,821,084
Federal funds sold	21,100,000	22,700,000
Short-term investments	8,355,686	6,288,663
Investment securities	5,265,679	8,054,821
Loans, net	85,995,128	75,306,255
Total assets	130,564,261	124,262,545
Total deposits	107,422,392	101,273,520
Repurchase agreements	544,341	883,603
Total shareholders'	20,084,483	20,331,849

equity

Segment Reporting

The Company's only business segment is Community Banking. During the periods presented this segment represented all the revenues and income of the consolidated group and therefore, is the only reported segment as defined by SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information."

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Assets

The Company's total assets were \$130.6 million as of December 31, 2007, an increase of \$6.3 million over December 31, 2006. Earning assets comprise \$122.4 million of the total asset volume, and consist of Federal funds sold, short-term investments, securities and loans, which collectively increased \$8.8 million from 2006. The Company has maintained liquidity by maintaining balances in overnight Federal funds sold and in short-term investments, primarily money market mutual funds, to provide funding for higher yielding loans as they are approved. As of December 31, 2007 and 2006, Federal funds sold balances were \$21.1 million and \$22.7 million, respectively and short-term investments balances were \$8.4 million and \$6.3 million, respectively. Investment securities classified as available for sale were \$5.3 million and \$8.1 million as of December 31, 2007 and 2006, respectively. The gross loan portfolio was \$87.3 million and \$76.4 million as of December 31, 2007 and 2006 respectively, a net increase of \$10.9 million.

The earning asset increase in 2007 has been funded principally with deposit growth within the Bank's market area. Deposits were \$107.4 million and \$101.3 million as of December 31, 2007 and 2006 respectively, a net increase of \$6.1 million. The mix of deposits as of December 31, 2007 includes non-interest bearing checking accounts of \$27.8 million, interest-bearing checking deposits of \$5.8 million, savings deposits of \$1.7 million, money market deposits of \$40.7 million, as well as time certificates of deposit of \$31.4 million. The deposit mix between 2007 and 2006 has remained consistent, with time deposits representing 29% and 28% of the Bank's deposits as of December 31, 2007 and 2006, respectively. Core deposits, comprised of demand, savings, money market and checking accounts, represented 71% and 72% of the Bank's deposits as of December 31, 2007 and 2006, respectively. The Bank has not accepted brokered deposits.

Investments

The Company's investments decreased during 2007 due to maturities that were used to fund loan growth.

The following table presents the maturity distribution of the amortized cost of investment securities at December 31, 2007, and the weighted average yield of such securities. The weighted average yields were calculated based on the amortized cost and effective yields to maturity of each security.

	One Year or Less	Over One Year Through Five Years	Over Five Years Through Ten Years	Over Ten Years	No Maturity	Total	Weighted Average Yield
Available for sale U. S. Government sponsored agency obligations	\$ 1,491,699	\$ 2,379,534	\$ 797,504	\$ 496,165	\$ -	\$ 5,164,902	3.36%
Mortgage-backed securities	-	-	-	-	100,777	100,777	4.48%
Total	\$ 1,491,699	\$ 2,379,534	\$ 797,504	\$ 496,165	\$ 100,777	\$ 5,265,679	
Weighted Average Yield	3.47%	3.77%	3.41%	4.91%	4.49%	3.75%	

The following table presents a summary of investments for any issuer that exceeds 10% of shareholders' equity at December 31, 2007:

	Amortized Cost	Fair Value
Federal Home Loan Mortgage Corporation	2,505,417	2,491,305

Please see also, "Notes to Consolidated Financial Statements."

Loans

The Bank's net loan portfolio was \$86.0 million at December 31, 2007 versus \$75.3 million at December 31, 2006, an increase of \$10.7 million. Loan demand has been steady throughout the year. The Company attributes the 2007 loan growth to the success of the Bank's loan business development program in generating loan demand to small to medium-sized businesses. Management believes that the loan growth will continue as the Bank's branch system deposit base grows and additional lending capacity is developed. The Bank's loans have been made to borrowers primarily in the New Haven and New London Counties of Connecticut. There are no other significant loan concentrations in the loan portfolio. With the sale of the New London branch in early 2008, the Bank will focus its lending efforts primarily on the greater New Haven market area.

The following table presents the maturities of loans in the Company's portfolio at December 31, 2007 by type of loan, and the sensitivities of loans to changes in interest rates:

	Due in one year or less	Due after one year through five years	Due after five years	Total	% of Total
Commercial loans secured					
by real estate	\$ 18,910,378	\$ 19,542,400	\$ 368,355	\$ 38,821,133	44.45%
Commercial loans	31,398,496	8,185,594	1,179,086	40,763,176	46.68%
Construction loans	5,230,624	1,017,831	-	6,248,455	7.16%
Residential real estate	7,660	36,554	98,119	142,333	0.16%
Consumer home equity	248,527	86,408	220,759	555,694	0.64%
Consumer installment	552,702	195,197	46,698	794,597	0.91%
Total	\$ 56,348,387	\$ 29,063,984	\$ 1,913,017	\$ 87,325,388	100.00%
Fixed rate loans	\$ 7,527,643	\$ 5,450,817	\$ 1,913,017	\$ 14,891,477	
Variable rate loans	48,820,744	23,613,167	-	72,433,911	
Total	\$ 56,348,387	\$ 29,063,984	\$ 1,913,017	\$ 87,325,388	

Please see also, "Notes to Consolidated Financial Statements."

Critical Accounting Policy

In the ordinary course of business, the Company has made a number of estimates and assumptions relating to reporting the results of operations and financial condition in preparing its financial statements in conformity with accounting principles generally accepted in the United States of America. Actual results could differ significantly from those estimates under different assumptions and conditions. The Company believes the following discussion addresses the Company's only critical accounting policy, which is the policy that is most important to the portrayal of the Company's financial condition and results, and requires management's most difficult, subjective and complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain. The Company has reviewed this critical accounting policy and estimates with its audit committee. Refer to the discussion below under "Allowance for Loan Losses" and Note 1 to the consolidated financial statements for a detailed description of our estimation process and methodology related to the allowance for loan losses.

Allowance for Loan Losses

The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. Loans are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

The allowance for loan losses is evaluated on a regular basis by management and is based upon management's periodic review of the collectibility of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

The allowance for loan losses consists of specific and general components. The specific component relates to allowances established for individual impaired loans. The general component relates to pools of loans segregated by loan type, and is based on historical loss experience adjusted by certain qualitative factors as determined by management and the board of directors. The allowance for loan losses does not contain an unallocated component.

Based upon this evaluation, management believes the allowance for loan losses of \$1,257,000 or 1.44% of gross loans at December 31, 2007 is adequate, under prevailing economic conditions, to absorb losses on existing loans. At December 31, 2006, the allowance for loan losses was \$1,063,000 or 1.39% of gross loans outstanding. The increase in the allowance is attributable to growth in the loan portfolio as well as an increase in the reserve factors for the general portion of the allowance. Based on prevailing nationwide economic conditions and forecasts, management and the Board of Directors determined to increase the reserve factors for the Company's general reserve components of the allowance. In addition to contributing to the overall increase in the allowance, the increase in the reserve factors contributed to the Company's increase in allowance as a percentage of loans.

The accrual of interest income on loans is discontinued whenever reasonable doubt exists as to its collectibility and generally is discontinued when loans are past due 90 days as to either principal or interest, or are otherwise considered impaired. When the accrual of interest income is discontinued, all previously accrued and uncollected interest is reversed against interest income. The accrual of interest on loans past due 90 days or more may be continued if the loan is well secured, and it is believed all principal and accrued interest income due on the loan will be realized, and the loan is in the process of collection. A non-accrual loan is restored to an accrual status when it is no longer delinquent and collectibility of interest and principal is no longer in doubt.

Management considers all non-accrual loans, other loans past due 90 days or more based on contractual terms, and restructured loans to be impaired. In most cases, loan payments that are past due less than 90 days and the related loans are not considered to be impaired.

Allowance for Loan Losses as of December 31, 2007 and 2006:

	2007	2006
Balance, beginning of year	\$ 1,062,661	\$ 778,051
Provision for loan losses	538,480	253,495
Recoveries of loans previously charged-off	11,973	68,182
Loans charged-off	(356,149)	(37,067)
Balance, end of year	\$ 1,256,965	\$ 1,062,661

Net (charge-offs) recoveries to average loans	(0.41%)	.05%
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Allocation of the Allowance for Loan Losses at December 31:

	2007		2006	
	Balance	Percent of Loans in Each Category to Total Loans	Balance	Percent of Loans in Each Category to Total Loans
Commercial loans secured by real estate	\$ 405,492	44.45%	\$ 444,937	41.87%
Commercial loans	634,516	46.68%	550,824	51.83%
Construction loans	61,907	7.16%	45,231	4.26%
Residential mortgages	139,521	0.16%	2,076	0.20%
Consumer home equity loans	3,756	0.64%	8,388	0.79%
Consumer installment loans	11,773	0.91%	11,205	1.05%
	\$ 1,256,965	100.00%	\$ 1,062,661	100.00%

Non-Accrual, Past Due and Restructured Loans

Non-accrual loans at December 31, 2007 and 2006 totaled \$530,246 and \$301,833 respectively. In 2007 and 2006, there were no loans considered “troubled debt restructurings” and no loans greater than 90 days past due and still accruing interest.

Potential Problem Loans

Other than loans identified as non-accrual at December 31, 2007, the Bank had no material loans as to which management has significant doubts as to the ability of the borrower to comply with the present repayment terms.

Deposits

Total deposits were \$107.4 million at December 31, 2007, an increase of \$6.1 million in comparison to total deposits as of December 31, 2006 of \$101.3 million. The Company attributes the 2007 deposit growth to the opening of the two new branches in 2006. Total deposits at December 31, 2007 consisted of non-interest bearing checking of \$27.8 million (25.9%), interest-bearing checking and money market deposits of \$46.5 million (43.3%), savings deposits of \$1.7 million (1.5%) and certificates of deposit of \$31.4 million (29.3%). The Bank continues to emphasize growth in core non-interest checking accounts and related interest bearing checking, money market deposit, and savings accounts and is less aggressive in attracting higher cost time deposits. As of December 31, 2007, these core deposits represented 70.7% of total deposits.

The Bank has not accepted brokered deposits. However, the Bank has the ability to issue brokered deposits should liquidity be needed to fund investments.

The Greater New Haven Market is highly competitive. The Bank faces competition from a large number of banks (ranging from small community banks to large international banks), credit unions, and other providers of financial services. The level of rates offered by the Bank reflects the high level of competition in our market.

As of December 31, 2007 the Bank's maturities of time deposits were:

(Thousands of dollars)	\$100,000 or greater	Less than \$100,000	Totals
Three months or less	\$ 5,943	\$ 2,757	\$ 8,700
Over three months to six months	2,937	3,027	5,964
Over six months to one year	5,079	6,167	11,246
Over one year	897	4,649	5,546
	\$ 14,856	\$ 16,600	\$ 31,456

Other

The increase in Other Assets Held for Sale is due to the transfer of the Clinton property from Premises and Equipment. The property is reflected at fair value net of estimated costs to sell, or \$414,900 as of December 31, 2007.

The following table presents average balance sheets (daily averages), interest income, interest expense, and the corresponding annualized rates on earning assets and rates paid on interest bearing liabilities for the years ended December 31, 2007 and 2006.

	2007			2006			Fluctuations in interest Income/Expense Total
	Average Balance	Interest Income/ Expense	Average Rate	Average Balance	Interest Income/ Expense	Average Rate	
(Dollars in thousands)							
Interest earning assets							
Loans (1)	\$ 83,977	\$ 7,539	8.98%	\$ 64,477	\$ 5,836	9.05%	\$ 1,703
Short-term	7,388	370	5.01%	5,757	279	4.85%	91
investments							
Investments	7,318	259	3.54%	9,307	313	3.36%	(54)
Federal funds sold	19,225	975	5.07%	12,630	652	5.16%	323
Total interest earning assets	117,908	9,143	7.76%	92,171	7,080	7.68%	2,063
Cash and due from banks	5,413			2,049			
Premises and equipment, net	4,269			4,443			
Allowance for loan losses	(1,161)			(903)			
Other	1,547			1,399			
Total assets	\$ 127,976			\$ 99,159			
Interest bearing liabilities							
Time certificates	\$ 31,150	1,566	5.03%	\$ 17,078	738	4.32%	828
Savings deposits	1,908	25	1.31%	2,651	37	1.40%	(12)
Money market / checking deposits	44,603	1,601	3.59%	35,234	1,254	3.56%	347
Capital lease obligations	1,187	176	14.83%	1,189	175	14.72%	1
Repurchase agreements	648	10	1.54%	1,253	19	1.52%	(9)
Total interest bearing liabilities	79,496	3,378	4.25%	57,405	2,223	3.87%	1,155
Non-interest bearing deposits	27,285			20,894			
Accrued expenses and other liabilities	729			576			
Shareholder's equity	20,466			20,284			

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Total liabilities and equity	\$ 127,976	\$ 99,159		
Net interest income	\$ 5,765	\$ 4,857	\$	908
Interest spread		3.51%		3.81%
Interest margin		4.89%		5.27%

(1) Includes nonaccruing loans.

RATE VOLUME VARIANCE ANALYSIS

The following table summarizes the variance in interest income and expense for 2007 and 2006 resulting from changes in assets and liabilities and fluctuations in interest rates earned and paid. The changes in interest income and expense attributable to both rate and volume have been allocated to both rate and volume on a pro rata basis.

(Dollars in thousands)	2007 vs 2006		
	Variance due to:		Total
	Volume	Rate	
Interest earning assets			
Loans	\$ 1,748	\$ (45)	\$ 1,703
Short-term investments	76	15	91
Investments	(64)	10	(54)
Federal funds sold	334	(11)	323
Total interest earning assets	2,094	(31)	2,063
Interest bearing liabilities			
Time certificates	525	303	828
Savings deposits	(10)	(2)	(12)
Money market / checking deposits	332	15	347
Capital lease obligations	-	1	1
Repurchase agreements	(9)	-	(9)
Total interest bearing liabilities	838	317	1,155
Net interest income	\$ 1,256	\$ (348)	\$ 908

The improvements realized in net interest income during 2007 reflect an increase in earning asset balances over 2006, as the average earning assets in 2007 of \$117.9 million were 28% greater than average earning assets in 2006, while the yields on all interest earning assets remained relatively stable. Overall, interest income attributed to volume increases considerably outweighed rate considerations (increase of \$2.1 million versus a decrease of \$31,000). Variances in the 2007 cost of interest bearing liabilities in comparison to 2006 were due to increased volume considerations of \$838,000 and increased rate considerations of \$317,000.

The Company intends for the Bank to continue to emphasize lending to small to medium-sized businesses in its market area as its strategy to increase assets under management and to improve earnings. The Bank will seek opportunities through marketing to increase its deposit base, with a primary objective of attracting core non-interest checking and related money market deposit accounts, in order to support its earning assets and also by considering additional branch locations and new product and service offerings.

The following are measurements of The Company's loss in relation to assets and equity, and average equity to average assets for the years ended December 31, 2007 and 2006:

	2007	2006
Loss on average assets	(.45%)	(.12%)
Loss on average equity	(2.80%)	(.58%)
Average equity to average assets	15.99%	20.46%

Results of Operations

The Company's net loss for fiscal year 2007 was \$574,000, an increase of \$456,000 from the net loss of \$118,000 in fiscal year 2006. In comparison to 2006, the 2007 operating results reflect increased net interest income due to increased average earning assets and interest rates. Additionally, non-interest income (from fees and other income) increased during 2007 due to an increase in service charges and fees, resulting from increases in deposit account balances, deposit account activity and deposit account charges. The increases in non-interest expenses in 2007 in comparison to 2006 were partially due to the full year of operations of the two new branches opened during 2006, The Bank of Southeastern Connecticut, and The Bank of North Haven, both of which are divisions of The Bank of Southern Connecticut, which contributed to an increase in salaries and benefits associated with the staffing of such branches. In addition, the net increase in operating expense is attributable to postretirement benefits, increases in professional services and a write-down of the Clinton office offset by a reduction in advertising and promotional expense.

Net Interest Income

The principal source of revenue for the Bank is net interest income. The Bank's net interest income is dependent primarily upon the difference or spread between the average yield earned on loans receivable and securities and the average rate paid on deposits and borrowings, as well as the relative amounts of such assets and liabilities. The Bank, like other banking institutions, is subject to interest rate risk to the degree that its interest-bearing liabilities mature or reprice at different times, or on a different basis, than its interest-earning assets.

For the year ended December 31, 2007, net interest income was \$5.8 million versus \$4.9 million for the year ended December 31, 2006, an increase of \$900,000 or 18.4%. The 2007 increase was primarily the result of increases in the volume of interest earning assets, net of the increased cost of funds on interest bearing liabilities, due to both volume and rate increases. The increase in average interest earning assets was comprised of increases in loans of \$19.5 million, decreases in investments of \$2.0 million, increases in short term investments of \$1.6 million, and increases in federal funds sold of \$6.6 million.

The yield on average interest earning assets for the twelve months ended December 31, 2007 was 7.76% versus 7.68% for same period in 2006, a slightly favorable increase of 8 basis points. The increase in the yield on assets reflects the increases in market interest rates that occurred throughout 2007, particularly in the prime lending rate and the Bank's base lending rate, offset by the increasing competitive market to attract new loans at higher rates.

The cost of average interest bearing liabilities was 4.25% for the twelve months ended December 31, 2007 versus 3.87% for the same period in 2006, an unfavorable increase of 38 basis points, reflecting a general increase in market interest rates. The increase in the cost of interest bearing liabilities was due to an increase in the volume of, and rates paid on, deposit accounts. The average rate of interest paid on time deposits increased 71 basis points in 2007 in comparison to 2006.

Due to the increase in the cost of interest bearing liabilities, which offsets the increase in the average yield on earning assets, the interest spread decreased to 3.51% for fiscal year 2007, a decrease of 30 basis points from the interest spread realized in 2006. Net interest margin decreased to 4.89% in 2007 from 5.27% in 2006, a decrease of 38 basis points which largely reflects the increasing deposit rates during 2007.

Noninterest Income

The \$156,000 increase in non-interest income for the twelve months ended December 31, 2007 versus 2006 is comprised of an increase of \$138,000 in service charges and fees, resulting from increases in deposit account balances, deposit account activity and deposit account charges; an increase of \$61,000 in loan prepayment penalties, \$39,000 in other loan fees, \$20,000 in all other fees, partially offset by a decrease of \$102,000 in gains on sales of loan participations related to SBA guaranteed loans.

Noninterest Expenses

Total noninterest expenses were \$6.7 million for the year ended December 31, 2007 versus \$5.5 million for 2006, an increase of \$1.2 million or 21.8%. A primary factor contributing to the increase in noninterest expense year-over-year was the full year of operations of the two new branches of The Bank of Southern Connecticut. The Bank of Southeastern Connecticut, a division of The Bank of Southern Connecticut located in New London, Connecticut opened on March 6, 2006. The Bank of North Haven, a division of The Bank of Southern Connecticut located in North Haven, Connecticut opened on July 10, 2006, however costs were incurred in the first quarter of 2006 in anticipation of the branch opening. The opening of these two branches has increased the Bank's operating expenses, primarily salaries and benefits expense and occupancy expense. The increase in salaries and benefits reflects the accrual for a post-retirement benefit of \$124,000 related to the Company's obligation to maintain a life insurance policy for the benefit of the retired Chief Executive Officer. In addition, the Company paid \$55,000 in performance bonuses in 2007 and also made a severance payment of \$30,000 to a terminated employee. As a result, salaries and benefits increased \$423,000 to \$3.5 million in fiscal year 2007 in comparison to fiscal year 2006.

In comparison to 2006, occupancy and equipment expenses increased \$89,000 to \$853,000, data processing expense increased \$63,000 to \$421,000, FDIC Insurance increased \$97,000 to \$124,000 in comparison to fiscal year 2006, all primarily due to the increase in the FDIC base ratio which became effective as of January 1, 2007. In addition, professional fees increased \$337,000, the result of higher legal costs, consulting fees and also expenses related to the Company's implementation of the Sarbanes Oxley Act. Other operating expenses increased by \$459,000 to \$990,000 largely as a result of the accrual of