FIRST NORTHERN COMMUNITY BANCORP
Form 10-Q
May 09, 2007

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

FORM 10-Q

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

For the Quarterly Period Ended March 31, 2007

OR

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

For the transition period from _______________ to _______________

Commission File Number 000-30707

First Northern Community Bancorp
(Exact name of registrant as specified in its charter)

California	**68-0450397**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

195 N. First Street, Dixon, California	**95620**
(Address of principal executive offices)	(Zip Code)

707-678-3041
(Registrant's telephone number including area code)

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or Section 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 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 check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes ¨ **No** x

The number of shares of Common Stock outstanding as of May 7, 2007 was 8,388,237.

FIRST NORTHERN COMMUNITY BANCORP

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PART I - FINANCIAL INFORMATION

ITEM 1.

CONSOLIDATED FINANCIAL STATEMENTS

CONDENSED CONSOLIDATED BALANCE SHEETS
(in thousands, except share amounts)

	(UNAUDITED) March 31, 2007	December 31, 2006
ASSETS		
Cash and due from banks	$ 27,682	$ 35,531
Federal funds sold	82,665	62,470
Investment securities - available-for-sale	80,136	74,180
Loans, net of allowance for loan losses of		
$7,950 at March 31, 2007 and $8,361 at December 31, 2006	462,708	475,549
Loans held-for-sale	7,718	4,460
Premises and equipment, net	8,225	8,060
Other Real Estate Owned	1,475	375
Accrued interest receivable and other assets	23,364	24,600
TOTAL ASSETS	$ 693,973	$ 685,225
LIABILITIES AND STOCKHOLDERS' EQUITY		
Liabilities		
Deposits		
Demand deposits	$ 179,410	$ 197,498
Interest-bearing transaction deposits	129,332	117,620
Savings and MMDA's	183,055	175,128
Time, under $100,000	50,908	47,137
Time, $100,000 and over	72,044	66,299
Total deposits	614,749	603,682
FHLB Advances and other borrowings	10,161	10,981
Accrued interest payable and other liabilities	6,117	8,572
TOTAL LIABILITIES	631,027	623,235
Stockholders' equity		
Common stock, no par value; 16,000,000 shares authorized;		
8,408,803 shares issued and outstanding at March 31, 2007 and 7,980,952 shares issued and outstanding at December 31, 2006	55,433	45,726
Additional paid in capital	977	977
Retained earnings	7,018	15,792
Accumulated other comprehensive loss	(482)	(505)
TOTAL STOCKHOLDERS' EQUITY	62,946	61,990
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 693,973	$ 685,225

See notes to unaudited condensed consolidated financial statements.

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UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(in thousands, except per share amounts)

	Three months ended March 31, 2007	Three months ended March 31, 2006
Interest Income		
Loans	$ 10,375	$ 9,684
Federal funds sold	860	960
Investment securities		
Taxable	650	532
Non-taxable	278	131
Other interest earning assets	29	24
Total interest income	12,192	11,331
Interest Expense		
Deposits	2,892	1,805
Other borrowings	77	134
Total interest expense	2,969	1,939
Net interest income	9,223	9,392
Recovery of provision for loan losses	(170)	(575)
Net interest income after recovery of provision for loan losses	9,393	9,967
Other operating income		
Service charges on deposit accounts	793	621
Gain on sales of other real estate owned	—	7
Gains on sales of loans held-for-sale	46	37
Investment and brokerage services income	67	45
Mortgage brokerage income	69	85
Loan servicing income	75	68
Fiduciary activities income	65	33
ATM fees	66	69
Signature based transaction fees	114	81
Other income	203	163
Total other operating income	1,498	1,209
Other operating expenses		
Salaries and employee benefits	4,473	4,543
Occupancy and equipment	998	855
Data processing	408	329
Stationery and supplies	146	123
Advertising	211	216
Directors' fees	54	34
Other expense	1,356	1,227
Total other operating expenses	7,646	7,327
Income before income tax expense	3,245	3,849
Provision for income taxes	1,155	1,447

Net income	$	2,090	$	2,402
Basic earnings per share	$	0.25	$	0.28
Diluted earnings per share	$	0.24	$	0.27

See notes to unaudited condensed consolidated financial statements.

UNAUDITED CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY AND COMPREHENSIVE INCOME

(in thousands, except share amounts)

	Common Stock		Comprehensive	Additional Paid-in	Retained	Accumulated Other Comprehensive Income /	
	Shares	Amounts	Income	Capital	Earnings	(Loss)	Total
Balance at December 31, 2006	7,980,952	$ 45,726		$ 977	$ 15,792	$ (505)	$ 61,990
Comprehensive income:							
Net income			$ 2,090		2,090		2,090
Other comprehensive gain:							
Unrealized holding gains on securities arising during the current period, net of tax effect of $15			23			23	23
Comprehensive income			$ 2,113				
6% stock dividend	476,976	10,851			(10,851)		—
Cash in lieu of fractional shares					(13)		(13)
Stock-based compensation and related tax benefits		181					181
Stock options exercised, net of swapped shares	10,592	—					—
Stock repurchase and retirement	(59,717)	(1,325)					(1,325)
Balance at March 31, 2007	8,408,803	$ 55,433		$ 977	$ 7,018	$ (482)	$ 62,946

See notes to unaudited condensed consolidated financial statements.

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

	(in thousands) Three months ended March 31, 2007	Three months ended March 31, 2006
Operating Activities		
Net Income	$ 2,090	$ 2,402
Adjustments to reconcile net income to net		
cash provided by operating activities:		
Depreciation	337	253
Recovery of provision for loan losses	(170)	(575)
Stock plan accruals	181	95
Tax benefit for stock options	—	206
Gains on sales of loans held-for-sale	(46)	(37)
Gains on sales of other real estate owned	—	(7)
Proceeds from sales of loans held-for-sale	9,566	3,260
Originations of loans held-for-sale	(12,778)	(3,485)
Decrease in accrued interest receivable and other assets	1,274	346
Decrease in accrued interest payable and other liabilities	(2,455)	(2,195)
Net cash (used in) provided by operating activities	(2,001)	263
Investing Activities		
Net increase in investment securities	(5,971)	(15,176)
Net decrease (increase) in loans	13,011	(6,693)
Net (increase) decrease in other real estate owned	(1,100)	275
Purchases of premises and equipment, net	(502)	(84)
Net cash provided by (used in) investing activities	5,438	(21,678)
Financing Activities		
Net increase in deposits	11,067	7,181
Net decrease in FHLB advances	(820)	(4,544)
Cash dividends paid	(13)	(8)
Tax benefit for stock options	—	(206)
Repurchase of stock	(1,325)	(1,549)
Net cash provided by financing activities	8,909	874
Net increase (decrease) in cash and cash equivalents	12,346	(20,541)
Cash and cash equivalents at beginning of period	98,001	122,692
Cash and cash equivalents at end of period	$ 110,347	$ 102,151
Supplemental disclosures of cash flow information:		
Cash paid during the period for:		
Interest	$ 2,958	$ 1,946
Income Taxes	$ 107	—
Supplemental disclosures of non-cash investing and financing activities:		
Stock dividend distributed	$ 10,851	$ 12,525

See notes to unaudited condensed consolidated financial statements.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2007 and 2006 and December 31, 2006

1. BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements of First Northern Community Bancorp (the "Company") have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) for interim financial information and with the instructions to Form 10-Q and Articles 9 and 10 of Regulation S-X. Accordingly, they do not include all of the information and notes required by GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. The results of operations for any interim period are not necessarily indicative of results expected for the full year. These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto contained in the Company's Annual Report to stockholders and Form 10-K for the year ended December 31, 2006 as filed with the Securities and Exchange Commission. The preparation of financial statements in conformity with GAAP also requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expense during the reporting period. Actual results could differ from those estimates. All material intercompany balances and transactions have been eliminated in consolidation.

Recently Issued Accounting Pronouncements:

In February 2006, the FASB issued SFAS No. 155, "Accounting for Certain Hybrid Financial Instruments," which amends the guidance in SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," and SFAS No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities." SFAS No. 155 provides entities with relief from having to separately determine the fair value of an embedded derivative that would otherwise be required to be bifurcated from its host contract in accordance with SFAS No. 133. SFAS No. 155 allows an entity to make an irrevocable election to measure such a hybrid financial instrument at fair value in its entirety, with changes in fair value recognized in earnings. SFAS No. 155 was effective January 1, 2007 for the Company for financial instruments acquired, issued or subject to a re-measurement event. The adoption of SFAS No. 155 did not have a material impact on the Company's financial condition, results of operations or cash flows.

In March 2006, the FASB issued SFAS No. 156, "Accounting for Servicing of Financial Assets," which amends the guidance in SFAS No. 140. SFAS No. 156 requires that an entity separately recognize a servicing asset or a servicing liability when it undertakes an obligation to service a financial asset under a servicing contract in certain situations. Such servicing assets or servicing liabilities are required to be measured initially at fair value, if practicable. SFAS No. 156 also allows an entity to measure its servicing assets and servicing liabilities subsequently using either the amortization method, which existed under SFAS No. 140, or the fair value measurement method. SFAS No. 156 was effective for the Company in the fiscal year beginning January 1, 2007. The adoption of SFAS No. 156 did not have a material impact on the financial condition, results of operations or cash flows of the Company.

In June 2006, the FASB issued Interpretation 48, "Accounting for Uncertainty in Income Taxes" ("FIN 48"), an interpretation of FASB Statement No. 109, "Accounting for Income Taxes." FIN 48 clarifies the accounting and reporting for income taxes where interpretation of the law is uncertain. FIN 48 prescribes a comprehensive model for the financial statement recognition, measurement, presentation and disclosure of income tax uncertainties with respect to positions taken or expected to be taken in income tax returns. FIN 48 is effective for fiscal years beginning after December 15, 2006. The Company adopted this Statement on January 1, 2007. As a result of the implementation of Interpretation 48, it was not necessary for the Company to recognize any increase in the liability for unrecognized tax benefits.

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The Company and its subsidiaries file income tax returns in the U.S. federal jurisdiction and California state jurisdictions. With few exceptions, the Company is no longer subject to U.S. federal and state examinations by tax authorities for years before 2003.

The Company will recognize interest and penalties accrued related to unrecognized tax benefits in income tax expense.

In September 2006, The Emerging Issues Task Force issued EITF 06-5, "Accounting for Purchases of Life Insurance-Determining the Amount That Could Be Realized in Accordance with FASB Technical Bulletin No. 85-4." This consensus concludes that a policyholder should consider any additional amounts included in the contractual terms of the insurance policy other than the cash surrender value in determining the amount that could be realized under the insurance contract. A consensus also was reached that a policyholder should determine the amount that could be realized under the life insurance contract assuming the surrender of an individual-life by individual-life policy (or certificate by certificate in a group policy). The consensuses are effective for fiscal years beginning after December 15, 2006. The adoption of EITF 06-5 did not have a material impact on the Company's financial condition, results of operations or cash flows.

Reclassifications

Certain reclassifications have been made to prior period balances in order to conform to the current year presentation.

2. ALLOWANCE FOR LOAN LOSSES

The allowance for loan losses is maintained at levels considered adequate by management to provide for loan losses that can be reasonably anticipated. The allowance is based on management's assessment of various factors affecting the loan portfolio, including problem loans, economic conditions and loan loss experience, and an overall evaluation of the quality of the underlying collateral.

Changes in the allowance for loan losses during the three-month periods ended March 31, 2007 and 2006 and for the year ended December 31, 2006 were as follows:

(in thousands)

	Three months ended March 31, 2007	Three months ended March 31, 2006	Year ended December 31, 2006
Balance, beginning of period	$ 8,361	$ 7,917	$ 7,917
(Recovery of) provision for loan losses	(170)	(575)	735
Loan charge-offs	(289)	(57)	(1,060)
Loan recoveries	48	513	769
Balance, end of period	$ 7,950	$ 7,798	$ 8,361

3. MORTGAGE OPERATIONS

Transfers and servicing of financial assets and extinguishments of liabilities are accounted for and reported based on consistent application of a financial-components approach that focuses on control. Transfers of financial assets that are sales are distinguished from transfers that are secured borrowings. Retained interests (mortgage servicing rights) in loans sold are measured by allocating the previous carrying amount of the transferred assets between the loans sold and retained interest, if any, based on their relative fair value at the date of transfer. Fair values are estimated using discounted cash flows based on a current market interest rate.

The Company recognizes a gain and a related asset for the fair value of the rights to service loans for others when loans are sold. The Company sold substantially all of its conforming long-term residential mortgage loans originated during the three months ended March 31, 2007 for cash proceeds equal to the fair value of the loans.

The recorded value of mortgage servicing rights is included in other assets, and is amortized in proportion to, and over the period of, estimated net servicing revenues. The Company assesses capitalized mortgage servicing rights for impairment based upon the fair value of those rights at each reporting date. For purposes of measuring impairment, the rights are stratified based upon the product type, term and interest rates. Fair value is determined by discounting estimated net future cash flows from mortgage servicing activities using discount rates that approximate current market rates and estimated prepayment rates, among other assumptions. The amount of impairment recognized, if any, is the amount by which the capitalized mortgage servicing rights for a stratum exceeds their fair value. Impairment, if any, is recognized through a valuation allowance for each individual stratum.

At March 31, 2007, the Company had $7,718,000 of mortgage loans held-for-sale. At March 31, 2007 and December 31, 2006, the Company serviced real estate mortgage loans for others of $112,273,000 and $112,742,000, respectively.

The following table summarizes the Company’s mortgage servicing rights assets as of March 31, 2007 and December 31, 2006.

(in thousands)

	December 31, 2006	Additions	Reductions	March 31, 2007
Mortgage servicing rights	$ 945	$ 43	$ 40	$ 948

There was no valuation allowance recorded for mortgage servicing rights as of March 31, 2007 and December 31, 2006.

4. OUTSTANDING SHARES AND EARNINGS PER SHARE

On January 25, 2007, the Board of Directors of the Company declared a 6% stock dividend paid March 30, 2007 to stockholders of record as of February 28, 2007.

Earnings per share amounts have been adjusted retroactively to reflect the effects of the stock dividend.

Earnings Per Share (EPS)

Basic EPS includes no dilution and is computed by dividing net income by the weighted average number of common shares outstanding for the period. Diluted EPS includes all common stock equivalents (“in-the-money” stock options, unvested restricted stock, stock units, warrants and rights, convertible bonds and preferred stock), which reflects the potential dilution of securities that could share in the earnings of an entity.

The following table presents a reconciliation of basic and diluted EPS for the three-month periods ended March 31, 2007 and 2006.

	(in thousands, except share and earnings per share amounts) Three months ended March 31,			
		2007		2006
Basic earnings per share:				
Net income	$	2,090	$	2,402
Weighted average common shares outstanding		8,431,880		8,503,922
Basic EPS	$	0.25	$	0.28
Diluted earnings per share:				
Net income	$	2,090	$	2,402
Weighted average common shares outstanding		8,431,880		8,503,922
Effect of dilutive options		259,902		315,896
Adjusted weighted average common shares outstanding		8,691,782		8,819,818
Diluted EPS	$	0.24	$	0.27

5. STOCK PLANS

On January 1, 2006, the Company adopted Statement of Financial Accounting Standards (“SFAS”) No. 123R, “Share-Based Payments,” which addresses the accounting for stock-based payment transactions whereby an entity receives employee services in exchange for equity instruments, including stock options. SFAS No. 123R eliminates the ability to account for stock-based compensation transactions using the intrinsic value method under Accounting Principles Board Opinion (“APB”) No. 25, “Accounting for Stock Issued to Employees,” and instead generally requires that such transactions be accounted for using a fair-value based method. The Company has elected the modified prospective transition method as permitted under SFAS No. 123R, and accordingly prior periods have not been restated to reflect the impact of SFAS No. 123R. The modified prospective transition method requires that stock-based compensation expense be recorded for all new and unvested stock options that are ultimately expected to vest as the requisite service is rendered beginning on January 1, 2006. Stock-based compensation for awards granted prior to January 1, 2006 is based upon the grant-date fair value of such compensation as determined under the pro forma provisions of SFAS No. 123, “Accounting for Stock-Based Compensation.” The Company issues new shares of common stock upon the exercise of stock options.

Prior to the adoption of SFAS No. 123R, the Company, during the first quarter of fiscal 2003, adopted the fair value recognition provisions of Financial Accounting Standards Board (“FASB”) Statement No. 148, *Accounting for Stock-Based Compensation - Transition and Disclosure, an amendment of FASB Statement No. 123*, for stock-based employee compensation, effective as of the beginning of the fiscal year. Under the prospective method of adoption selected by the Company, stock-based employee compensation recognized for all stock options granted after January 1, 2003 is based on the fair value recognition provisions of Statement 123. For stock options issued prior to January 1, 2003, the Company is using the intrinsic value method, under which compensation expense is recorded on the date of grant only if the current market price of the underlying stock exceeds the exercise price.

The following table presents the activity related to stock options and restricted stock for the three months ended March 31, 2007.

	Number of Shares	Weighted Average Exercise Price	Aggregate Intrinsic Value	Weighted Average Remaining Contractual Term
Options outstanding at Beginning of Period	549,000	$ 10.32		
Granted	49,924	16.75		
Cancelled / Forfeited	—	—		
Exercised	(13,324)	3.38	$ 240,921	
Options outstanding at End of Period	585,600	$ 11.03	$ 4,815,806	6.04
Exercisable (vested) at End of Period	421,707	$ 8.65	$ 4,218,298	5.06

The weighted average fair value of options and restricted stock granted during the three-month period ended March 31, 2007 was $9.58 per share.

As of March 31, 2007, there was $817,209 of total unrecognized compensation related to non-vested stock options. This cost is expected to be recognized over a weighted average period of approximately 2.3 years.

The Company determines fair value at grant date using the Black-Scholes-Merton pricing model that takes into account the stock price at the grant date, the exercise price, the risk free interest rate, the volatility of the underlying stock and the expected life of the option.

The weighted average assumptions used in the pricing model are noted in the following table. The expected term of options granted is derived from historical data on employee exercise and post-vesting employment termination behavior. The risk free rate for periods within the contractual life of the option is based on the U.S. Treasury yield curve in effect at the time of the grant. Expected volatility is based on both the implied volatilities from the traded option on the Company's stock and historical volatility on the Company's stock.

The Bank expenses the fair value of the option on a straight line basis over the vesting period. The Bank estimates forfeitures and only recognizes expense for those shares expected to vest. The Bank's estimated forfeiture rate in the first three months of 2007, based on historical forfeiture experience, is approximately 0.0%.

A summary of the weighted average assumptions used in valuing stock options during the three months ended March 31, 2007 is presented below:

	Three Months Ended March 31, 2007
Risk Free Interest Rate	4.67%
Expected Dividend Yield	0.0%
Expected Life in Years	4.18
Expected Price Volatility	26.03%

The Company has a 2000 Employee Stock Purchase Plan ("ESPP"). Under the plan, the Company is authorized to issue to an eligible employee shares of common stock. There are 265,000 (adjusted for the 2007 stock dividend) shares authorized under the Plan. The Plan will terminate February 27, 2017. The Plan is implemented by participation periods of not more than twenty-seven months each. The Board of Directors determines the commencement date and duration of each participation period. The Board of Directors approved the current participation period of November 24, 2006 to November 23, 2007. An eligible employee is one who has been continually employed for at least ninety (90) days prior to commencement of a participation period. Under the terms of the Plan, employees can choose to have up to 10 percent of their compensation withheld to purchase the Company's common stock each participation period. The purchase price of the stock is 85 percent of the lower of the fair market value on the last trading day before the Date of Participation or the fair market value on the last trading day during the participation period.

As of March 31, 2007, there was $35,000 of recognized compensation and $92,000 of unrecognized compensation related to ESPP options. This cost is expected to be recognized over a weighted average period of approximately 0.75 years.

The weighted average fair value at grant date is $6.08.

A summary of the weighted average assumptions used in valuing ESPP options during the three months ended March 31, 2007 is presented below:

	Three Months Ended March 31, 2007
Risk Free Interest Rate	5.00%
Expected Dividend Yield	0.00%
Expected Life in Years	1.00
Expected Price Volatility	22.97%

6. FIRST NORTHERN BANK - EXECUTIVE RETIREMENT PLAN

First Northern Bank has an unfunded noncontributory defined benefit pension plan provided in two forms to a select group of highly compensated employees. Four executives have Salary Continuation Benefits providing retirement benefits between $50,000 and $100,000 depending on responsibilities and tenure at the bank. The retirement benefits are paid for 10 years following retirement at age 65. Reduced retirement benefits are available after age 55 and 10 years of service.

The Supplemental Executive Retirement Plan is intended to provide a fixed annual benefit for 10 years plus 6 months for each full year of service over 10 years (limited to 180 months total) subsequent to retirement at age 65. Reduced benefits are payable as early as age 55 if the participant has at least 10 years of service. Two employees currently have Supplemental Executive Retirement agreements. The agreements provide a target benefit of 2% (2.5% for the CEO) times years of service times final average compensation. Final average compensation is defined as three-year average salary plus seven-year average bonus. The target benefit is reduced by benefits from social security and First Northern Bank's profit sharing plan. The maximum target benefit is 50% of final average compensation.

	Three months ended March 31,			
	2007		2006	
Components of Net Periodic Benefit Cost				
Service Cost	$	30,383	$	41,146
Interest Cost		28,784		16,155
Amortization of prior service cost		21,821		3,257
Net periodic benefit cost	$	80,988	$	60,558

The Bank estimates that the annual net periodic benefit cost will be $323,745 for the year ended December 31, 2007. This compares to annual net periodic benefit costs of $260,592 for the year ended December 31, 2006.

Estimated Contributions for Fiscal 2007

For unfunded plans, contributions to the “Executive Salary Continuation Plan” are the benefit payments made to participants. At December 31, 2006 the Bank expected to make benefit payments of $54,144 in connection with the “Executive Salary Continuation Plan” during fiscal 2007.

7. FIRST NORTHERN BANK - DIRECTORS' RETIREMENT PLAN

First Northern Bank has an unfunded noncontributory defined benefit pension plan ("Directors' Retirement Plan") for directors of the bank. The plan provides a retirement benefit equal to $1,000 per year of service as a director up to a maximum benefit of $15,000. The retirement benefit is payable for 10 years following retirement at age 65. Reduced retirement benefits are available after age 55 and 10 years of service.

	Three months ended March 31,			
	2007		2006	
Components of Net Periodic Benefit Cost				
Service Cost	$	14,366	$	13,518
Interest Cost		6,736		5,943
Amortization of net loss		121		234
Net periodic benefit cost	$	21,223	$	19,695

The Bank estimates that the annual net periodic benefit cost will be $84,890 for the year ended December 31, 2007. This compares to annual net periodic benefit costs of $78,774 for the year ended December 31, 2006.

Estimated Contributions for Fiscal 2007

For unfunded plans, contributions to the "Directors' Retirement Plan" are the benefit payments made to participants. At December 31, 2006 the Bank expected to make cash contributions of $15,000 to the "Directors' Retirement Plan" during fiscal 2007.

ITEM 2.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

FORWARD-LOOKING STATEMENTS

This report contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, and subject to the "safe harbor" created by those sections. Forward-looking statements include the information concerning possible or assumed future results of operations of the Company set forth under the heading "Management's Discussion and Analysis of Financial Condition and Results of Operations." Forward-looking statements also include statements in which words such as "expect," "anticipate," "intend," "plan," "believe," estimate," "consider" or similar expressions are used, and include assumptions concerning the Company's operations, future results and prospects. These forward-looking statements are based upon current expectations and are subject to risks, uncertainties and assumptions, which are difficult to predict. Therefore, actual outcomes and results may differ materially from those set forth in or implied by the forward-looking statements and related assumptions. Some factors that may cause actual results to differ from the forward-looking statements include the following: (i) the effect of changing regional and national economic conditions, including the continuing fiscal challenges for the State of California; (ii) uncertainty regarding the economic outlook resulting from the continuing hostilities in Iraq and the war on terrorism, as well as actions taken or to be taken by the United States or other governments as a result of further acts or threats of terrorism; (iii) significant changes in interest rates and prepayment speeds; (iv) credit risks of commercial, agricultural, real estate, consumer and other lending activities; (v) adverse effects of current and future federal and state banking or other laws and regulations or governmental fiscal or monetary policies; (vi) competition in the banking industry; (vii) changes in accounting standards; and (viii) other external developments which could materially impact the Company's operational and financial performance. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof. The Company undertakes no obligation to update any forward-looking statements to reflect events or circumstances arising after the date on which they are made. For additional information concerning risks and uncertainties related to the Company and its operations, please refer to the Company's Annual Report on Form 10-K for the year ended December 31, 2006 and Item 1A. of Part II of this Report.

The following is a discussion and analysis of the significant changes in the Company's Unaudited Condensed Consolidated Balance Sheets and of the significant changes in income and expenses reported in the Company's Unaudited Condensed Consolidated Statements of Income and Stockholders' Equity and Comprehensive Income as of and for the three-month periods ended March 31, 2007 and 2006 and should be read in conjunction with the Company's consolidated 2006 financial statements and the notes thereto contained in the Company's Annual Report to Stockholders and Form 10-K for the year ended December 31, 2006, along with other financial information included in this Report.

INTRODUCTION

This overview of Management's Discussion and Analysis highlights selected information in this quarterly report and may not contain all of the information that is important to you. For a more complete understanding of trends, events, commitments, uncertainties, liquidity, capital resources and critical accounting estimates, you should carefully read this entire quarterly report, together with our Consolidated Financial Statements and the Notes to Consolidated Financial Statements included in our Annual Report on Form 10-K for the year ended December 31, 2006.

Our subsidiary, First Northern Bank of Dixon (the "Bank"), is a California state-chartered bank that derives most of its revenues from lending and deposit taking in the Sacramento Valley region of Northern California. Interest rates, business conditions and customer confidence all affect our ability to generate revenues. In addition, the regulatory environment and competition can challenge our ability to generate those revenues.

Significant results and developments during the first quarter 2007 include:

· Net income of $2.09 million, down 12.9% over the $2.40 million earned in the same fiscal period last year. (First quarter 2007 net income was increased through a $100,000, net of tax, recovery of provision for loan losses from a prior period. First quarter 2006 net income was increased through a $339,000, net of tax, recovery of provision for loan losses from a prior period.)

Without the additional items referenced above, net income would have been $1.99 million for 2007 and $2.06 million for 2006, a decrease of 3.4%

· Diluted earnings per share for the three months ended March 31, 2007 of $0.24, down 11.1% from the $0.27 reported in the same period last year (all 2006 per share earnings have been adjusted for the 6% stock dividend paid March 30, 2007).

· Recovery of provision for loan losses from a prior period of $170,000 for the three-month period ended March 31, 2007 compared to a recovery of provision for loan losses from a prior period of $575,000 for the same period in 2006.

· Provision for unfunded lending commitment losses of $50,000 for the three-month period ended March 31, 2007 compared to a provision for unfunded lending commitment losses of $100,000 for the same period in 2006.

· Annualized Return on Average Assets for the three-month period ended March 31, 2007 of 1.22%, compared to 1.44% for the same period in 2006.

· Annualized Return on Beginning Equity for the three-month period ended March 31, 2007 of 13.49%, compared to 16.91% for the same period in 2006.

· Total assets at March 31, 2007 of $694.0 million, an increase of $32.0 million, or 4.8%, from prior-year first quarter levels.

· Total deposits of $614.7 million at March 31, 2007, an increase of $25.7 million or 4.4% compared to March 31, 2006.

· Total net loans at March 31, 2007 (including loans held-for-sale) increased $2.4 million, or 0.5%, to $470.4 million compared to March 31, 2006.

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Total investment securities at March 31, 2007 increased $18.2 million, or 29.4%, to $80.1 million compared to March 31, 2006.

SUMMARY

The Company recorded net income of $2,090,000 for the three-month period ended March 31, 2007, representing a decrease of $312,000 or 13.0% from net income of $2,402,000 for the same period in 2006.

The following table presents a summary of the results for the three-month periods ended March 31, 2007 and 2006.

(Amounts in thousands, except percentage and per share amounts)

.	Three months ended March 31, 2007	Three months ended March 31, 2006
For the Period:		