SOUTHERN CONNECTICUT BANCORP INC
Form 10KSB
March 30, 2004

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

F O R M 10 - KSB

[X] ANNUAL REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 For the Fiscal Year Ended December 31, 2003.

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 333-59824

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

Connecticut (State or other jurisdiction of incorporation or organization)	06-1594123 (I.R.S. Employer Identification Number)
215 Church Street New Haven, Connecticut (Address of Principal Executive Offices)	06510 (Zip Code)
Issuer's telephone number	(203) 782-1100

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

None

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

Common Stock, par value $.01 per share
(Title of Class)

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 __X__ No _____

Check if disclosure of delinquent filers in response to Item 405 of Regulation S-B is not 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. [ ]

State issuer's revenue for its most recent fiscal year: $3,008,418

Aggregate market value of the voting stock held by nonaffiliates (assumes directors and executive officers are nonaffiliates) of the registrant as of February 27, 2004: $8,338,700

Number of shares of the registrant's Common Stock, par value $.01 per share, outstanding as of February 27, 2004: 1,063,320

DOCUMENTS INCORPORATED BY REFERENCE

Proxy Statement for 2004 Annual Meeting of Shareholders. (A of this Form 10-KSB definitive proxy statement will be filed with the Securities and Exchange Commission within 120 days after the close of the fiscal year covered by this Form 10-KSB.)	Incorporated into Part III

Transitional Small Business Disclosure Format (check one):

Yes _____; No__X__

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Part III

PART I

Item 1. Description of Business.

Southern Connecticut Bancorp, Inc. ("Bancorp"), a Connecticut corporation, was incorporated on November 8, 2000 to serve as a bank holding company. Bancorp owns one hundred percent of the capital stock of The Bank of Southern Connecticut (the "Bank"), a state chartered bank in New Haven, Connecticut, which commenced operations on October 1, 2001 after receiving its Final Certificate of Authority from the Connecticut Banking Commissioner and its deposit insurance from the Federal Deposit Insurance Corporation ("FDIC"). Bancorp invested $10,000,000 of the net proceeds of its July 26, 2001 stock offering to purchase the capital stock of the Bank and an additional $360,000 to cover the Bank's pre-opening deficit. The $10,000,000 of initial equity capital for the Bank required under The Bank of Southern Connecticut's Temporary Certificate of Authority substantially exceeded the statutory minimum equity capital for a new Connecticut bank of $5,000,000. Bancorp chose a holding company structure because it provides flexibility that would not otherwise be available. For example, Bancorp could acquire additional banks, establish de novo banks and other businesses, including mortgage companies, leasing companies, insurance agencies and small business investment companies. Bancorp may in the future decide to engage in additional businesses permitted to bank holding companies or financial holding companies. Before Bancorp could acquire interests in other banks, establish de novo banks or expand into other businesses, it may need to obtain regulatory approvals and might need additional capital.

Bancorp has leased a free-standing building located at 215 Church Street, New Haven, Connecticut, located in the central business and financial district of New Haven. It has assigned this lease to The Bank of Southern Connecticut, and the Bank has assumed all rights and obligations under this lease. Both Bancorp and the Bank operate from this facility. On October 7, 2002 the Bank opened a branch office in Branford, Connecticut at West Main Street and Summit Place. On August 15, 2002 the Bank also purchased a building at 1475 Whalley Avenue in the Westville section of New Haven for a new branch office site which was opened March 24, 2003.

The following table sets forth the location of the Bank's branch offices and other related information:

Office	Location	Status
Main Office	215 Church Street, New Haven, Connecticut	Leased
Branford Office	445 West Main Street, Branford, Connecticut	Leased
Amity Office	1475 Whalley Avenue, New Haven, Connecticut	Owned

Bancorp has submitted an application to the Department of Banking of the State of Connecticut to charter a bank to be located in New London, Connecticut. The application is pending with the Department of Banking and a decision is anticipated in the second quarter of 2004. Presuming approval by the Department of Banking, Bancorp will proceed to file an application with the Federal Deposit Insurance Corporation for deposit insurance approval and an application with the Federal Reserve Bank of Boston for approval to acquire the new state chartered bank. The New London based bank will be named The Bank of Southeastern Connecticut and will be operated similarly to The Bank of Southern Connecticut. Bancorp will provide certain management and operations support and services to the two banks as well as certain infrastructure. Bancorp will seek to raise additional capital in order to capitalize the new bank as well as for other purposes. (See further discussion below and in Liquidity)

Bancorp entered into a lease on January 14, 2004 with the City of New London for a facility located at 15 Mason Street, New London, Connecticut. This facility is intended to be the main office of the proposed wholly owned state chartered subsidiary bank to be named The Bank of Southeastern Connecticut. (See Description of Property)

Bancorp anticipates, subject to regulatory approval of the proposed bank, improving the leased building and purchasing furniture and equipment for the proposed Bank of Southeastern Connecticut, which is expected to commence operations in the fourth quarter of 2004 (See Description of Property). Currently, there are no plans involving the significant purchase or sale of property or equipment in the next twelve months. Bancorp intends to recruit a majority of Directors, as well as the executive management and employees of The Bank of Southeastern Connecticut from within the New London market area. Outside of staffing the new bank, Bancorp does not anticipate a significant change in the number of its employees.

Bancorp will seek to raise $10 to $15 million in new capital of which approximately $6 million will be used to fund the start up of the new bank. Bancorp expects the new bank to be operating by the end of 2004. The balance will be retained by Bancorp for other business purposes including the likely contribution of additional capital to The Bank of Southern Connecticut.

On November 17, 2003, SCB Capital, Inc., a wholly-owned subsidiary of Bancorp, was incorporated. SCB Capital, Inc. will engage in a limited range of investment banking, advisory and financial brokerage services primarily to small to medium size business clients of Bancorp and the general public located in Connecticut. SCB Capital, Inc. is in the process of applying for approval as and membership with the National Association of Security Dealers as a broker-dealer. SCB Capital, Inc. has not been capitalized nor has it commenced operations. The amount to be invested in SCB Capital, Inc. will be determined by Bancorp's Board of Directors following completion of the application process.

Bancorp's current and proposed bank subsidiaries are not expected to compete with large institutions for the primary banking relationships of large corporations, but to compete for niches in this business segment and for the consumer business of employees of such entities. The Bank of Southern Connecticut focuses on small to medium-sized businesses, professionals and individuals and their employees. This focus includes retail, service, wholesale distribution, manufacturing and international businesses. The Bank of Southern Connecticut attracts these customers based on relationships and contacts which the Bank's directors and management have within and beyond its primary service area. It is anticipated that the proposed The Bank of Southeastern Connecticut will pursue a similar strategy in the greater New London market. The strategy includes, among other factors, substantial local bank board representation, local credit decision authority, focus on the local business community, personal service, and support of community interests. Additional employees will be recruited to staff the new bank.

Greater New Haven, where The Bank of Southern Connecticut is located, is currently served by approximately 70 offices of commercial banks, none of which are headquartered in New Haven. In addition, New Haven Savings Bank, a mutual savings bank, has 16 branches in the New Haven market. All of these banks are substantially larger than The Bank of Southern Connecticut expects to be in the near future and are able to offer products and services which may be impracticable to provide at this time. The New Haven Savings Bank has approval to convert to a stock state chartered savings bank charter and to acquire two other bank holding companies located in the state of Connecticut during 2004.

There are numerous banks and other financial institutions serving the communities surrounding New Haven which also draw customers from New Haven, posing significant competition to attract deposits and loans. The Bank of Southern Connecticut also experiences competition from out-of-state financial institutions. The Bank will have to continue to obtain customers from the customer base of such existing banks and financial institutions and from growth in New Haven and the surrounding area. Many of such banks and financial

institutions are well established and well capitalized, allowing them to provide a greater range of services (including trust services) than the Bank will be able to offer in the near future.

Intense market demands, economic pressures and significant legislative and regulatory actions have eroded banking industry classifications which were once clearly defined and have increased competition among banks and other financial institutions. Market dynamics and legislative and regulatory changes impacting banks and other financial institutions have resulted in a number of new competitors offering services historically offered only by commercial banks; non-bank corporations offering services traditionally offered only by banks; increased customer awareness of product and service differences among competitors; and increased merger activity.

Additional legislative and regulatory changes may affect The Bank of Southern Connecticut in the future; however, the nature of such changes and the effect of their implementation cannot be assessed. New rules and regulations may, among other things, revise limits on interest rates on various categories of deposits and may limit or influence interest rates on loans. Monetary and fiscal policies of the United States government and its instrumentalities, including the Federal Reserve, significantly influence the growth of loans, investments and deposits. The present bank regulatory scheme is undergoing significant change both as it affects the banking industry itself and as it affects competition between banks and non-bank financial institutions.

The Bank of Southern Connecticut currently offers products and services described as "core" products and services which are more completely described below. Through correspondent and other relationships, it is expected that the Bank will be able to help our customers meet all of their banking needs, including obtaining services which The Bank of Southern Connecticut may not offer directly.

The Bank of Southern Connecticut continues to attract a sound base of core deposits, including checking accounts, money market accounts, savings accounts, sweep accounts, NOW accounts and a variety of certificates of deposits and IRA accounts. To attract deposits, The Bank of Southern Connecticut is employing an aggressive marketing plan in its service area and features a broad product line and rates and services competitive with those offered in the New Haven market. The primary sources of deposits have been and are expected to be, residents of, and businesses and their employees located in, New Haven and the surrounding communities. The Bank is obtaining these deposits through personal solicitation by its officers and directors, outside programs and advertisements published and / or broadcasted in the local media.

Deposits and The Bank of Southern Connecticut's equity capital are the sources of funds for lending and investment activities. Repayments on loans, investment income and proceeds from the sale and maturity of investment securities also provide additional funds for these purposes. While scheduled principal repayments on loans and investment securities are a relatively predictable source of funds, deposit flows and loan prepayments are greatly influenced by general interest rates, economic conditions and competition. The Bank is expected to manage the pricing of deposits to maintain a desired deposit balance. The Bank offers drive-in teller services, wire transfer, lock box and safe deposit services.

The Bank of Southern Connecticut's loan strategy is to offer a broad range of loans to businesses and individuals in its service area, including commercial and business loans, personal loans, mortgage loans, home equity loans, automobile loans and education loans. The Bank has received lending approval status from the Small Business Administration ("SBA") to enable it to make SBA loans to both the Greater New Haven business community and companies throughout the State of Connecticut. The marketing focus on small to medium-size businesses and professionals may result in an assumption of certain lending risks that are different from or greater than those which would apply to loans made to larger companies or consumers. Commercial loans generally entail certain additional risks because repayment is usually dependent on the success of the enterprise. The Bank seeks to manage the credit risk inherent in its loan portfolio through credit controls, loan diversification and a loan review program. Prior to approving a loan, the Bank evaluates: the credit histories of

potential borrowers; the value and liquidity of available collateral; the purpose of the loan; the source and reliability of funds for repayment and other factors considered relevant in the circumstances.

Loans are made on a variable or fixed rate basis with fixed rate loans limited to five year terms. All loans are approved by The Bank of Southern Connecticut's management and the Loan Committee of the Bank's Board of Directors. At the present time, the Bank is not syndicating or securitizing loans. The Bank, at times, participates in multi-bank loans to companies in its service area. Commercial loans and commercial real estate loans may be written for terms of up to twenty years. Loans to purchase or refinance commercial real estate are supported by personal guarantees of the makers and related parties and are collateralized by the subject real estate, which may in 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.

Other services currently provided include, cashier's checks, money orders, travelers checks, bank by mail, direct deposit and U. S. Savings Bonds. The Bank of Southern Connecticut 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 currently expect to offer trust services but may offer trust services through a joint venture with a larger institution. To offer such services in the future, the Bank would need the approval of the Connecticut Banking Commissioner.

Another significant activity for The Bank of Southern Connecticut is maintaining an investment portfolio. Although granting a variety of loans to generate interest income and loan fees is an important aspect of the Bank's business plan, the aggregate amount of loans will be subject to maintaining a satisfactory loan-to-deposit ratio. The Bank's overall portfolio objective is to maximize the long-term total rate of return through active management of portfolio holdings taking into consideration estimated asset/liability and liquidity needs, tax equivalent yields and maturities. 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 expects that investments in equity securities will be very limited. The Bank's current investment portfolio is limited to U. S. government agency obligations and agency issue 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.

Overall, The Bank of Southern Connecticut's plan of operation is focused on responsible growth and pricing of deposits and loans, and investment in high quality U. S. government securities to achieve a net interest margin sufficient to cover operating expenses, achieve profitable operations and maintain liquidity. The Bank is seeking to develop additional fee income sources to supplement the core bank product offerings.

Currently, The Bank of Southern Connecticut has 29 full-time and no part-time employees. Most routine day-to-day banking transactions are performed at the Bank by its employees. However, the Bank has entered into a number of arrangements for banking services such as correspondent banking, data processing and armored carriers.

Supervision and Regulation

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

Regulations to which Bancorp is subject

As a bank holding company, Bancorp is regulated by and subject to the supervision of the Board of Governors of the Federal Reserve System (the "FRB") and is required to file with the FRB an annual report and such other information as may be required. The FRB has the authority to conduct examinations of Bancorp as well.

The Bank Holding Company Act of 1956 (the "BHC Act") limits the types of companies which Bancorp may acquire or organize and the activities in which they may engage. In general, a bank holding company and its subsidiaries are prohibited from engaging in or acquiring control of any company engaged in non-banking activities unless such activities are so closely related to banking or managing and controlling banks as to be a proper incident thereto. Activities determined by the FRB to be so closely related to banking within the meaning of the BHC Act include operating a mortgage company, finance company, credit card company, factoring company, trust company or savings association; performing certain data processing operations; providing limited securities brokerage services; acting as an investment or financial advisor; acting as an insurance agent for certain types of credit-related insurance; leasing personal property on a full-payout, non-operating basis; providing tax planning and preparation service; operating a collection agency; and providing certain courier services. The FRB also had determined that certain other activities, including real estate brokerage and syndication, land development, property management and underwriting of life insurance unrelated to credit transactions, are not closely related to banking and therefore are not a proper activity for a bank holding company.

In November 1999, Congress amended certain provisions of the BHC Act through passage of the Gramm-Leach-Bliley Act. Under this new legislation, a bank holding company may elect to become a "financial holding company" and thereby engage in a broader range of activities than would be permissible for traditional bank holding companies. In order to qualify for the election, all of the depository institution subsidiaries of the bank holding company must be well capitalized and well managed, as defined under FRB regulations, and all such subsidiaries must have achieved a rating of "satisfactory" or better with respect to meeting community credit needs. Pursuant to the Gramm-Leach-Bliley Act, financial holding companies are permitted to engage in activities that are "financial in nature" or incidental or complementary thereto, as determined by the FRB. The Gramm-Leach-Bliley Act identifies several activities as "financial in nature", including, among others, insurance underwriting and agency activities, investment advisory services, merchant bank and underwriting, and dealing in or making a market in securities.

The Gramm-Leach-Bliley Act also makes it possible for entities engaged in providing various other financial services to form financial holding companies and form or acquire banks. Accordingly, the Gramm-Leach-Bliley Act makes it possible for a variety of financial services firms to offer products and services comparable to the products and services offered by the Bank.

There are various statutory and regulatory limitations regarding the extent to which present and future banking subsidiaries of Bancorp can finance or otherwise transfer funds to Bancorp or its non-banking subsidiaries, whether in the form of loans, extensions of credit, investments or asset purchases, including regulatory limitation on the payment of dividends directly or indirectly to Bancorp from the Bank. Federal and state bank regulatory agencies also have the authority to limit further the Bank's payment of dividends based on such factors as the maintenance of adequate capital for such subsidiary bank, which could reduce the amount of dividends otherwise payable. Under the policy of the FRB, Bancorp is expected to act as a source of financial strength to the Bank and to commit resources to support the Bank in circumstances where Bancorp might not elect to do so absent such policy.

The FRB has established capital adequacy guidelines for bank holding companies that are similar to the Federal Deposit Insurance Corporation ("FDIC") capital requirements for the Bank described below.

Regulations to which the Bank is subject

The Bank of Southern Connecticut 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 regulatory and insurer of deposits. While the Bank is not a member of the Federal Reserve System, it is subject to certain regulations of the FRB. 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 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.

Federal laws and regulations also limit, with certain exceptions, the ability of state banks to engage in activities or make equity investments that are not permissible for national banks. Bancorp does not expect such provisions to have a material adverse effect on Bancorp or the Bank.

Capital Standards

The FDIC has adopted risk-based capital guidelines to which FDIC-insured, state-chartered banks that are not members of the Federal Reserve System, such as the Bank, are subject. The guidelines establish a systematic analytical framework that makes regulatory capital requirements more sensitive to the differences in risk profiles among banking organizations. Banks are required to maintain minimum levels of capital based upon their total assets and total "risk-weighted assets." For purposes of these requirements, capital is comprised of both Tier 1 and Tier 2 capital. Tier 1 capital consists primarily of common stock and retained earnings. Tier 2 capital consists primarily of loan loss reserves, subordinated debt, and convertible securities. In determining total capital, the amount of Tier 2 capital may not exceed the amount of Tier 1 capital. A bank's total "risk-based assets" are determined by assigning the bank's assets and off-balance sheet items (e.g., letters of credit) to one of four risk categories based upon their relative credit risks. The greater the risk associated with an asset, the greater the amount of such asset that will be subject to capital requirements.

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 exposure; asset growth; compensation; fees and benefits; and such other operational and managerial standards as the agency deems appropriate. The federal banking agencies adopted final 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; 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 Federal Deposit Insurance Act. The final regulations establish deadlines for submission and review of such safety and soundness compliance plans.

The federal banking agencies also have adopted final 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.

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. The law requires each federal banking agency to promulgate regulations defining the following five categories in which an insured depository institution will be placed, based on the level of its capital ratios: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized and critically undercapitalized. In September 1992, the federal banking agencies issued uniform final regulations implementing the prompt corrective action provisions of federal law.

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 regulatory. 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. As of December 31, 2003, the most recent notification from the Federal Deposit Insurance Corporation and the State of Connecticut Department of Banking categorized the Bank as well capitalized under the regulatory framework for prompt corrective

action. There are no conditions or events that management believes have changed the Bank's category.

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.

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 law 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 savings 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 Financial Institutions Reform, Recovery and Enforcement Act (FIRREA) amended the CRA to require public disclosure of an institution's CRA rating and require the FDIC to provide a written evaluation 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 or other financial institutions, which require regulatory approval based, in part, on CRA Compliance considerations.

Interstate Banking and Branching

Under the Riegel-Neal Interstate Banking and Branching Efficiency Act of 1994, as amended (the "Interstate Act, a bank holding company that is adequately capitalized and managed may obtain approval under the BHCA to acquire an existing bank located in another state generally without regard to state law prohibitions on such acquisitions. A bank holding company, however, can not be permitted to make such an acquisition if, upon consummation, it would control (a) more than 10% of the total amount of deposits of insured depository institutions in the United States or (b) 30% or more of the deposits in the state in which the bank is located. A state may limit the percentage of total deposits that may be held in that state by any one bank or bank holding company if application of such limitation does not discriminate against out of state banks. An out of state bank holding company may not acquire a state bank in existence for less than a minimum length of time that may be prescribed by state law except that a state may not impose more than a five year existence requirement. Since June 1, 1997 (and prior to that date in some instances), banks have been able to expand across state lines where qualifying legislation adopted by certain states prior to that date prohibits such interstate expansion. Banks may also expand across state lines through the acquisition of an individual branch of a bank located in another state or through the establishment of a de novo branch in another state where the law of the state in which the branch is to be acquired or established specifically authorizes such acquisition or de novo branch establishment.

The USA PATRIOT Act

In response to the events of September 11, 2001, the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001, or the USA PATRIOT Act, was signed into law on October 26, 2001. The USA PATRIOT Act gives the federal government new powers to address terrorist threats through enhanced domestic security measures, expanded surveillance powers, increased information sharing and broadened anti-money laundering requirements. By way of amendments to the Bank Secrecy Act, Title III of the USA PATRIOT Act takes measures intended to encourage information sharing among bank regulatory agencies and law enforcement bodies. Further, certain provisions of Title III impose affirmative obligations on a broad range of

financial institutions, including banks, thrifts, brokers, dealers, credit unions, money transfer agents and parties registered under the Commodity Exchange Act.

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

- Pursuant to Section 352, all financial institutions must establish anti-money laundering programs that include, at minimum: (i) internal policies, procedures, and controls; (ii) specific designation of an anti-money laundering compliance officer; (iii) ongoing employee training programs; and (iv) an independent audit function to test the anti-money laundering program.

- Section 326 authorizes the Secretary of the Department of Treasury, in conjunction with other bank regulators, to issue regulations by October 26, 2002 that provide for minimum standards with respect to customer identification at the time new accounts are opened.

- Section 312 requires financial institutions that establish, maintain, administer, or manage private banking accounts or correspondence accounts in the United States for non-United States persons or their representatives (including foreign individuals visiting the United States) to establish appropriate, specific, and, where necessary, enhanced due diligence policies, procedures, and controls designed to detect and report money laundering.

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

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

The federal banking agencies have begun to propose and implement regulations pursuant to the USA PATRIOT Act. These proposed and interim regulations would require financial institutions to adopt the policies and procedures contemplated by the USA PATRIOT Act.

Sarbanes-Oxley Act of 2002

On July 30, 2002, the President signed into law the Sarbanes-Oxley Act of 2002 ("Sarbanes-Oxley"), which implemented legislative reforms intended to address corporate and accounting fraud. In addition to the establishment of a new accounting oversight board that will enforce auditing, quality control and independence standards and will be funded by fees from all publicly traded companies, Sarbanes-Oxley places certain restrictions on the scope of services that may be provided by accounting firms to their public company audit clients. Any non-audit services being provided to a public company audit client will require preapproval by the company's audit committee. In addition, Sarbanes-Oxley makes certain changes to the requirements for audit partner rotation after a period of time. Sarbanes-Oxley requires chief executive officers and chief financial officers, or their equivalent, to certify to the accuracy of periodic reports filed with the Securities and Exchange Commission, subject to civil and criminal penalties if they knowingly or willingly violate this certification requirement. The Company's Chief Executive Officer and Chief Financial Officer, and the Bank's President, have signed certifications to this Form 10-KSB as required by Sarbanes-Oxley. In addition, under Sarbanes-Oxley, counsel will be required to report evidence of a material violation of the securities laws or a breach of fiduciary duty by a company to its chief executive officer or its chief legal officer, and, if such officer does not appropriately respond, to report such evidence to the audit committee or other similar committee of the board of directors or the board itself.

Under Sarbanes-Oxley, longer prison terms will apply to corporate executives who violate federal securities laws; the period during which certain types of suits can be brought against a company or its officers is extended; and bonuses issued to top executives prior to restatement of a company's financial statements are now subject to disgorgement if such restatement was due to corporate misconduct. Executives are also prohibited from trading the company's securities during retirement plan "blackout" periods, and loans to company executives (other than loans by financial institutions permitted by federal rules and regulations) are restricted. In addition, a provision directs that civil penalties levied by the Securities and Exchange Commission as a result of any judicial or administrative action under Sarbanes-Oxley be deposited to a fund for the benefit of harmed investors. The Federal Accounts for Investor Restitution provision also requires the Securities and Exchange Commission to develop methods of improving collection rates. The legislation accelerates the time frame for disclosures by public companies, as they must immediately disclose any material changes in their financial condition or operations. Directors and executive officers must also provide information for most changes in ownership in a company's securities within two business days of the change.

Sarbanes-Oxley also increases the oversight of, and codifies certain requirements relating to audit committees of public companies and how they interact with the company's "registered public accounting firm." Audit Committee members must be independent and are absolutely barred from accepting consulting, advisory or other compensatory fees from the issuer. In addition, companies must disclose whether at least one member of the committee is a "financial expert" (as such term is defined by the Securities and Exchange Commission) and if not, why not. Under Sarbanes-Oxley, a company's registered public accounting firm is prohibited from performing statutorily mandated audit services for a company if such company's chief executive officer, chief financial officer, comptroller, chief accounting officer or any person serving in equivalent positions had been employed by such firm and participated in the audit of such company during the one-year period preceding the audit initiation date. Sarbanes-Oxley also prohibits any officer or director of a company or any other person acting under their direction from taking any action to fraudulently influence, coerce, manipulate or mislead any independent accountant engaged in the audit of the company's financial statements for the purpose of rendering the financial statements materially misleading. Sarbanes-Oxley also requires the Securities and Exchange Commission to prescribe rules requiring inclusion of any internal control report and assessment by management in the annual report to shareholders. Sarbanes-Oxley requires the company's registered public accounting firm that issues the audit report to attest to and report on management's assessment of the company's internal controls.

Factors Affecting Future Results

In addition to historical information, this Form 10-KSB includes certain forward looking statements that involve risks and uncertainties such as statements of Bancorp's plans, expectations and unknown outcomes. Bancorp's actual results could differ materially from management expectations. Factors that could contribute to those differences include, but are not limited to, general economic conditions, legislative and regulatory changes, monetary and fiscal policies of the federal government, changes in tax policies, rates and regulations of federal and local tax authorities, changes in interest rates, deposit flows, the cost of funds, demand for loan products, demand for financial services, competition, changes in the quality or composition of the Bank's loan and investment portfolios, changes in ownership status resulting in, among other things, change in accounting principles, policies or guidelines, and other economic, competitive, governmental and technological factors affecting the Company's operations, markets, products, services and prices.

Item 2. Description of Property.

Bancorp executed a lease for a free-standing building located at 215 Church Street, New Haven, Connecticut, in the central business and financial district of New Haven. The lease was assigned to The Bank of Southern Connecticut, and the Bank assumed, all obligations there under. The location is a former bank branch, which has been renovated for use as the headquarters of

the Bank and Bancorp. The building has a drive-up teller, an automated teller machine, two vaults and a night deposit drop.

The lease is for an initial term of five years and three months, with an option to extend the lease for up to three additional terms of five years. There was no base rent payable for the first three months of the initial term and monthly rent was $4,117 until August 1, 2001. The annual base rent during the balance of the initial term will be $107,400 for the first year and increases each year to $125,500 for the fifth year. The base rent for the option periods is also 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. The Bank, as Bancorp's assignee, will have a right of first refusal to purchase the building.

To the extent that the building contains space not needed for operations, the Bank expects to sublease such excess to the extent practicable. The Bank of Southern Connecticut had subleased approximately 1,045 square feet to Laydon and Company, LLC, an entity owned by Elmer A. Laydon, the son of Elmer F. Laydon, one of Bancorp's directors.

The Bank of Southern Connecticut entered into a lease agreement on August 7, 2002 to lease the facility at 445 West Main Street, Branford, Connecticut, the site of the Branford branch which opened for business on October 7, 2002.

The Branford branch lease is for an initial term of five years, with an option to extend the lease for up to three additional terms of five years. The base rent payable for the initial term and monthly rent is $3,095 until September 30, 2007. 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.

On August 15, 2002 the Bank also purchased an additional branch facility at 1475 Whalley Avenue, New Haven, Connecticut, the site of the Amity branch location which opened March 24, 2003.

On January 14, 2004 Bancorp entered into a lease agreement to lease the facility at 15 Mason Street, New London, Connecticut, the site of the proposed Bank of Southeastern Connecticut. Pending regulatory approval of The Bank of Southeastern Connecticut, the facility will be improved to accommodate the new bank. Improvements, furnishings and equipment are estimated to be $159,000. The Bank of Southeastern Connecticut is expected to commence operations in the fourth quarter of 2004. The Lease is for an initial term of five years, with three successive five year option periods. Base rent is $45,580 annually until January 14, 2009. The base rent for the option years is subject to increases. Bancorp is responsible for pro rata allocations for taxes, utilities, common charges and other customary expenses of the premises. Upon the commencement of bank operations, it is Bancorp's intention to assign the lease to The Bank of Southeastern Connecticut.

Item 3. Legal Proceedings.

There are no legal proceedings currently pending or threatened against Bancorp or The Bank of Southern Connecticut or their property. Bancorp is not aware of any proceeding contemplated by a governmental entity involving Bancorp or the Bank.

Bancorp's wholly-owned subsidiary, The Bank of Southern Connecticut, was involved in litigation during 2003 with its former President and Chief Operating Officer, Gary D. Mullin, for breach of contract in connection with Mr. Mullin's dismissal for cause. Mr. Mullin notified the Bank of his claim in March 2003. The only parties to the dispute were the Bank and Mr. Mullin. The matter has been settled satisfactorily with no material impact to Bancorp or the Bank.

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

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

PART II

Item 5. Market for Common Equity, Related Stockholder Matters and Small Business Issuer Purchases Of Equity Securities.

Bancorp's Common Stock is quoted on the Over the Counter Market System under the symbol "SCNO."

The following table sets forth the high and low sales price* per share of Bancorp's Common Stock, as reported on the Over the Counter Market as quoted on Bloomberg Market Data System (TM) for the last two years:
(The prices listed may not reflect actual transactions.)

Quarter Ended	High	Low
March 31, 2003	$ 8.25	$ 7.80
June 30, 2003	$10.75	$ 7.70
September 30, 2003	$10.30	$ 8.65
December 31, 2003	$10.00	$ 8.65
March 31, 2002	$12.00	$ 8.50
June 30,2002	$11.00	$ 8.50
September 30, 2002	$10.00	$ 7.85
December 31, 2002	$ 9.50	$ 8.05

*Share price have not been adjusted to reflect the 10% stock dividend declared January 13, 2004.

Holders

There were approximately 100 registered shareholders of record of Bancorp's Common Stock as of March 19, 2004.

Dividends

No cash dividends have been declared to date by Bancorp. Management expects that earnings, if any, will be retained and that no cash dividends will be paid in the near future. Bancorp may, however, declare stock dividends at the discretion of its Board of Directors. Bancorp declared a 10% stock dividend on January 13, 2004 to shareholders of record as January 30, 2004. Bancorp issued 96,653 shares in connection with the stock dividend.

Bancorp's sole operating subsidiary is The Bank of Southern Connecticut. Bancorp is dependent upon the ability of the Bank to declare and pay dividends to Bancorp. The Bank's ability to declare dividends is dependent unit 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 not permit 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. However, during 2002, the Bank requested, and was granted, permission from the State of Connecticut Department of Banking, to pay a special cash dividend to Bancorp in the amount of $200,000. At December 31, 2003 and 2002, no cash dividends may be declared by the Bank without regulatory approval.

The payment of 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 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 Bancorp are authorized for issuance as of December 31, 2003:

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)	Numb remai futu equity (exclu

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Equity compensation plan approved by security holders	228,811	$ 8.48
Equity compensation plans not approved by security holders	132,481	$12.00
Total	361,292	$ 9.77

The 2001 option and warrant plans were not approved by security holders.

*Numbers and dollars have not been adjusted to reflect the 10% stock dividend declared January 13, 2004.

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1 The 2001 Option Plan was terminated on May 14,2002.

Recent Sales of Unregistered Securities

Bancorp has not sold unregistered securities.

Repurchase of Securities

Bancorp has not repurchased any of its securities.

Item 6. Management's Discussion and Analysis and Results of Operations.

Management's Discussion and Analysis of Financial Condition and Results of Operations

De Novo banks in Connecticut have reached profitability on average within three to four years after commencement of operations. The Bank of Southern Connecticut was profitable in the fourth quarter of 2003, the ninth quarter of operation.

Southern Connecticut Bancorp, Inc.
Financial Highlights

As of and for the years ended December 31, 2003 and 2002:

	2003	2002
Operating Data		

Interest income	$ 2,512,086	$ 1,125,321
Interest expense	574,795	441,813
Net interest income	1,937,291	683,508
Provision for loan losses	213,100	220,000
Noninterest income	496,332	86,163
Noninterest expenses	2,818,450	1,933,684
Net loss	(597,927)	(1,384,013)
Basic and diluted loss per share	(.56)	(1.30)

Balance Sheet Data

Cash and due from banks	$ 1,147,883	$ 1,245,010
Federal funds sold	966,000	1,144,000
Short-term investments	454,115	662,419
Investment securities	8,478,068	9,501,492
Loans, net	40,818,718	19,049,212
Total assets	56,386,040	35,500,115
Total deposits	47,273,875	24,992,931
Repurchase agreements	339,752	822,259
Total shareholders equity	7,314,302	8,274,679

Assets

Bancorp's total assets were $56.4 million as of December 31, 2003, an increase of $20.9 million over December 31, 2002. Earning assets comprise $51.2 million of the total asset volume, and consist of Federal Funds sold, short-term investments, securities and loans, a $20.6 million increase from 2002. Bancorp has maintained liquidity by maintaining balances in overnight Federal Funds and in Money Market Mutual Funds to provide funding for higher yielding loans as

they are approved. As of December 31, 2003, Federal Funds Sold balances were $966,000 and Money Market Mutual Fund balances were $454,115. Bank investment securities classified as available for sale were $8.5 million and $9.5 million as of December 31, 2003 and 2002, respectively. The loan portfolio was $41.2 million and $19.3 million as of December 31, 2003 and 2002 respectively, a net increase of $21.9 million.

The earning asset growth in 2003 has been funded by deposit growth within the Bank's market area. Deposits were $47.3 million and $25.0 million as of December 31, 2003 and 2002 respectively, a net increase of $22.3 million. The mix of deposits as of December 31, 2003 includes non-interest bearing checking accounts of $13.8 million, interest- bearing checking deposits of $3.5 million, savings deposits of $2.6 million, money market deposits of $17.3 million, as well as time certificates of deposit of $10.1 million. The deposit mix between 2003 and 2002 has not substantially changed. The Bank has not accepted any brokered deposits.

The following table presents the maturity distribution of investment securities at December 31, 2003 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	One Year Through	After Five but Within	Over	No

Available for sale	or Less	Five Years	Ten Years	Ten Years	Maturit
U. S. Government Agency obligations	$ --	$2,501,421	$4,199,527	$ 500,000	$
Mortgage-backed securities	--	--	--	--	1,576,
Total	$ --	$2,501,421	$4,199,527	$ 500,000	$1,576,
Weighted average yield		2.35%	2.77%	4.00%	3.

The following table presents a summary of investments for any issuer that exceeds 10% of shareholders' equity at December 31, 2003.

	Amortized Cost	Fair Value
U. S. Government agencies:		
Federal Home Loan Mortgage Corp.	$ 4,450,515	$ 4,317,460
Federal Home Loan Bank	2,798,665	2,713,760
Federal National Mortgage Association	1,528,646	1,446,848

Loans

The Bank's net loan portfolio was $40.8 million at December 31, 2003. Loan demand has been robust throughout the year. The loan to deposit ratio as of December 31, 2003 was 87.2%. In comparison, the loan to deposit ratio as of December 31, 2002 was 77.1%. Bancorp's target for this ratio is 80% to 83%, and attributes the year end 2003 ratio to the success of the Bank's loan business development program to small to medium businesses, as well as an improving economy, in generating loan demand. Management believes that the ratio will decline to within the targeted band and will generally remain within the band over time as the Bank's branch system deposit base grows. The deployment of new deposit growth and Federal Funds Sold, money market mutual fund investments and federal agency and other investments into the loan portfolio have produced a positive impact on net interest spread - see the table depicting the Distribution of Assets, Liabilities and Shareholders' Equity; Interest Rates and Interest Differential on Page 22 of this Form 10-KSB. There are no significant loan concentrations in the loan portfolio.

The following table presents the maturities of loans in Bancorp's portfolio at December 31, 2003 by type of loan, and the sensitivities of loans to changes in interest rates:

(Thousands of dollars)	Due in one year or less	Due after one year through five years	Due After five years	Total
Commercial loans secured				

by real estate	$ 3,699	$12,119	$ 2,226	$18,044
Residential real estate	81	867	--	948
Construction loans	773	728	--	1,501
Commercial loans	10,193	5,203	3,188	18,584
Consumer installment	671	534	--	1,205
Consumer home equity	445	588	10	1,043
Total	$15,862	$20,039	$ 5,424	$41,325
Fixed rate loans	$ 2,156	$ 4,010	$ 3,887	$10,053
Variable rate loans	13,706	16,029	1,537	31,272
Total	$15,862	$20,039	$ 5,424	$41,325

Critical Accounting Policy

In the ordinary course of business, Bancorp 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 principals generally accepted in the United States of America. Actual results could differ significantly from those estimates under different assumptions and conditions. Bancorp believes the following discussion addresses Bancorp's only critical accounting policy, which is the policy that is most important to the portrayal of Bancorp'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.

Allowance for Loan Losses

The allowance for loan losses, a material estimate susceptible to significant change in the near-term, is established as losses are estimated to have occurred through a provision for losses charged against operations, and is maintained at a level that management considers adequate to absorb losses in the loan portfolio. Management's judgment in determining the adequacy of the allowance is inherently subjective and is based on the evaluation of individual loans, pools of homogeneous loans, the known and inherent risk characteristics and size of the loan portfolios, the assessment of current economic and real estate market conditions, estimates of the current value of underlying collateral, past loan loss experience, review of regulatory authority examination reports and evaluations of specific loans and other relevant factors. Loans, including impaired loans, are charged against the allowance for loan losses when management believes that the uncollectibility of principal is confirmed. Any subsequent recoveries are credited to the allowance for loan losses when received. In connection with the determination of the allowance for loan losses, management obtains appraisals for significant properties, when considered necessary.

The reserve consists of specific, general and unallocated components. The specific component relates to loans that are classified doubtful, substandard or special mention. For such loans that are also classified as impaired, an

allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan. The general component covers non-classified loans and is based on historical loss experience adjusted for qualitative factors. An unallocated component may be maintained to cover uncertainties that could affect management's estimate of probably losses.The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general losses in the portfolio.

Based upon this evaluation, management believes the allowance for loan losses of $421,144 or 1.02% of gross loans at December 31, 2003 is adequate, under prevailing economic conditions, to absorb losses on existing 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. Bancorp considers consumer installment loans to be pools of smaller balance homogeneous loans, which are collectively evaluated for impairment.

Analysis of Allowance for Loan Losses

	2003	2002
Balance at beginning of period	$ 232,000	$ 12,000
Charge-offs	(24,572)	--
Recoveries	616	--
Net (charge-offs) recoveries	(23,956)	--
Additions charged to operations	213,100	220,000
Balance at end of period	$ 421,144	$ 232,000
Net charge-offs to average loans	0.08%	--

Allocation of the Allowance for Loan Losses at December 31:

	2003		2002	
	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	$165,986	43.66%	$ 88,083	45.56%

Construction loans	35,589	3.63%	8,538	2.94%
Residential	4,833	2.29%	3,828	7.92%
Commercial	192,075	44.98%	74,041	38.29%
Consumer Installment	21,361	2.92%	3,550	3.67%
Consumer Home Equity	1,300	2.52%	785	1.62%
Unallocated	--	--	53,175	--
	$421,144	100.00%	$232,000	100.0%

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Non-Accrual, Past Due and Restructured Loans

Non-accrual loans at December 31, 2003 totaled $94,063. There were no restructured loans. There were no loans in 2003 considered as "troubled debt restructurings."

Potential Problem Loans

Other than loans identified as non-accrual at December 31, 2003, the Bank had no 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 $47.3 million at December 31, 2003, an increase of $22.3 million in comparison to total deposits as of December 31, 2002 of $25.0 million. The deposit total at December 31, 2003 consists of non-interest bearing checking of $13.8 million (29.1%), interest bearing checking and money market deposits of $20.8 million (43.9%), savings of $2.6 million (5.6%) and certificates of deposit of $10.1 million (21.4%). The Bank has not accepted any brokered deposits and has no present plans to review this policy.

The Bank continues to offer competitive interest rates in the very competitive New Haven County marketplace in order to fund expected loan growth.

As of December 31, 2003 the Bank's maturities of time deposits were:

(Thousands of dollars)	$100,000 or greater	Less than $100,000	Totals
Three months or less	$ 2,056	$ 796	$ 2,852
Over three months to one year	4,491	866	5,357
Over one year	505	1,395	1,900
	$ 7,052	$ 3,057	$10,109

Other

The increase in premises and equipment is primarily due to the improvements made to the building and related site used for the Amity branch of the Bank.

In September, 2002, the Bank began offering securities sold under agreements to repurchase, which are classified as secured borrowings, and generally mature within one to three days from the transaction date. Securities sold under agreements to repurchase are recorded at the amount of cash received in connection with the transaction. The Bank may be required to provide additional collateral based on the changes in fair value of the underlying securities.

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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, 2003 and 2002.

Distribution of Assets, Liabilities and Shareholders' Equity; Interest Rates and Interest Differential

	2003			2002	
(Dollars in thousands)	Average Balance	Interest Income/ Expense	Average Rate	Average Balance	Interest Income/ Expense
Interest earning assets					
Loans (1)	$ 29,091	$ 2,224	7.64%	$ 9,095	$ 744
Short term investments	993	7	0.70%	3,642	59
Investments	8,747	256	2.93%	7,649	263
Federal funds sold	2,379	25	1.05%	3,692	59
Total interest earning assets	41,210	2,512	6.10%	24,078	1,125
Cash and due from banks	1,396			902	
Premises and equipment, net	3,381			1,915	
Allowance for loan losses	(303)			(70)	
Other	1,068			756	
Total assets	$ 46,752			$ 27,581	
Interest bearing liabilities					
Time certificates	$ 6,534	166	2.54%	$ 5,106	156
Savings deposits	1,984	21	1.06%	625	10
Money market / checking deposits	18,381	211	1.15%	7,514	135
Capital lease obligations	1,191	169	14.19%	936	137
Repurchase agreements and other	914	8	0.88%	388	4
Total interest bearing liabilities	29,004	575	1.98%	14,569	442
Non-interest bearing deposits	9,645			3,686	
Accrued expenses and other liabilities	357			210	
Shareholder's equity	7,746			9,116	

Total liabilities and equity	$ 46,752			$ 27,581	
Net interest income		$ 1,937			$ 683
Interest margin			4.70%		
Interest spread			4.12%		

(1) Includes nonaccruing loans.

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RATE VOLUME VARIANCE ANALYSIS

The following table summarizes the variance in interest income and expense for 2003 and 2002 resulting from changes in assets and liabilities and fluctuations in interest rates earned and paid. The change in interest attributable to both rate and volume have been allocated to both rate and volume on a pro rata basis.

(Dollars in thousands)	2003 vs. 2002 Variance due to: Volume	Rate	Total
Interest Earning Assets			
Loans	$ 1,532	($ 52)	$ 1,480
Short Term Investments	(29)	(23)	(52)
Investments	35	(42)	(7)
Federal Funds Sold	(17)	(17)	(34)
	1,521	(134)	1,387
Interest bearing liabilities			
Time certificates	$ 39	(29)	$ 10
Savings deposits	15	(4)	11
Money market / checking deposits	139	(63)	76
Capital lease obligations	37	(5)	32
Repurchase agreements	5	(1)	4
	235	(102)	133
Net Interest Income	$ 1,286	($ 32)	$ 1,254

The improvements realized in net interest income during 2003 primarily reflect substantial increased earning asset volume over 2002, as the average earning assets in 2003 of $41.2 million were 71% greater than average earning assets in 2002. Overall, interest income attributed to volume considerations considerably outweighed rate considerations (increase of $1,521,000 verses a decrease of $134,000). With respect to variances in the 2003 cost of interest bearing liabilities in comparison to 2002, increased volume considerations of $235,000 also outweighed decreased rate considerations of $102,000.

Loan growth has been the primary factor in improving net interest income, as the net portfolio growth of $21.8 million in 2003 was accompanied by a $1.3 million increase in net interest income. Bancorp intends for the Bank to continue to emphasize lending to small to medium businesses in its market area as its strategy to increase assets under management and to improve earnings. The Bank will seek opportunities to increase its deposit base in order to support its earning assets through marketing and by considering additional branch locations and new product and service offerings.

The following are measurements of Bancorp's earnings (loss) in relation to assets and equity, and average equity to average assets for the year ended December 31, 2003 and 2002.

	2003	2002
Return on average assets	(1.28)%	(5.02)%
Return on average equity	(7.72)%	(15.18)%
Average equity to average assets	16.56 %	33.05 %

Results of Operations

Bancorp's net loss for fiscal year 2003 was $598,000, a decrease of $786,000 from the net loss of $1,384,000 in fiscal year 2002. The decrease in the 2003 loss was primarily due to increases in net interest income and non-interest income, partly offset by an increase in non-interest expenses.

Net Interest Income

For the year December 30, 2003, net interest income was $1,937,000 versus $684,000 for the year ended December 31, 2002, a $1.3 million or 183% increase. The 2003 increase was primarily the result of a $17.1 million increase in average earning assets. The increase in average earning assets was comprised of increases in average loans of $20.0 million and investments of $1.1 million, partially offset by a decrease in lower yielding short term investments of $2.6 million and federal funds sold of $1.3 million.

The yield on average interest earning assets for the twelve months ended December 31, 2003 was 6.10% versus 4.67% for same period in 2002, an increase of 143 basis points. The increase in the yield on assets reflects the increased ratio of loans to the total of earning assets over 2002.

The cost of average interest bearing liabilities was 1.98% for the twelve months ended December 31, 2003 versus 3.03% for the same period in 2002, a favorable decrease of 105 basis points. The decrease in the cost of interest bearing liabilities was due to the $10.9 million increase in the average outstanding balances of low rate money market and interest bearing checking deposits in comparison to the total increase in interest bearing liabilities of $14.4 million, as well as the generally lower interest rate environment prevalent in 2003.

Due to the improvements in 2003 in the yield on average earning assets, and the favorable decrease in the cost of interest bearing liabilities, the interest spread improved to 4.12% for fiscal year 2003, an increase of 248 basis points over the interest spread realized in 2002. Net interest margin improved to 4.70% in 2003 from the 2.84% in 2002, a favorable change of 186 basis points.

Noninterest Income

The $410,000 increase in non-interest income for the twelve months ended December 31, 2003 versus 2002 is the result of $177,000 referral fee income and gains on sales of loan participations related to Small Business Administration ("SBA") guaranteed loans in the fourth quarter of 2003, increased deposit account service charges and fees of $42,000, other noninterest fee income of $147,000 and $44,000 of gains on the sales of investment securities for the year. The Bank of Southern Connecticut intends to originate SBA guaranteed loans in the future and expects to continue to earn fee income from SBA loan participation sales and referrals. The increase in other noninterest fee income is attributable to volume growth in the loan and deposit portfolios, as well as the receipt of an approximately $32,000 prepayment penalty on a loan.

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Noninterest Expenses

Total noninterest expenses were $2.8 million for the year ended December 31, 2003 versus $1.9 million for 2002, an increase of $900,000 or 47%. The increase in expenses is due to the growth in Bancorp's loan and deposit volume as well as the addition of the Amity office in March of 2003, requiring additional staffing and other operating expenses. As a result, salaries and benefits increased $548,000 to $1.5 million in fiscal year 2003 in comparison to fiscal year 2002, and occupancy and equipment expenses increased by $184,000 in fiscal year 2003 to $370,000.

Professional services decreased for the year ended December 31, 2003 versus the year ended December 31, 2002 by $61,000. The decrease is primarily the result of hiring Michael M. Ciaburri as President and Chief Operating Officer of the Bank as of February 12, 2003, who had worked up to that point as a consultant to the bank developing new loan and deposit account volume.

Off-Balance-Sheet Arrangements

See Note 12 to the accompanying consolidated Financial Statements for required disclosure regarding off-balance-sheet arrangements.

Liquidity

Bancorp's liquidity position as of December 31, 2003 and December 31, 2002 consisted of liquid assets totaling $11.1 million and $12.6 million, respectively. This represents 19.6% and 35.5% of total assets at December 31, 2003 and 2002, respectively. The liquidity ratio is defined as the percentage of liquid assets to total assets. The following categories of assets as described in the accompanying balance sheet are considered liquid assets: Cash and due from banks, federal funds sold, short-term investments and securities available for sale. Liquidity is a measure of Bancorp's ability to generate adequate cash to meet financial obligations. The principal cash requirements of a financial institution are to cover downward fluctuations in deposits and increases in its loan portfolio.

Management believes Bancorp's short-term assets have sufficient liquidity to cover potential fluctuations in deposit accounts and loan demand and to meet other anticipated operating cash requirements.

Capital

The following table illustrates the Bank's regulatory capital ratios at December 31:

	2003	2002
Leverage Capital	14.16%	23.76 %
Tier 1 Risk - Based Capital	16.33%	31.52 %
Total Risk - Based Capital	17.24%	32.43 %

Capital adequacy is one of the most important factors used to determine the safety and soundness of individual banks and the banking system. Based on the above ratios, the Bank is considered to be "well capitalized" under applicable regulations. To be considered "well capitalized" an institution must generally have a leverage capital ratio of at least 5%, a Tier 1 risk-based capital ratio of at least 6% and a total risk-based capital ratio of at least 10%.

Bancorp's actual and required ratios are not substantially different from those shown above.

Subject to regulatory approval and completion of a public offering of additional common shares during 2004, Bancorp has intentions to establish The Bank of Southeastern Connecticut in the fourth quarter of 2004. Bancorp also anticipates commencing the operations of SCB Capital, Inc. in the second half of 2004. Provided both regulatory approval of the new bank subsidiary and the success of the public offering, Bancorp will capitalize both of these entities in 2004. The application for the Bank of Southeastern Connecticut specifies that

the initial capitalization of The Bank of Southeastern Connecticut will be approximately $6 million. The National Association of Security Dealers rules and regulations require a minimum capitalization for SCB Capital, Inc. to be not less than $25,000.

Market Risk

Market risk is defined as the sensitivity of income to fluctuations in interest rates, foreign exchange rates, equity prices, commodity prices and other market-driven rates or prices. Based upon on the nature of the Company's business, market risk is primarily limited to interest rate risk, which is the impact that changing interest rates have on current and future earnings.

Bancorp's goal is to maximize long-term profitability, while minimizing its exposure to interest rate fluctuations. The first priority is to structure and price Bancorp's assets and liabilities to maintain an acceptable interest rate spread, while reducing the net effect of changes in interest rates. In order to reach an acceptable interest rate spread, Bancorp must generate loans and seek acceptable long-term investments to replace the lower yielding balances in Federal Funds sold and short-term investments. The focus also must be on maintaining a proper balance between the timing and volume of assets and liabilities re-pricing within the balance sheet. One method of achieving this balance is to originate variable loans for the portfolio to offset the short-term re-pricing of the liabilities. In fact, a number of the interest bearing deposit products have no contractual maturity. Customers may withdraw funds from their accounts at any time and deposits balances may therefore run off unexpectedly due to changing market conditions.

The exposure to interest rate risk is monitored by the Asset and Liability Management Committee ("ALCO") consisting of senior management personnel and selected members of the Board of Directors. ALCO reviews the interrelationships within the balance sheet to maximize net interest income within acceptable levels of risk. ALCO reports to the Board of Directors on a quarterly basis regarding the status of ALCO activities within the Company.

Impact of Inflation and Changing Prices

Bancorp's financial statements have been prepared in terms of historical dollars, without considering changes in relative purchasing power of money over time due to inflation. Unlike most industrial companies, virtually all of the assets and liabilities of a financial institution are monetary in nature. As a result, interest rates have a more significant impact on a financial institution's performance than the effect of general levels of inflation. Interest rates do not necessarily move in the same direction or in the same magnitude as the prices of goods and services. Notwithstanding this fact, inflation can directly affect the value of loan collateral, in particular, real estate. Inflation, or disinflation, could significantly affect Bancorp's earnings in future periods.

"Safe Harbor" Statement Under Private Securities Litigation Reform Act of 1995.

Certain statements contained in Bancorp's public reports, including this report, and in particular in this "Management's Discussion and Analysis or Plan of Operation", may be forward looking and subject to a variety of risks and uncertainties. These factors include, but are not limited to, (1) changes in prevailing interest rates which would affect the interest earned on Bancorp's interest earning assets and the interest paid on its bearing liabilities, (2) the timing of re-pricing of Bancorp's interest earning assets and interest bearing liabilities, (3) the effect of changes in governmental monetary policy, (4) the effect of changes in regulations applicable to Bancorp and the conduct of its business, (5) changes in competition among financial service companies, including possible further encroachment of non-banks on services traditionally provided by banks and the impact of recently enacted federal legislation, (6) the ability of competitors which are larger than Bancorp to provide products and services which it is impracticable for Bancorp to provide, (7) the effect of Bancorp's opening of branches, (8) the effect of any decision by Bancorp to engage in any business not historically permitted to it. Other such factors may be described in Bancorp's filings with the SEC.

Although Bancorp believes that it offers the loan and deposit products and has the resources needed for success, future revenues and interest spreads and yields cannot be reliably predicted. These trends may cause Bancorp to adjust its operations in the future. Because of the foregoing and other factors, recent trends should not be considered reliable indicators of future financial results or stock prices.

Item 7. Financial Statements

The consolidated balance sheets of Bancorp as of December 31, 2003 and 2002, and the related consolidated statements of operations, shareholders' equity and cash flows for the years then ended, together with the report thereon of McGladrey & Pullen, LLP dated March 5, 2004 are included as part of this Form 10-KSB in the "Financial Report" following page 33 hereof.

Item 8. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

Not applicable.

Item 8a. Controls and Procedures

(a) Evaluation of disclosure controls and procedures

Based upon an evaluation of the effectiveness of Bancorp's disclosure controls and procedures performed by Bancorp's management, with participation of Bancorp's Chief Executive Officer and its Chief Financial Officer as of the end of the period covered by this report, Bancorp's Chief Executive Officer and Chief Financial Officer concluded that Bancorp's disclosure controls have been effective.

As used herein, "disclosure controls and procedures" mean controls and other procedures of Bancorp that are designed to ensure that information required to be disclosed by Bancorp in the reports that it files or submits under the Securities Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the Commissions rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by Bancorp in the reports that it files or submits under the Securities Exchange Act is accumulated and communicated to Bancorp's management, including its principal executive, and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

(b) Changes in Internal Controls

There have not been any significant changes in Bancorp's internal controls or in other factors that occurred during Bancorp's fiscal year ended December 31, 2003 that could significantly affect these controls subsequent to the evaluation referenced in paragraph (a) above.

PART III

Item 9. Directors and Executive Officers of the Registrant

The information required by this Item 9 is incorporated into this Form 10-KSB by reference to Bancorp's definitive proxy statement for its 2004 Annual Meeting of Shareholders (the "Definitive Proxy Statement").

Item 10. Executive Compensation

The information required by this Item 10 is incorporated into this Form 10-KSB by reference to the Definitive Proxy Statement.

Item 11. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

The information required by this Item 11 is incorporated into this Form 10-KSB by reference to the Definitive Proxy Statement.

Item 12. Certain Relationships and Related Transactions

The information required by this Item 12 is incorporated into this Form 10-KSB by reference to the Definitive Proxy Statement.

Item 13. Exhibits, List and Reports on Form 8-K

(a) Exhibits

No.	Description
3(i)	Amended and Restated Certificate of Incorporation of the Issuer (incorporated by reference to Exhibit 3(i) to Issuer's Quarterly Report on Form 10-QSB dated June 30, 2002)
3(ii)	By-Laws of the Issuer (incorporated by reference to Exhibit 3(ii) to the Issuer's Registration Statement on Form SB-2 (No. 333-59824))
10.1	Lease, dated as of August 17, 2000, between 215 Church Street, LLC and the Issuer (incorporated by reference to Exhibit 10.1 to the Issuer's Registration Statement on Form SB-2 (No. 333-59824))
10.2	Letter agreement dated January 3, 2001 amending the Lease between 215 Church Street, LLC and the Issuer (incorporated by reference to Exhibit 10.2 to the Issuer's Registration Statement on Form SB-2 (No. 333-59824))
10.3	First Amendment to Lease dated March 30, 2001 between 215 Church Street, LLC and the Issuer (incorporated by reference to Exhibit 10.3 to the Issuer's Registration Statement on Form SB-2 (No. 333-59824))
10.4	Second Amendment to Lease dated March 31, 2001 between 215 Church Street, LLC and the Issuer (incorporated by reference to Exhibit 10.4 to the Issuer's Registration Statement Form SB-2 (No. 333-59824))
10.5	Assignment of Lease dated April 11, 2001 between the Issuer and The Bank of Southern Connecticut (incorporated by reference to Exhibit 10.5 to the Issuer's Registration Statement on Form SB-2 (No. 333-59824))
10.6	Employment Agreement dated as of January 23, 2001, between The Bank of Southern Connecticut, the Issuer and Joseph V. Ciaburri (incorporated by reference to Exhibit 10.6 to the Issuer's Registration Statement on Form SB-2 (No. 333-59824))
10.7	Employment Agreement dated as of March 29, 2001 between The Bank of Southern Connecticut, and Gary D. Mullin (incorporated by reference to Exhibit 10.7 to the Issuer's Registration Statement on Form SB-2 (No. 333-59824))
10.8	Issuer's 2001 Stock Option Plan (incorporated by reference to Exhibit 10.8 to the Issuer's Registration Statement on Form SB-2 (No. 333-59824))

10.9	Issuer's 2001 Warrant Plan (incorporated by reference to Exhibit 10.9 to the Issuer's Registration Statement on Form SB-2 (No. 333-59824))

10.10	Sublease dated January 1, 2001 between Michael Ciaburri, d/b/a Ciaburri Bank Strategies and The Bank of Southern Connecticut (incorporated by reference to Exhibit 10.10 to the Issuer's Registration Statement on Form SB-2 (No. 333-59824))
10.11	Sublease dated January 1, 2001 between Laydon and Company, LLC and The Bank of Southern Connecticut (incorporated by reference to Exhibit 10.11 to the Issuer's Registration Statement on Form SB-2 (No. 333-59824))
10.12	Issuer's 2001 Supplemental Warrant Plan (incorporated by reference to Exhibit 10.12 to Issuer's Annual Report on Form 10-KSB dated March 29, 2002)
10.13	Issuer's 2002 Stock Option Plan (incorporated by reference to Appendix B to Issuer's Definitive Proxy Statement dated April 18, 2002).
10.14	Employment Agreement dated as of February 12, 2003, between The Bank of Southern Connecticut and Michael M. Ciaburri. (incorporated by reference to Exhibit 10.14 to Issuer's Form 10-QSB dated May 14, 2003).
10.15	Amendment to Employment Agreement dated as of October 20, 2003, between The Bank of Southern Connecticut and Southern Connecticut Bancorp, Inc. and Joseph V. Ciaburri. (incorporated by reference to Exhibit 10.15 to issuer's Form 10-QSB dated November 12, 2003)
10.16	Lease dated January 14, 2004 between The City of New London and the Issuer (attached hereto)
10.17	Lease dated August 2, 2002, between 469 West Main Street LLC and The Bank of Southern Connecticut (attached hereto)
14.	Code of Ethics (attached hereto)
21.	Subsidiaries (incorporated by reference to Exhibit 21 to Issuer's form 10-KSB dated March 31, 2003)
31.1	Section Rule 13(a)-14(a)/15(d)-14(a) Certification by Chairman and Chief Executive Officer.
31.2	Section Rule 13(a)-14(a)/15(d)-14(a) Certification by President and Chief Operating Officer.
31.3	Section Rule 13(a)-14(a)/15(d)-14(a) Certification by Vice President and Chief Financial Officer.
32.1	Section 1350 Certification by Chairman and Chief Executive Officer.
32.2	Section 1350 Certification by President and Chief Operating Officer.
32.3	Section 1350 Certification by Vice President and Chief Financial Officer.

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Item 14. Principal Accountant Fees and Services

Bancorp's Principal Accountants, McGladrey & Pullen, LLP provide audit, audit related and tax advisory and tax return preparation services for Bancorp and The Bank of Southern Connecticut. The following table summaries the fees provided in 2003 and 2002 respectively:

	2003	2002
Audit Fees	$81,583	$74,344
Audit Related Fees	$ 6,235	$ 9,600
Tax Fees	$ 7,565	$ 7,065
All Other Fees	NONE	NONE

Audit fees consist of fees for professional services rendered for the audit of the consolidated financial statements, review of financial statements included in quarterly reports included on Form 10-QSB, and services connected with statutory and regulatory filings or engagements. Audit related fees are principally for consultations on various accounting and reporting matters. Tax service fees consist of fees for tax return preparation for Bancorp.

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SIGNATURES

In accordance with Section 13 or 15 (d) of the Exchange Act, the registrant has caused this report to be signed on its behalf by the undersigned, thereunto duly

SOUTHERN CONNECTICUT BANCORP, INC.
(Registrant)

By: /S/ Joseph V. Ciaburri

Name: Joseph V. Ciaburri
Title: Chairman and Chief Executive Officer

Date: March 30, 2004

In accordance with the Exchange Act, this report has been signed below by the following persons on behalf of the registrant and in capacities and on the dates indicated.

/S/ Joseph V. Ciaburri	March 30, 2004
Joseph V. Ciaburri Chief Executive Officer and Director	Date
/S/ Elmer F. Laydon	March 30, 2004
Elmer F. Laydon Vice Chairman and Director	Date
/S/ Juan Jose Alvarez de Lugo	March 30, 2004
Juan Jose Alvarez de Lugo Director	Date
/S/ G. Leon Jacobs	March 30, 2004

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G. Leon Jacobs Date
Director

/S/ Joshua H. Sandman March 30 2004
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Joshua H. Sandman Date
Director

/S/ Alphonse F. Spadaro, Jr. March 30, 2004
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Alphonse F. Spadaro, Jr. Date
Director

/S/ Carl R. Borrelli March 30, 2004
------------------------------------ ------------------
Carl R. Borrelli Date
Director

/S/ William F. Weaver March 30, 2004
------------------------------------ ------------------
William F. Weaver Date
Chief Financial Officer

Exhibit Index

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SOUTHERN CONNECTICUT BANCORP, INC. AND SUBSIDIARY

FINANCIAL REPORT
December 31, 2003 and 2002

CONTENTS

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Southern Connecticut Bancorp, Inc. and Subsidiary
New Haven, Connecticut

We have audited the accompanying consolidated balance sheets of Southern Connecticut Bancorp, Inc. and Subsidiary (the "Company") as of December 31, 2003 and 2002, and the related consolidated statements of operations, shareholders' equity and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Southern Connecticut Bancorp, Inc. and Subsidiary as of December 31, 2003 and 2002, and the results of their operations and their cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

/s/ McGladrey & Pullen, LLP

New Haven, Connecticut
March 5, 2004

SOUTHERN CONNECTICUT BANCORP, INC. AND SUBSIDIARY

CONSOLIDATED BALANCE SHEETS
December 31, 2003 and 2002

	2003
ASSETS	
Cash and due from banks (Note 2)	$ 1,147,88
Federal funds sold	966,00
Short-term investments (Note 2)	454,11
Cash and cash equivalents	2,567,99
Available for sale securities (at fair value) (Note 3)	8,478,06
Federal Home Loan Bank stock (Note 7)	21,50
Loans receivable (net of allowance for loan losses: 2003 $421,144; 2002 $232,000) (Note 4)	40,818,71
Accrued interest receivable	196,54
Premises and equipment, net (Note 5)	3,459,91
Other assets	843,29

Total assets	$ 56,386,04
LIABILITIES AND SHAREHOLDERS' EQUITY	
Liabilities	
Deposits (Note 6)	
Noninterest bearing deposits	$ 13,781,28
Interest bearing deposits	33,492,58
Total deposits	47,273,87
Repurchase agreements	339,75
Accrued expenses and other liabilities	267,23
Capital lease obligations (Note 8)	1,190,87
Deferred tax liability (Note 9)	
Total liabilities	49,071,73
Commitments and Contingencies (Notes 7, 8, 11, 12, 13, 16 and 17)	
Shareholders' Equity (Notes 10 and 13)	
Preferred stock, no par value; 500,000 shares authorized; none issued	
Common stock, par value $.01; shares authorized: 5,000,000; shares issued and outstanding: 2003 1,063,320; 2002 966,667	10,63
Additional paid-in capital	10,704,26
Accumulated deficit	(3,100,84
Accumulated other comprehensive income (loss) - net unrealized (loss) gain on available for sale securities	(299,75
Total shareholders' equity	7,314,30
Total liabilities and shareholders' equity	$ 56,386,04

See Notes to Consolidated Financial Statements.

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SOUTHERN CONNECTICUT BANCORP, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF OPERATIONS
For the Years Ended December 31, 2003 and 2002

2003

Interest Income:	
Interest and fees on loans	$ 2,224,5
Interest on securities	255,5
Interest on Federal funds sold and short-term investments	31,9
Total interest income	2,512,0
Interest Expense:	
Interest expense on deposits (Note 6)	397,9
Interest expense on capital lease obligations	168,7
Interest expense on repurchase agreements and other borrowings	8,0
Total interest expense	574,7
Net interest income	1,937,2
Provision for Loan Losses (Note 4)	213,1
Net interest income after provision for loan losses	1,724,1
Noninterest Income:	
Service charges and fees	128,2
Gains and fees from sales and referrals of SBA loans	177,0
Gains on sales of available for sale securities (Note 3)	44,5
Other noninterest income	146,5
Total noninterest income	496,3
Noninterest Expenses:	
Salaries and benefits (Note 7)	1,462,0
Occupancy and equipment expense	369,7
Professional services	307,4
Data processing and other outside services	196,8
Advertising and promotional expenses	94,6
Forms, printing and supplies	59,8
Other operating expenses	327,8
Total noninterest expenses	2,818,4
Net loss	$ (597,9
Basic and Diluted Loss per Share	$ (0.
Dividends per Share	$

See Notes to Consolidated Financial Statements.

SOUTHERN CONNECTICUT BANCORP, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY For the Years Ended December 31, 2003 and 2002

	Number of Shares	Common Stock	Additional Paid-In Capital	Accumulated Deficit
Balance, December 31, 2001	966,667	$ 9,667	$ 10,705,382	$ (1,118,902
Comprehensive income:				
Net loss	-	-	-	(1,384,013
Unrealized holding gain on available for sale securities (Note 15)	-	-	-	-
Total comprehensive loss				
Balance, December 31, 2002	966,667	9,667	10,705,382	(2,502,915
Comprehensive income (loss):				
Net loss	-	-	-	(597,927
Unrealized holding loss on available for sale securities (Note 15)	-	-	-	-
Total comprehensive loss				
10% stock dividend declared January 13, 2004 - 96,653 shares	96,653	966	(966)	-
Fractional shares to be paid in cash	-	-	(147)	-
Balance, December 31, 2003	1,063,320	$10,633	$ 10,704,269	$ (3,100,842

See Notes to Consolidated Financial Statements.

SOUTHERN CONNECTICUT BANCORP, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS
For the Years Ended December 31, 2003 and 2002

	2003
Cash Flows From Operations	
Net loss	$ (597,927)
Adjustments to reconcile net loss to net cash used in operating activities:	
Amortization and accretion of premiums and discounts on investments, net	34,071
Provision for loan losses	213,100
Gains on sales of available for sale securities	(44,505)
Gains on sales of SBA loans	(122,269)
Depreciation and amortization	219,853
Increase in cash surrender value of life insurance	(38,344)
Changes in assets and liabilities:	
Increase in deferred loan fees	29,219
Increase in accrued interest receivable	(8,873)
(Increase) decrease in other assets	(148,063)
Increase (decrease) in accrued expenses and other liabilities	88,596
Net cash used in operating activities	(375,142)
Cash Flows From Investing Activities	
Purchases of available for sale securities	(10,949,683)
Principal repayments on available for sale securities	1,038,338
Proceeds from maturities of available for sale securities	6,185,000
Proceeds from sales of available for sale securities	4,357,995
Purchases of held to maturity securities	-
Maturities of held to maturity securities	-
Purchase of FHLB stock	(21,000)
Proceeds from sales of SBA loans	1,295,122
Net increase in loans receivable	(23,184,678)
Purchase of life insurance policy	-
Purchases of premises and equipment	(626,847)
Net cash used in investing activities	(21,905,753)
Cash Flows From Financing Activities	
Net increase in demand, savings and money market deposits	18,523,708
Net increase in time certificates of deposit	3,757,236
Net (decrease) increase in repurchase agreements	(482,507)
Principal repayments on capital lease obligations	(973)
Net cash provided by financing activities	21,797,464
Net decrease in cash and cash equivalents	(483,431)
Cash and cash equivalents	
Beginning	3,051,429

Ending	$ 2,567,998

SOUTHERN CONNECTICUT BANCORP, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS, Continued
For the Years Ended December 31, 2003 and 2002

	2003
Supplemental Disclosures of Cash Flow Information:	
Cash paid for:	
Interest	$ 551,398
Income taxes	$ -
Supplemental Disclosures of Non-Cash Investing and Financing Activities:	
Transfer of held to maturity securities to available for sale securities (Note 3)	$ -
Unrealized holding (losses) gains on available for sale securities arising during the period	$ (402,208)
Fractional stock dividend shares payable in cash	$ 147
Capital lease incurred for acquisition of building	$ -

See Notes to Consolidated Financial Statements.

SOUTHERN CONNECTICUT BANCORP, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2003 and 2002

Note 1. Nature of Operations and Summary of Significant Accounting Policies

Southern Connecticut Bancorp, Inc. (the "Company"), a Connecticut corporation, is a bank holding company incorporated on November 8, 2000 and is the sole shareholder of the Bank of Southern Connecticut (the "Bank"). The Bank provides a full range of banking services to commercial and consumer customers, primarily concentrated in the New Haven County area of Connecticut, through its main office in New Haven, Connecticut and two branch offices in New Haven and Branford, Connecticut. In 2003, SCB Capital, Inc. was formed as a Connecticut corporation, and in 2004, the Company plans to capitalize SCB Capital, Inc., which will become a subsidiary of the Company. SCB Capital, Inc. will engage in a limited range of investment banking, advisory and brokerage services, primarily with small and medium size business clients.

Principles of consolidation and basis of financial statement presentation

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary, the Bank, and have been prepared in accordance with accounting principles generally accepted in the United States of America and general practices within the banking industry. All significant intercompany balances and transactions have been eliminated. In preparing the consolidated financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosures of contingent assets and liabilities as of the date of the balance sheet and the reported amounts of income and expenses for the reporting period. Actual results could differ from those estimates.

Significant group concentrations of credit risk

Most of the Company's activities are with customers located within the New Haven County region of Connecticut. Note 3 discusses the types of securities that the Company invests in and Note 4 discusses the types of lending that the Company engages in. The Company does not have any significant concentrations in any one industry or customer.

The following is a summary of the Company's significant accounting policies.

Cash and cash equivalents and statement of cash flows

Cash and due from banks, Federal funds sold, and short-term investments are recognized as cash equivalents in the statements of cash flows. Federal funds sold generally mature in one day. For purposes of reporting cash flows, the Company considers all highly liquid debt instruments purchased with an original maturity of three months or less to be cash equivalents. Cash flows from deposits are reported net. The Company maintains amounts due from banks and Federal funds sold which, at times, may exceed Federally insured limits. The Company has not experienced any losses from such concentrations.

Investments in debt and marketable equity securities

Management determines the appropriate classification of securities at the date individual investment securities are acquired, and the appropriateness of such classification is reassessed at each balance sheet date.

Debt securities that management has the positive intent and ability to hold to maturity are classified as "held to maturity" and recorded at amortized cost. "Trading" securities, if any, are carried at fair value with unrealized gains and losses recognized in earnings. Securities not classified as held to maturity or trading, including equity securities with readily determinable fair values, are classified as "available for sale" and recorded at fair value, with unrealized gains and losses excluded from earnings and reported in other comprehensive income, net of taxes.

Purchase premiums and discounts are recognized in interest income using the interest method over the terms of the securities. Declines in the fair value of held to maturity and available for sale securities below their cost that are deemed to be other than temporary are reflected in earnings as realized losses. In estimating other-than-temporary impairment losses, management considers (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, and (3) the intent and ability of the Company to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value. Gains and losses on the sale of securities are recorded on the trade date and are determined using the specific identification method.

The sale of a held to maturity security within three months of its maturity date or after collection of at least 85% of the principal outstanding at the time the security was acquired is considered a maturity for purposes of classification and disclosure.

Transfers of financial assets

Transfers of financial assets are accounted for as sales when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the Company, (2) the transferee obtains the right to pledge or exchange the transferred assets and no condition both constrains the transferee from taking advantage of that right and provides more than a trivial benefit for the transferor, and (3) the transferor does not maintain effective control over the transferred assets through either (a) an agreement that both entitles and obligates the transferor to repurchase or redeem the assets before maturity or (b) the ability to unilaterally cause the holder to return specific assets, other than through a cleanup call.

Servicing

Servicing assets are recognized as separate assets when rights are acquired through purchase or through sale of financial assets. Generally, purchased servicing rights are capitalized at the cost to acquire the rights. For sales of loans, a portion of the original cost of the loan is allocated to the servicing right, and if the pass-through rate to the investor is less than the note rate, to an interest-only strip, based on relative fair value. Fair value is based on a valuation model that calculates the present value of estimated future net servicing and interest income. The valuation model incorporates assumptions that market participants would use in estimating future net servicing and interest income, such as the cost to service, the discount rate, the custodial earnings rate, an inflation rate, ancillary income, prepayment speeds and default rates and losses. Capitalized servicing rights are reported in other assets and are amortized into non-interest income in proportion to, and over the period of, the estimated future net servicing income of the underlying financial assets. Interest only strips are also reported in other assets and are amortized into interest income under the same method as servicing assets.

Servicing assets and interest-only strips are evaluated for impairment based upon the fair value of the assets as compared to amortized cost. Impairment is determined by stratifying the assets into tranches based on predominant risk characteristics, such as interest rate, loan type and investor type. Impairment is recognized through a valuation allowance for an individual tranche, to the extent that fair value is less than the capitalized amount for the tranche. If the Company later determines that all or a portion of the impairment no longer exists for a particular tranche, a reduction of the allowance may be recorded as an increase to income.

Servicing fee income is recorded for fees earned for servicing loans. The fees are based on a contractual percentage of the outstanding principal; or a fixed amount per loan and are recorded as income when earned. The amortization of mortgage servicing rights is netted against loan servicing fee income, and the amortization of interest-only strips is netted against interest income.

Loans receivable

Loans receivable are stated at their current unpaid principal balances, net of the allowance for loan losses and net deferred loan origination fees and costs. The Company has the ability and intent to hold its loans receivable for the foreseeable future or until maturity or payoff.

Impaired loans, if any, are measured based on the present value of expected future cash flows discounted at the loan's effective interest rate or, as a practical expedient, at the loan's observable market price or the fair value of the collateral, if the loan is collateral dependent. The amount of impairment, if any, and any subsequent changes are recorded as adjustments to the allowance for loan losses. A loan is impaired when it is probable the Company will be unable to collect all contractual principal and interest payments due in accordance with the terms of the loan agreement.

A loan is classified as a restructured loan when certain concessions have been made to the original contractual terms, such as a reduction in interest rate or deferral of interest or principal payments, due to the borrower's financial condition.

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

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Company considers consumer installment loans to be pools of small balance homogeneous loans, which are collectively evaluated for impairment.

Allowance for loan losses

The allowance for loan losses, a material estimate which could change significantly in the near-term, is established as losses are estimated to have occurred through a provision for losses charged against operations, and is maintained at a level that management considers adequate to absorb losses in the loan portfolio. Management's judgment in determining the adequacy of the allowance is inherently subjective and is based on the evaluation of individual loans, pools of homogeneous loans, the known and inherent risk characteristics and size of the loan portfolios, the assessment of current economic and real estate market conditions, estimates of the current value of underlying collateral, past loan loss experience, review of regulatory authority examination reports and evaluations of specific loans and other relevant factors. Loans, including impaired loans, are charged against the allowance for loan losses when management believes that the uncollectibility of principal is confirmed. Any subsequent recoveries are credited to the allowance for loan losses when received. In connection with the determination of the allowance for loan losses, management obtains appraisals for significant properties, when considered necessary.

The allowance consists of specific, general and unallocated components. The specific component relates to loans that are classified as either doubtful, substandard or special mention. For such loans that are also classified as impaired, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan. The general component covers non-classified loans and is based on historical loss experience adjusted for qualitative factors. An unallocated component may be maintained to cover uncertainties that could affect management's estimate or probable losses. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general losses in the portfolio.

Management believes the allowance for loan losses is adequate. While management uses available information to recognize losses on loans, future additions to the allowance or write-downs may be necessary based on changes in economic conditions. In addition, various regulatory agencies, as an integral part of their examination process, periodically review the Company's allowance for loan losses. Such agencies have the authority to require the Company to recognize additions to the allowance or charge-offs based on the agencies' judgments about information available to them at the time of their examination.

Interest and fees on loans

Interest on loans is accrued and included in operating income based on contractual rates applied to principal amounts outstanding. The accrual of interest income 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

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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 nonaccrual loan is restored to an accrual status when it is no longer delinquent and collectibility of interest and principal is no longer in doubt.

Loan origination fees, net of direct loan origination costs, are deferred and amortized as an adjustment to the loan's yield generally over the contractual life of the loan, utilizing the interest method.

Premises and equipment

Premises and equipment are stated at cost for purchased assets, and for assets under capital lease, at the lower of fair value or the net present value of the minimum lease payments required over the term of the lease, net of accumulated depreciation and amortization. Leasehold improvements are capitalized and amortized over the shorter of the terms of the related leases or the estimated economic lives of the improvements. Depreciation is charged to operations using the straight-line method over the estimated useful lives of the related assets which range from 3 to 20 years. Gains and losses on dispositions are recognized upon realization. Maintenance and repairs are expensed as incurred and improvements are capitalized.

Impairment of long-lived assets

Long-lived assets, including premises and equipment, which are held and used by the Company, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If impairment is indicated by that review, the asset is written down to its estimated fair value through a charge to noninterest expense.

Repurchase agreements

Repurchase agreements, which are classified as secured borrowings, generally mature within one to three days from the transaction date, and are reflected at the amount of cash received in connection with the transaction. The Company may be required to provide additional collateral based on the fair value of the underlying securities.

Income taxes

The Company recognizes income taxes under the asset and liability method. Under this method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases, and loss carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized.

Stock compensation plans

Statement of Financial Accounting Standards (SFAS) No. 123, "Accounting for Stock-Based Compensation", encourages all entities to adopt a fair value based method of accounting for employee stock compensation plans, whereby compensation cost is measured at the grant date based on the value of the award and is recognized over the service period, which is usually the vesting period. However, it also allows an entity to continue to measure compensation cost for those plans using the intrinsic value based method of accounting prescribed by Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees", whereby compensation cost is the excess, if any, of the quoted market price of the stock at the grant date (or other measurement date) over the amount an employee must pay to acquire the stock. Stock options issued to employees and directors under the Company's stock option and warrant plans have no intrinsic value at the grant date, and under Opinion No. 25 no compensation cost is recognized for them. The Company has elected to continue with the accounting methodology in Opinion No. 25 and, as a result, has provided pro forma disclosures of net loss and earnings (loss) per share and other disclosures, as if the fair value based method of accounting had been applied.

Had compensation cost for issuance of such options and warrants been recognized based on the fair values of awards on the grant dates, in accordance with the method described in SFAS No. 123, reported net loss and per share amounts for 2003 and 2002 would have been increased to the pro forma amounts shown below:

	2003	20
Net loss, as reported	$ (597,927)	$ (1
Deduct: total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(229,473)	
Pro forma net loss	$ (827,400)	$ (1
Basic and diluted loss per share:		
As reported	$ (0.56)	$
Pro forma	$ (0.78)	$

Related party transactions

Directors and officers of the Company and the Bank and their affiliates have been customers of and have had transactions with the Bank, and it is expected that such persons will continue to have such transactions in the future. Management believes that all deposit accounts, loans, services and commitments comprising such transactions were made in the ordinary course of business, and on substantially the same terms, including interest rates, as those prevailing at the time for comparable transactions with other customers who are not

directors or officers. In the opinion of management, the transactions with related parties did not involve more than normal risks of collectibility or favored treatment or terms, or present other unfavorable features. Notes 2, 8 and 14 contain details regarding related party transactions.

Comprehensive income

Accounting principles generally require that recognized revenue, expenses, gains and losses be included in net income. Although certain changes in assets and liabilities, such as unrealized gains and losses on available for sale securities, are reported as a separate component of the shareholders' equity section of the balance sheets, such items, along with net income or loss, are components of comprehensive income.

Fair value of financial instruments

The following methods and assumptions were used by the Company in estimating the fair value of its financial instruments.

Cash and due from banks, Federal funds sold, short-term investments, accrued interest receivable and repurchase agreements

The carrying amount is a reasonable estimate of fair value.

Securities

Fair values, excluding restricted Federal Home Loan Bank stock, are based on quoted market prices or dealer quotes, if available. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities. The carrying value of Federal Home Loan Bank stock approximates fair value based on the redemption provisions of the stock.

Loans receivable

For variable rate loans which reprice frequently, and have no significant changes in credit risk, fair value is based on the loan's carrying value. The fair value of fixed rate loans is estimated by discounting the future cash flows using the year-end rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities.

Servicing assets

The fair value is based on market prices for comparable servicing contracts, when available, or alternatively, is based on a valuation model that calculates the present value of estimated future net servicing income.

Deposits

The fair value of demand deposits, regular savings and certain money market deposits is the amount payable on demand at the reporting date. The fair value of certificates of deposit and other time deposits is estimated using a discounted cash flow calculation that applies interest rates currently being offered for deposits of similar remaining maturities to a schedule of aggregated expected maturities on such deposits.

Off-balance-sheet instruments

Fair values for the Company's off-balance-sheet instruments (lending commitments) are based on fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the counterparties' credit standing.

Recent accounting pronouncements

In November 2002, the FASB issued Interpretation No. 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others," ("FIN 45"), which covers guarantees such as standby letters of credit, performance guarantees, and direct or indirect guarantees of the indebtedness of others, but not guarantees of funding. FIN 45 requires a guarantor to recognize, at the inception of a guarantee, a liability in an amount equal to the fair value of the obligation undertaken in issuing the guarantee, and requires disclosure about the maximum potential payments that might be required, as well as the collateral or other recourse obtainable. The recognition and measurement provisions of FIN 45 were effective on a prospective basis after December 31, 2002, and its adoption by the Company on January 1, 2003 has not had a significant effect on the Company's consolidated financial statements.

In January 2003, the FASB issued Interpretation No. 46, "Consolidation of Variable Interest Entities," ("FIN 46"), which establishes guidance for determining when an entity should consolidate another entity that meets the definition of a variable interest entity. FIN 46 requires a variable interest entity to be consolidated by a company if that company will absorb a majority of the expected losses, will receive a majority of the expected residual returns, or both. Transfers to qualified special-purpose entities ("QSPEs") and certain other interests in a QSPE are not subject to the requirements of FIN 46. On December 17, 2003, the FASB revised FIN 46 ("FIN 46R") and deferred the effective date of FIN 46 to no later than the end of the first reporting period that ends after March 15, 2004, however, for special-purpose entities, FIN 46 would be required to be applied as of December 31, 2003. This Interpretation did not have a material effect on the Company's consolidated financial statements.

In April 2003, the FASB issued SFAS 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities." This Statement amends SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," and clarifies accounting for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities under SFAS No. 133. This Statement is effective for contracts entered into or modified after June 30, 2003, except in certain circumstances, and for hedging relationships designated after June 30, 2003. This Statement did not have a material effect on the Company's consolidated financial statements.

In May 2003, the FASB issued SFAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity." This Statement provides new rules on the accounting for certain financial instruments that, under previous guidance, issuers could account for as equity. Such financial instruments include mandatorily redeemable shares, instruments that require the issuer to buy back some of its share in exchange for cash or other assets, or obligations that can be settled with shares, the monetary value of which is fixed. Most of the guidance in SFAS No. 150 is effective for financial instruments entered into or modified after May 31, 2003, and otherwise is effective at the beginning of the first interim period beginning after June 30, 2003. This Statement had no effect on the Company's consolidated financial statements.

Reclassifications

Certain 2002 amounts have been reclassified to conform with the 2003 presentation, and such reclassifications had no effect on 2002 net loss or shareholders' equity.

Note 2. Restrictions on Cash and Cash Equivalents

The Company is required to maintain reserves against its respective transaction accounts and non-personal time deposits. At December 31, 2003, the Company was required to have cash and liquid assets of approximately $208,000 to meet these requirements. In addition, at December 31, 2003 and 2002, the Company was required to maintain $125,000 and $25,000, respectively in the Federal Reserve Bank for clearing purposes. Also, approximately $212,000 and $100,000, respectively, of short-term investments are maintained at another financial institution to secure available customer letters of credit with that institution, and approximately $11,000 and $10,000, respectively, of short-term investments are maintained with that institution to secure an available credit card line of credit for a Company director.

Note 3. Available for Sale Securities

The amortized cost, gross unrealized gains, gross unrealized losses and approximate fair values of available for sale securities at December 31, 2003 and 2002 are as follows:

2003	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	
U.S. Government Agency obligations	$ 7,200,948	$ -	$ (269,550)	$
Mortgage-backed securities	1,576,878	-	(30,208)	
	$ 8,777,826	$ -	$ (299,758)	$

At December 31, 2003, all securities above were in an unrealized loss position, and there were no unrealized losses on securities that have existed for a period of twelve months or more. Management believes that none of the unrealized losses on these securities are other than temporary because all of the unrealized losses relate to debt and mortgage-backed securities issued by U.S. Government Agencies, which the Company has both the intent and the ability to hold until maturity or until the fair value fully recovers. In addition, management considers the issuers of the securities to be financially sound and the Company will receive all contractual principal and interest related to these investments.

SOUTHERN CONNECTICUT BANCORP, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, Continued
December 31, 2003 and 2002

2002	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses
U.S. Government Agency obligations	$ 8,902,682	$ 110,252	$ (1,000)
Mortgage-backed securities	496,360	-	(6,802)
	$ 9,399,042	$ 110,252	$ (7,802)

The amortized cost and fair value of available for sale debt securities at December 31, 2003 by contractual maturity are presented below. Actual maturities of mortgage-backed securities may differ from contractual maturities because the mortgages underlying the securities may be called or repaid without any penalties. Because mortgage-backed securities are not due at a single maturity date, they are not included in the maturity categories in the following summary:

	Amortized Cost	Fair Value
Maturity:		
Within one year	$ -	$ -
After 1 but within 5 years	2,501,421	2,447,405
After 5 but within 10 years	4,199,527	4,013,413
Over 10 years	500,000	470,580
Mortgage-backed securities	1,576,878	1,546,670
	$ 8,777,826	$ 8,478,068

At December 31, 2003 and 2002, available for sale securities with a carrying value of $2,911,572 and $2,568,750, respectively, were pledged as collateral under repurchase agreements with Bank customers and to secure public deposits.

During 2003, proceeds from sales of available for sale securities were $4,357,995 and gross gains of $44,505 were recognized on such sales. During 2002, there were no sales of available for sale securities.

In December 2002, the Company transferred all of its held to maturity securities, which had a carrying value of $7,517,682, to the available for sale category. At the time of the transfer, the Company recognized an unrealized gain of $66,973, net of taxes, as an adjustment to other comprehensive income. The transfer of these securities resulted from a change in the Company's overall investment strategies and for liquidity purposes.

Note 4. Loans Receivable and Allowance for Loan Losses

A summary of the Company's loan portfolio at December 31, 2003 and 2002 is as follows:

	2003
Commercial loans secured by real estate	$ 18,043,588
Commercial loans	18,584,292
Construction and land loans, net of undisbursed portion of $729,220 in 2003 and $19,830 in 2002	1,500,891
Residential mortgages	948,258
Consumer home equity loans	1,042,717
Consumer installment loans	1,204,920
Total loans	41,324,666
Net deferred loan fees	(84,804)
Allowance for loan losses	(421,144)
Loans receivable, net	$ 40,818,718

The Company services certain loans that it has sold without recourse to third parties. The aggregate of loans serviced for others approximated $1,174,000 and $-0- as of December 31, 2003 and 2002, respectively.

The balance of capitalized servicing rights, included in other assets at December 31, 2003 and 2002, was $20,798 and $-0-, respectively. No impairment charges related to servicing rights were recognized during the years ended December 31, 2003 and 2002.

The changes in the allowance for loan losses for the years ended December 31, 2003 and 2002 are as follows:

	2003
Balance, beginning of year	$ 232,000
Provision for loan losses	213,100

Recoveries of loans previously charged-off	616
Loans charged-off	(24,572)
Balance, end of year	$ 421,144

At December 31, 2003, the unpaid principal balances of loans delinquent 90 days or more and placed on nonaccrual status were $94,063. At December 31, 2002, there were no loans delinquent 90 days or more or placed on nonaccrual status.

The following information relates to impaired loans as of and for the years ended December 31, 2003 and 2002:

	2003	
Loans receivable for which there is a related allowance for credit losses	$ 94,063	$
Loans receivable for which there is no related allowance for credit losses	$ -	$
Allowance for credit losses related to impaired loans	$ 21,381	$
Average recorded investment in impaired loans	$ 13,317	$

There was no interest income on impaired loans collected or recognized in 2003 and 2002. If nonaccrual loans had been current throughout their terms, additional interest income of approximately $4,800 would have been recognized in 2003. The Company has no commitments to lend additional funds to borrowers whose loans are impaired.

The Company's lending activities are conducted principally in the New Haven County section of Connecticut. The Company grants commercial and residential real estate loans, commercial business loans and a variety of consumer loans. In addition, the Company may grant loans for the construction of residential homes, residential developments and for land development projects. All residential and commercial mortgage loans are collateralized by first or second mortgages on real estate. The ability and willingness of borrowers to satisfy their loan obligations is dependent in large part upon the status of the regional economy and regional real estate market. Accordingly, the ultimate collectibility of a substantial portion of any resulting real estate acquired is susceptible to changes in market conditions.

The Company has established credit policies applicable to each type of lending activity in which it engages, evaluates the creditworthiness of each customer on an individual basis and, when deemed appropriate, obtains collateral. Collateral varies by each borrower and loan type. The market value of collateral is monitored on an ongoing basis and additional collateral is obtained when warranted. Important types of collateral include business assets, real estate, automobiles, marketable securities and time deposits. While collateral provides assurance as a secondary source of repayment, the Company ordinarily requires the primary source of repayment to be based on the borrower's ability to generate continuing cash flows.

SOUTHERN CONNECTICUT BANCORP, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, Continued
December 31, 2003 and 2002

Note 5. Premises and Equipment

At December 31, 2003 and 2002, premises and equipment consisted of the following:

	2003
Land	$ 255,766
Premises under capital lease	1,192,036
Building and improvements	674,046
Leasehold improvements	817,366
Furniture and fixtures	399,032
Equipment	483,626
Construction in progress	-
	3,821,872
Less accumulated depreciation and amortization	(361,957)
	$ 3,459,915

For the years ended December 31, 2003 and 2002, depreciation and amortization expense related to premises and equipment totaled $219,853 and $117,498, respectively.

Premises under capital lease of $1,192,036, and related accumulated amortization of $67,939 and $57,489, as of December 31, 2003 and 2002, respectively, are included in premises and equipment.

Note 6. Deposits

At December 31, 2003 and 2002, deposits consisted of the following:

	2003
Noninterest bearing	$ 13,781,286
Interest bearing:	
Time certificates, less than $100,000	3,057,294
Time certificates, $100,000 or more	7,051,249
Savings	2,633,341
Money market	17,251,327
Checking	3,499,378
Total interest bearing	33,492,589
Total deposits	$ 47,273,875

Contractual maturities of time certificates of deposit as of December 31, 2003 are summarized below:

Due within:	
1 year	$ 8,208,163
1-2 years	1,028,318
2-3 years	140,000
3-4 years	557,020
4-5 years	175,042
	$ 10,108,543

Interest expense on certificates of deposit in denominations of $100,000 or more was $90,394 and $87,538 for the years ended December 31, 2003 and 2002, respectively.

Note 7. Commitments

Federal Home Loan Bank borrowings and stock

The Bank is a member of the Federal Home Loan Bank of Boston ("FHLB"). At December 31, 2003 and 2002, the Bank had the ability to borrow from the FHLB based on a certain percentage of the value of the Bank's qualified collateral, as defined in the FHLB Statement of Products Policy, at the time of the borrowing. In accordance with an agreement with the FHLB, the qualified collateral must be free and clear of liens, pledges and encumbrances. There were no borrowings outstanding with the FHLB at December 31, 2003 and 2002.

The Bank is required to maintain an investment in capital stock of the FHLB in an amount equal to a percentage of its outstanding mortgage loans and contracts secured by residential properties, including mortgage-backed securities. No ready market exists for FHLB stock and it has no quoted market value. For disclosure purposes, such stock is assumed to have a market value which is equal to cost since the Bank can redeem the stock with FHLB at cost.

Other available borrowings

During 2003, the Company obtained secured and unsecured lines of credit with other financial institutions with total available borrowings of $4,400,000. There are no borrowings outstanding under these lines of credit as of December 31, 2003.

Employment agreements

The Company and the Bank have entered into an employment agreement (the "Chairman Agreement") with the Chairman and Chief Executive Officer of the Company and the Bank with an initial term of five years beginning October 1, 2001, which may be extended for additional one-year terms at the end of the initial term. In October 2003, the Company amended the Chairman Agreement to extend the initial five-year term by one year. The Chairman Agreement provides for a base salary with annual adjustments, and an annual bonus, as determined by

the Board of Directors. The Chairman Agreement also provides for vacation and various insurance benefits and reimbursement for travel, entertainment and bank-related education and convention expenses.

Also, under the Chairman Agreement, the Company issued to the Chairman options to purchase 50,000 shares of the Company's stock under the terms of the Company's 2001 Stock Option Plan (see Note 10).

In the event of the early termination of the Chairman for any reason other than cause, the Company would be obligated to compensate the Chairman, in accordance with the terms of the Chairman Agreement, through the full term of the Chairman Agreement. Also upon termination of the Chairman, for reasons other than cause, the Chairman Agreement provides that the Chairman will serve as a consultant to the Company, on a year to year basis, and will be compensated at the rate of

$60,000 per year plus the employee benefits previously described. Further, in the event the Chairman's position shall end or his responsibilities be significantly reduced as a result of a business combination (as defined), the Chairman will be entitled to a lump sum payment equal to three times his then current annual compensation.

Also, the Company entered into an employment agreement (the "President Agreement") with the new President of the Bank effective in February 2003, which expires on December 31, 2004. The President Agreement provides for a base salary and an annual bonus as determined by the Board of Directors. The President Agreement also provides for vacation and various insurance benefits and reimbursement for automobile, travel, entertainment, club dues and bank-related education and convention expenses. Also, under the President Agreement, the Company issued to the President options to purchase 20,000 shares of the Company's stock under the terms of the Company's 2002 Stock Option Plan.

Note 8. Lease and Subleases

The Company leases the Bank's main office under a twenty-year capital lease that expires in 2021. In addition, the Company leases its Branford branch office under a twenty-year capital lease that expires in 2022. Under the terms of the leases, the Bank will pay all executory costs including property taxes, utilities and insurance. The Company has also entered into an operating lease for the main office of its new bank subsidiary expected to be formed and become operational in 2004 (see Note 17). The initial term of the lease expires in 2008, and the lease contains three five-year renewal options. The Company also leases the driveway to its main office and certain equipment under non-cancelable operating leases.

The Company has also entered into a five-year sublease agreement for excess office space in its premises with a tenant, the principal of which is related to the Company's Vice Chairman. During 2002, the Company also had a sublease with another related party, which lease was terminated in early 2003 when such related party became an officer of the Bank.

At December 31, 2003, future minimum lease payments to be made and received under these leases by year and in the aggregate, are as follows:

Year	Capital Leases	Operating Leases	Su
2004	$ 156,984	$ 51,911	
2005	161,506	51,911	
2006	166,028	50,555	
2007	171,424	49,199	
2008	178,564	49,199	
2009 and thereafter	2,822,967	44,319	
	3,657,473	$ 297,094	

Less amount representing interest	(2,466,594)
Present value of future minimum lease payments - capital lease obligation	$ 1,190,879

Total rent expense charged to operations under the operating leases approximated $3,200 and $3,000 for the years ended December 31, 2003 and 2002, respectively. Rental income under the subleases approximated $17,200 and $17,800 for the years ended December 31, 2003 and 2002, respectively.

Note 9. Income Taxes

A reconciliation of the anticipated income tax benefit (computed by applying the statutory Federal income tax rate of 34% to the loss before income taxes) to the amount reported in the statement of operations for the years ended December 31, 2003 and 2002 is as follows:

	2003
Benefit for income taxes at statutory Federal rate	$ (203,295)
State tax benefit, net of Federal benefit	(29,201)
Increase in valuation allowance	253,878
Other	(21,382)
	$ -

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At December 31, 2003 and 2002, the components of gross deferred tax assets and liabilities are as follows:

	2003
Deferred tax assets:	
Allowance for loan losses	$ 164,036
Net operating loss carryforwards	906,259
Start-up costs	142,401
Unrealized loss on available for sale securities	116,756
Other	66,796

Gross deferred tax assets	1,396,248
Less valuation allowance	(1,304,609)
Deferred tax assets - net of valuation allowance	91,639
Deferred tax liabilities:	
Tax bad debt reserve	25,736
Depreciation	65,903
Unrealized gain on available for sale securities	-
Gross deferred tax liabilities	91,639
Net deferred tax liability	$ -

As of December 31, 2003, the Company had tax net operating loss carryforwards of approximately $2,325,000 available to reduce future Federal and state taxable income, which expire in 2021 through 2023.

The net changes in the valuation allowance for 2003 and 2002 were increases of $370,634 and $526,329, respectively. The changes in the valuation allowance have been allocated between operations and equity to adjust the deferred tax asset to an amount considered by management more likely than not to be realized. The portion of the change in the valuation allowance allocated to equity is to eliminate the tax benefit related to the unrealized holding gains or losses on available for sale securities.

Note 10. Shareholders' Equity

Stock dividend

On January 13, 2004, the Company declared a 10% stock dividend that was distributed on February 16, 2004. As a result, the 2003 balance sheet and statement of changes in shareholders' equity, and all per share amounts, have been retroactively revised to reflect this dividend as if it were effective at December 31, 2003. Generally accepted accounting principles require such dividends to be recorded at fair value; however, when there is an accumulated deficit, the Securities and Exchange Commission (SEC) advises that such stock dividends be accounted for by capitalizing the stock issued at par value only, through a reduction in additional paid-in capital.

Income (loss) per share

The Company is required to present basic income (loss) per share and diluted income (loss) per share in its statements of operations. Basic and fully diluted income (loss) per share are computed by dividing net income (loss) by the weighted average number of common shares outstanding. Diluted per share amounts assume exercise of all potential common stock instruments unless the effect is to reduce the loss or increase the income per share. For the periods presented, the common stock equivalents described below have been excluded from the computation of the net loss per share because the inclusion of such equivalents is anti-dilutive. Weighted average shares outstanding were 1,063,320 for the years ended December 31, 2003 and 2002, after giving effect to the stock dividend declared in January 2004.

Stock options

The Company has adopted two stock option plans, the 2001 Stock Option Plan (the "2001 Option Plan") and the 2002 Stock Option Plan (the "2002 Option Plan"), under which an aggregate of 340,780 shares of the Company's common stock are reserved for issuance upon the exercise of both incentive options and nonqualified options granted under both option plans.

Under both option plans, the exercise price for each share covered by an option may not be less than the fair market value of a share of the Company's common stock on the date of grant. For incentive options granted to a person who owns more than 10% of the combined voting power of the Company or any subsidiary ("ten percent shareholder"), the exercise price cannot be less than 110% of the fair market value on the date of grant.

Options under both options plans have a term of ten years unless otherwise determined at the time of grant, except that incentive options granted to any ten percent shareholder will have a term of five years unless a shorter term is fixed. Under both option plans, unless otherwise fixed at the time of grant, 40% of the options become exercisable one year from the date of grant, and 30% of the options become exercisable at each of the second and third anniversaries from the date of grant.

Upon adoption of the 2002 Option Plan in May 2002, the Company determined that no additional options will be granted under the 2001 Option Plan.

A summary of the status of the stock options at December 31, 2003 and 2002, and changes during the years then ended, is as follows. The 2003 and 2002 information has been presented to give effect to the stock dividend declared in January 2004.

2003

	Number of Shares	Weighted-Average Exercise Price	Number of Shares
Outstanding at beginning of year	74,140	$10.91	85,800
Granted	255,110	7.66	16,280
Terminated	(11,770)	9.08	(27,940
Outstanding at end of year	317,480	8.37	74,140
Exercisable at end of year	44,814	$10.91	23,320
Weighted-average fair value per option of options granted during the year	$ 2.44		$ 1.90

At December 31, 2003, the exercise prices on outstanding options ranged from $7.27 to $10.91, and at December 31, 2002, the exercise price on all options outstanding was $10.91. The weighted-average remaining contractual life for the options outstanding at December 31, 2003 and 2002 is 9.2 and 8.7 years, respectively.

Stock warrants

The Company adopted the 2001 Warrant Plan and the 2001 Supplemental Warrant Plan (the "Warrant Plans"), under which an aggregate of 110,000 shares of the Company's common stock were reserved for issuance upon the exercise of warrants granted to non-employee directors of the Company and the Bank, and certain other individuals involved in the organization of the Bank.

Warrants under the Warrant Plans have a term of ten years. Forty percent of the warrants become exercisable one year from the date of grant, and 30% of the warrants become exercisable at each of the second and third anniversaries from the date of grant.

A summary of the status of the warrants at December 31, 2003 and 2002, and changes during the years then ended, is as follows. The 2003 and 2002 information has been presented to give effect to the stock dividend declared in January 2004.

	2003		20
	Number of Shares	Weighted-Average Exercise Price	Number of Shares
Outstanding at beginning of year	79,953	$10.91	79,953
Granted	-	-	-
Exercised	-	-	-
Outstanding at end of year	79,953	10.91	79,953
Exercisable at end of year	55,967	$10.91	31,981
Weighted-average fair value per warrant of warrants granted during the year	N/A		N/A

The weighted-average remaining contractual life for the warrants outstanding at December 31, 2003 and 2002 is 7.7 and 8.7 years, respectively.

The fair value of options and warrants issued in 2003 and 2002 was estimated at the grant date using the Black-Scholes option-pricing model with the following assumptions:

	2003	2
Dividend rate	-	
Risk free interest rate	2.88% to 4.02%	2
Weighted-average expected lives	8 years	8 y
Volatility	20%	2

Note 11. 401(k) Profit Sharing Plan

The Bank's employees are eligible to participate in the Bank of Southern Connecticut 401(k) Profit Sharing Plan (the "Plan") under Section 401(k) of the Internal Revenue Code. The Plan covers substantially all employees of the Bank. Under the terms of the Plan, participants can contribute a discretionary percentage of compensation, with total annual contributions subject to Federal limitations. The Bank may make discretionary contributions to the Plan. Participants are immediately vested in their contributions and become fully vested in employer contributions after three years of service. There were no discretionary contributions made by the Bank during 2003 and 2002.

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Note 12. Financial Instruments with Off-Balance-Sheet Risk

In the normal course of business, the Company is a party to financial instruments with off-balance-sheet risk to meet the financing needs of its customers. These financial instruments include commitments to extend credit and involve, to varying degrees, elements of credit and interest rate risk in excess of the amounts recognized in the financial statements. The contractual amounts of these instruments reflect the extent of involvement the Company has in particular classes of financial instruments.

The contractual amounts of commitments to extend credit represents the amounts of potential accounting loss should: the contract be fully drawn upon; the customer default; and the value of any existing collateral become worthless. The Company uses the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments and evaluates each customer's creditworthiness on a case-by-case basis. Management believes that the Company controls the credit risk of these financial instruments through credit approvals, credit limits, monitoring procedures and the receipt of collateral as deemed necessary.

Financial instruments whose contract amounts represent credit risk are as follows at December 31, 2003:

	2003	2002
Commitments to extend credit:		
Future loan commitments	$ 3,752,000	$ 2,890
Unused lines of credit	9,065,661	5,518
Undisbursed construction loans	729,220	19
Financial standby letters of credit	933,055	338
	$ 14,479,936	$ 8,765

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments to extend credit generally have fixed expiration dates or other termination clauses and may require payment of a fee by the borrower. Since these commitments could expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The amount of collateral obtained, if deemed necessary by the Company upon extension of credit, is based on management's credit evaluation of the counter party. Collateral held varies, but may include residential and commercial property, deposits and securities.

Standby letters of credit are written commitments issued by the Company to guarantee the performance of a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. As of January 1, 2003, newly issued or modified guarantees that are not derivative contracts have been recorded on the Company's consolidated balance sheet at their fair value at inception. The liability related to guarantees recorded at December 31, 2003 was not significant.

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Note 13. Regulatory Matters

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

Quantitative measures established by regulation to ensure capital adequacy require the Company and the Bank to maintain minimum amounts and ratios (set forth in the table below) of total and Tier I capital (as defined in the regulations) to risk-weighted assets (as defined), and of Tier I capital (as defined) to average assets (as defined). Management believes, as of December 31, 2003, that the Company and the Bank meet all capital adequacy requirements to which they are subject.

As of December 31, 2003, the most recent notification from the Federal Deposit Insurance Corporation and the State of Connecticut Department of Banking categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, the Bank must maintain minimum total risk-based, Tier I risk-based, and Tier I leverage ratios as set forth in the table. There are no conditions or events since then, that management believes have changed the Bank's category.

The Bank's actual capital amounts and ratios at December 31, 2003 and 2002 were (dollars in thousands):

2003	Actual		For Capital Adequacy Purposes		Ca Pr Ac
	Amount	Ratio	Amount	Ratio	Amo
Total Capital to Risk-Weighted Assets	$ 8,013	17.24%	$ 3,718	8.00%	$ 4
Tier I Capital to Risk-Weighted Assets	7,592	16.33%	1,860	4.00%	2
Tier I Capital to Average Assets	7,592	14.16%	2,145	4.00%	2

For Capital Ca

2002	Actual		Adequacy Purposes		Pr Ac
	Amount	Ratio	Amount	Ratio	Amo
Total Capital to Risk-Weighted Assets	$ 8,309	32.43%	$ 2,050	8.00%	$ 2
Tier I Capital to Risk-Weighted Assets	8,077	31.52%	1,025	4.00%	1
Tier I Capital to Average Assets	8,077	23.76%	1,360	4.00%	1

The Company's actual and required ratios are not substantially different from those shown above.

Restrictions on dividends, loans or advances

The Company's ability to pay cash dividends is dependent on the Bank's ability to pay dividends to the Company. However, certain restrictions exist regarding the ability of the Bank to transfer funds to the Company in the form of cash dividends, loans or advances. Regulatory approval is required to pay dividends in excess of the Bank's net earnings retained in the current year plus retained net earnings for the preceding two years. The Bank is also prohibited from paying dividends that would reduce its capital ratios below minimum regulatory requirements, and the Federal Reserve Board may impose further dividend restrictions on the Company. During 2002, the Bank requested, and was granted, permission from the State of Connecticut Department of Banking, to pay a special dividend to the Company in the amount of $200,000. At December 31, 2003 and 2002, no dividends may be declared by the Bank without regulatory approval.

Under Federal Reserve regulation, the Bank is also limited to the amount it may loan to the Company, unless such loans are collateralized by specified obligations. Loans or advances to the Company by the Bank are limited to 10% of the Bank's capital stock and surplus on a secured basis.

Note 14. Related Party Transactions

In the normal course of business, the Company may grant loans to executive officers, directors and members of their immediate families, as defined, and to entities in which these individuals have more than a 10% equity ownership. Such loans are transacted at terms including interest rates, similar to those available to unrelated customers.

Changes in loans outstanding to such related parties during 2003 and 2002 are as follows:

	2003	20

Balance, beginning of year	$ 534,637	$
Additional loans	1,225,195	
Repayments	(962,411)	
Balance, end of year	$ 797,421	$

Related party deposits aggregated approximately $7,108,000 and $3,999,000 as of December 31, 2003 and 2002, respectively.

Included in professional services for the years ended December 31, 2003 and 2002 are approximately $4,800 and $7,900, respectively, in legal fees incurred for services provided by law firms, principals of which are directors of the Company. Included in consulting fees for the years ended December 31, 2003 and 2002 are $29,300 and $127,400, respectively, in consulting fees and expenses paid to entities, the principals of which are related to Company directors.

In addition, during 2003 and 2002, the Company paid approximately $1,500 and $46,900, respectively, for capital expenditures and maintenance to certain companies, principals of which are directors of the Company.

Also during 2003 and 2002, the Company purchased investment securities, including accrued interest and fees, of approximately $10,950,000 and $8,176,000, respectively, through an investment brokerage firm, an employee of which is related to the Company's Chairman and Chief Executive Officer.

Lastly, as described in Note 8, rental income and expense reimbursements of approximately $16,500 and $14,800 were received in 2003 and 2002, respectively, from tenants, the principals of which are related to the Company's Chairman and Chief Executive Officer, and the Company's Vice Chairman.

Note 15. Other Comprehensive Income

Other comprehensive income, which is comprised solely of the change in unrealized gains and losses on available for sale securities, is as follows:

	2003	
	Before-Tax Amount	Taxes
Unrealized holding losses arising during period	$ (446,713)	$ 44,321
Less reclassification adjustment for gains recognized		

in income	44,505	(4,416)
Unrealized holding loss on available for sale securities, net of taxes	$ (402,208)	$ 39,905

	2002	
	Before-Tax Amount	Taxes
Unrealized holding losses arising during period	$ (7,252)	$ 2,824
Add adjustment for unrealized gains on held to maturity securities transferred to available for sale securities	109,702	(42,729)
Unrealized holding gain on available for sale securities, net of taxes	$ 102,450	$ (39,905)

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Note 16. Fair Value of Financial Instruments and Interest Rate Risk

SFAS No. 107, "Disclosures About Fair Value of Financial Instruments" ("Statement No. 107"), requires disclosure of fair value information about financial instruments, whether or not recognized in the balance sheet, for which it is practicable to estimate that value. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rates and estimates of future cash flows. In that regard, the derived fair value estimates cannot be substantiated by comparisons to independent markets and, in many cases, could not be realized in immediate settlement of the instrument. Statement No. 107 excludes certain financial instruments from its disclosure requirements. Accordingly, the aggregate fair value amounts presented do not represent the underlying value of the Company.

Management uses its best judgment in estimating the fair value of the Company's financial instruments; however, there are inherent weaknesses in any estimation technique. Therefore, for substantially all financial instruments, the fair value estimates presented herein are not necessarily indicative of the amounts the Company could have realized in a sales transaction at December 31, 2003 and 2002. The estimated fair value amounts for 2003 and 2002 have been measured as of their respective year-ends, and have not been reevaluated or updated for purposes of these consolidated financial statements subsequent to those respective dates. As such, the fair values of these financial instruments subsequent to the respective reporting dates may be different from the amounts reported at each year-end.

The information presented should not be interpreted as an estimate of the fair value of the entire Company since a fair value calculation is only required for a limited portion of the Company's assets and liabilities. Due to the wide range of valuation techniques and the degree of subjectivity used in making the estimate, comparisons between the Company's disclosures and those of other bank holding companies may not be meaningful.

As of December 31, 2003 and 2002, the recorded book balances and estimated fair values of the Company's financial instruments were:

	2003		
	Recorded Book Balance	Fair Value	Recorded Book Balance
Financial Assets:			
Cash and due from banks	$ 1,147,883	$ 1,147,883	$ 1,245,010
Federal funds sold	966,000	966,000	1,144,000
Short-term investments	454,115	454,115	662,419
Available for sale securities	8,478,068	8,478,068	9,501,492
Federal Home Loan Bank stock	21,500	21,500	500
Loans receivable, net	40,818,718	40,818,116	19,049,212
Accrued interest receivable	196,545	196,545	187,672
Servicing rights	20,798	20,798	--
Financial Liabilities:			
Noninterest-bearing deposits	13,781,286	13,781,256	6,401,759
Time certificates of deposits	10,108,543	10,197,429	6,351,307
Savings deposits	2,633,341	2,633,341	1,029,433
Money market deposits	17,251,327	17,251,327	8,858,585
Interest bearing checking accounts	3,499,378	3,499,378	2,351,847
Repurchase agreements	339,752	339,752	822,529

Unrecognized financial instruments

Loan commitments on which the committed interest rate is less than the current market rate are insignificant at December 31, 2003 and 2002.

The Company assumes interest rate risk (the risk that general interest rate levels will change) as a result of its normal operations. As a result, the fair values of the Company's financial instruments will change when interest rate levels change and that change may be either favorable or unfavorable to the Company. Management attempts to match maturities of assets and liabilities to the extent believed necessary to minimize interest rate risk. However, borrowers with fixed rate obligations are less likely to prepay in a rising rate environment and more likely to prepay in a falling rate environment. Conversely, depositors who are receiving fixed rates are more likely to withdraw funds before maturity in a rising rate environment and less likely to do so in a falling rate environment. Management monitors rates and maturities of assets and liabilities and attempts to minimize interest rate risk by adjusting terms of new loans and deposits and by investing in securities with terms that mitigate the Company's overall interest rate risk.

Note 17. Business Developments

During 2003, the Company's Board of Directors approved the establishment of a new commercial bank in New London, Connecticut and the Company plans to raise between $10 million to $15 million in capital through a public offering of its common stock to fund the establishment of the new bank and for other corporate purposes. In October, the Company submitted its final application to the State of Connecticut Department of Banking related to the establishment of the new bank. Subject to regulatory approval and the successful raising of capital, the Company plans to open the new bank in the fourth quarter of 2004.