

FEDERAL TRUST CORP
Form 10-Q
November 04, 2005

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

FORM 10-Q

(Mark One)

Quarterly report under Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended September 30, 2005

Transition report under Section 13 or 15(d) of the Exchange Act

For the transition period from _____ to _____

Commission file number 33-27139

FEDERAL TRUST CORPORATION

(Exact Name of Registrant as Specified in Its Charter)

Florida

59-2935028

*(State or Other Jurisdiction
of Incorporation or Organization)*

*(I.R.S. Employer
Identification No.)*

**312 West 1st Street
Sanford, Florida 32771**

(Address of Principal Executive Offices)

(407) 323-1833

N/A

(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)

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

Yes No

Indicate by check mark whether the Registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act):

Yes No

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act):

Yes No

State the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date:

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Common stock, par value \$.01 per share

8,299,343 shares

(class)

Outstanding at October 28, 2005

FEDERAL TRUST CORPORATION AND SUBSIDIARIES

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FEDERAL TRUST CORPORATION AND SUBSIDIARIES

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

Condensed Consolidated Balance Sheets
(\$ in thousands, except per share amounts)

| | At | |
|---|-----------------------|----------------------|
| | September 30, 2005 | December 31, 2004 |
| | (Unaudited) | |
| Assets | | |
| Cash and due from banks | \$ 6,656 | \$ 3,645 |
| Interest-earning deposits | 1,305 | 3,836 |
| Cash and cash equivalents | 7,961 | 7,481 |
| Securities available for sale | 47,196 | 41,172 |
| Loans, less allowance for loan losses of \$4,326 in 2005 and \$3,835 in 2004 | 624,119 | 521,331 |
| Accrued interest receivable | 3,706 | 3,254 |
| Premises and equipment, net | 13,834 | 12,499 |
| Foreclosed assets | 107 | 326 |
| Federal Home Loan Bank stock | 10,610 | 7,385 |
| Mortgage servicing rights, net | 801 | 868 |
| Bank-owned life insurance | 6,898 | 6,717 |
| Deferred tax asset | 1,176 | 1,119 |
| Other assets | 1,407 | 979 |
| Total assets | \$ 717,815 | \$ 603,131 |
| Liabilities and Stockholders' Equity | | |
| Liabilities: | | |
| Noninterest-bearing demand deposits | \$ 15,120 | \$ 21,305 |
| Interest-bearing demand deposits | 48,807 | 48,792 |
| Money-market deposits | 76,592 | 76,236 |
| Savings deposits | 4,610 | 6,237 |
| Time deposits | 304,090 | 251,546 |
| Total deposits | 449,219 | 404,116 |
| Federal Home Loan Bank advances | 209,200 | 143,700 |
| Other borrowings | 1,200 | 885 |
| Junior subordinated debentures | 5,155 | 5,155 |
| Capital lease obligation | 2,835 | 3,049 |
| Accrued interest payable | 908 | 811 |
| Official checks | 1,260 | 1,045 |
| Other liabilities | 4,770 | 4,983 |
| Total liabilities | 674,547 | 563,744 |
| Stockholders' equity: | | |
| Common stock, \$.01 par value, 15,000,000 shares authorized; 8,299,343 and 8,061,813 shares issued in 2005 and 2004, respectively | 83 | 81 |
| Additional paid-in capital | 33,555 | 32,059 |
| Retained earnings | 10,625 | 8,089 |
| Unallocated ESOP shares (47,114 shares in 2005 and 119,375 shares in 2004) | (340) | (862) |
| Accumulated other comprehensive income (loss) | (655) | 20 |

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| | | |
|--|------------|------------|
| Total stockholders' equity | 43,268 | 39,387 |
| Total liabilities and stockholders' equity | \$ 717,815 | \$ 603,131 |

See Accompanying Notes to Condensed Consolidated Financial Statements.

FEDERAL TRUST CORPORATION AND SUBSIDIARIES

Condensed Consolidated Statements of Earnings (Unaudited)
(\$ in thousands, except per share amounts)

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|-------------------------------------|---------------|------------------------------------|-----------------|
| | 2005 | 2004 | 2005 | 2004 |
| Interest income: | | | | |
| Loans | \$ 7,788 | \$ 5,683 | \$ 22,082 | \$ 16,362 |
| Securities | 510 | 334 | 1,450 | 914 |
| Other | 113 | 71 | 350 | 196 |
| Total interest income | 8,411 | 6,088 | 23,882 | 17,472 |
| Interest expense: | | | | |
| Deposits | 3,367 | 1,901 | 8,642 | 5,316 |
| Other | 1,828 | 812 | 4,695 | 2,307 |
| Total interest expense | 5,195 | 2,713 | 13,337 | 7,623 |
| Net interest income | 3,216 | 3,375 | 10,545 | 9,849 |
| Provision for loan losses | 200 | 150 | 500 | 850 |
| Net interest income after provision for loan losses | 3,016 | 3,225 | 10,045 | 8,999 |
| Other income: | | | | |
| Service charges and fees | 102 | 108 | 327 | 394 |
| Gain on sale of loans held for sale | 17 | 117 | 287 | 296 |
| Net gains on sales of securities available for sale | 80 | 16 | 208 | 60 |
| Rental income | 70 | 83 | 234 | 214 |
| Increase in cash surrender value of life insurance policies | 60 | 65 | 175 | 200 |
| Other | 318 | 291 | 848 | 801 |
| Total other income | 647 | 680 | 2,079 | 1,965 |
| Other expenses: | | | | |
| Salary and employee benefits | 1,246 | 1,275 | 3,716 | 3,646 |
| Occupancy expense | 417 | 408 | 1,225 | 1,169 |
| Professional services | 122 | 123 | 490 | 450 |
| Data processing | 157 | 152 | 468 | 451 |
| Other | 385 | 502 | 1,192 | 1,359 |
| Total other expenses | 2,327 | 2,460 | 7,091 | 7,075 |
| Earnings before income taxes | 1,336 | 1,445 | 5,033 | 3,889 |
| Income taxes | 452 | 491 | 1,763 | 1,287 |
| Net earnings | \$ 884 | \$ 954 | \$ 3,270 | \$ 2,602 |
| Earnings per share: | | | | |
| Basic | \$.11 | \$.13 | \$.41 | \$.38 |
| Diluted | \$.11 | \$.13 | \$.40 | \$.37 |
| Weighted-average shares outstanding for (in thousands): | | | | |

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| | | | | |
|--------------------------|--------|--------|--------|--------|
| Basic | 8,217 | 7,322 | 8,057 | 6,797 |
| Diluted | 8,352 | 7,486 | 8,176 | 6,959 |
| Cash dividends per share | \$.03 | \$.02 | \$.09 | \$.06 |

See Accompanying Notes to Condensed Consolidated Financial Statements.

FEDERAL TRUST CORPORATION AND SUBSIDIARIES

Condensed Consolidated Statements of Stockholders' Equity
For the Nine Months Ended September 30, 2005 and 2004
(\$ in thousands)

| | Common Stock | | Additional Paid-In Capital | Retained Earnings | Unallocated ESOP Shares | Accumulated Other Compre- hensive Income (Loss) | Total Stockholders Equity |
|--|--------------|--------|----------------------------------|----------------------|-------------------------------|--|---------------------------------|
| | Shares | Amount | | | | | |
| Balance at December 31, 2003 | 6,661,807 | \$ 67 | \$ 22,069 | \$ 5,629 | \$ (979) | \$ (329) | \$ 26,457 |
| Comprehensive income: | | | | | | | |
| Net earnings (unaudited) | | | | 2,602 | | | 2,602 |
| Change in unrealized loss on securities available for sale, net of income taxes of \$329 (unaudited) | | | | | | 139 | 139 |
| Comprehensive income (unaudited) | | | | | | | 2,741 |
| Proceeds from sale of common stock, net of offering costs of \$478 (unaudited) | 1,400,000 | 14 | 10,008 | | | | 10,022 |
| Issuance of common stock, stock options exercised (unaudited) | 6 | | | | | | |
| ESOP shares allocated (4,453 shares) (unaudited) | | | | | 32 | | 32 |
| Dividends paid (unaudited) | | | | (400) | | | (400) |
| Balance at Sept. 30, 2004 (unaudited) | 8,061,813 | \$ 81 | \$ 32,077 | \$ 7,831 | \$ (947) | \$ (190) | \$ 38,852 |
| Balance at December 31, 2004 | 8,061,813 | \$ 81 | \$ 32,059 | \$ 8,089 | \$ (862) | \$ 20 | \$ 39,387 |
| Comprehensive income: | | | | | | | |
| Net earnings (unaudited) | | | | 3,270 | | | 3,270 |
| Change in unrealized gain on securities available for sale, net of income taxes of \$407 (unaudited) | | | | | | (675) | (675) |
| Comprehensive income (unaudited) | | | | | | | 2,595 |
| Tax benefit related to exercise of stock options (unaudited) | | | 169 | | | | 169 |
| Issuance of common stock, stock options exercised (unaudited) | 237,530 | 2 | 989 | | | | 991 |
| ESOP shares allocated (2,261 shares) (unaudited) | | | 7 | | 16 | | 23 |
| ESOP shares sold (70,000 shares) (unaudited) | | | 331 | | 506 | | 837 |
| Dividends paid (unaudited) | | | | (734) | | | (734) |
| Balance at Sept. 30, 2005 (unaudited) | 8,299,343 | \$ 83 | \$ 33,555 | \$ 10,625 | \$ (340) | \$ (655) | \$ 43,268 |

See Accompanying Notes to Condensed Consolidated Financial Statements.

FEDERAL TRUST CORPORATION AND SUBSIDIARIES

Condensed Consolidated Statements of Cash Flows
(Unaudited in thousands)

| | Nine Months Ended September 30 | |
|---|-----------------------------------|-----------------|
| | 2005 | 2004 |
| Cash flows from operating activities: | | |
| Net earnings | \$ 3,270 | \$ 2,602 |
| Adjustments to reconcile net earnings to net cash provided by operating activities: | | |
| Depreciation and amortization | 524 | 513 |
| Provision for loan losses | 500 | 850 |
| Provision for deferred taxes | 351 | |
| Net amortization of premiums and discounts on securities | 70 | 272 |
| Net amortization of loan origination fees, costs, premiums and discounts | 725 | 743 |
| Amortization of mortgage servicing rights | 247 | 181 |
| Valuation allowance on mortgage servicing rights | | 30 |
| Increase in cash surrender value of life insurance policies | (175) | (135) |
| Proceeds from sales of loans held for sale | 18,390 | 10,636 |
| Loans originated for resale | (10,106) | (3,781) |
| Gain on sale of loans held for sale | (287) | (179) |
| Net gain on sales of securities available for sale | (208) | (44) |
| Tax benefit from exercise of options | 169 | |
| Cash provided by (used in) resulting from changes in: | | |
| Accrued interest receivable | (452) | (133) |
| Other assets | (434) | (237) |
| Accrued interest payable | 97 | 172 |
| Official checks | 215 | (139) |
| Other liabilities | (937) | 772 |
| Net cash provided by operating activities | <u>11,958</u> | <u>10,772</u> |
| Cash flows from investing activities: | | |
| Purchase of securities available for sale | (17,432) | (13,645) |
| Proceeds from principal repayments and sales of securities available for sale | 13,003 | 7,494 |
| Loan principal repayments, net of originations | 39,931 | 13,651 |
| Purchase of loans | (154,783) | (63,132) |
| Purchase of premises and equipment | (1,859) | (928) |
| Purchase of Federal Home Loan Bank stock | (3,225) | (475) |
| Net proceeds from sale of foreclosed assets | 343 | 1,231 |
| Net cash used in investing activities | <u>(124,022)</u> | <u>(55,804)</u> |
| Cash flows from financing activities: | | |
| Net increase in deposits | 45,103 | 31,207 |
| Net increase in Federal Home Loan Bank advances | 65,500 | 15,000 |
| Net increase (decrease) in other borrowings | 315 | (1,300) |
| Principal repayments under capital lease obligation | (214) | (143) |
| Net increase in advance payments by borrowers for taxes and insurance | 747 | 741 |
| Dividends paid | (734) | (266) |
| Proceeds from sales of common stock and ESOP shares | 1,827 | |
| Net cash provided by financing activities | <u>112,544</u> | <u>45,239</u> |
| Net increase in cash and cash equivalents | 480 | 207 |
| Cash and cash equivalents at beginning of period | 7,481 | 5,733 |
| Cash and cash equivalents at end of period | <u>\$ 7,961</u> | <u>\$ 5,940</u> |

FEDERAL TRUST CORPORATION AND SUBSIDIARIES**Condensed Consolidated Statements of Cash Flows, Continued
(Unaudited in thousands)**

| | Nine Months Ended September 30 | |
|--|-----------------------------------|-----------|
| | 2005 | 2004 |
| Supplemental disclosure of cash flow information-Cash paid during the period for: | | |
| Interest | \$ 13,240 | \$ 7,364 |
| Income taxes | \$ 2,055 | \$ 622 |
| Noncash transactions: | | |
| Foreclosed assets acquired in settlement of loans | \$ 124 | \$ 939 |
| Accumulated other comprehensive income (loss), net change in unrealized gain (loss) on securities available for sale, net of tax | \$ (675) | \$ 139 |
| Transfer of loans in portfolio to loans held for sale | \$ 9,700 | \$ 11,735 |
| Mortgage servicing rights recognized upon sale of loans held for sale | \$ 180 | \$ 48 |
| ESOP shares allocated | \$ 23 | \$ |
| Securitization of loans held for sale | \$ 2,538 | \$ 32 |

See Accompanying Notes to Condensed Consolidated Financial Statements.

FEDERAL TRUST CORPORATION AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements (Unaudited)

(1) Description of Business and Basis of Presentation

Organization. Federal Trust Corporation (Federal Trust) is the sole shareholder of Federal Trust Bank (the Bank). Federal Trust operates as a unitary savings and loan holding company. Federal Trust 's primary business activity is the operation of the Bank. The Bank is federally-chartered as a stock savings bank. The Bank 's deposits are insured up to the applicable limits by the Federal Deposit Insurance Corporation. The Bank provides a wide range of banking services to individual and corporate customers through its six offices located in Orange, Seminole and Volusia counties, Florida. Federal Trust Mortgage Company (the Mortgage Company), a wholly-owned subsidiary of Federal Trust, was established in May 2005 to provide residential loan products for customers of the Bank, to close mortgage loans on behalf of certain third party purchasers, and to sell mortgage loans in the secondary market.

The condensed consolidated financial statements include the accounts of Federal Trust, the Bank and the Mortgage Company (collectively referred to herein as, the Company). All significant intercompany accounts and transactions have been eliminated in consolidation.

In the opinion of management, the accompanying condensed consolidated financial statements contain all adjustments (principally consisting of normal recurring accruals) necessary to present fairly the financial position as of September 30, 2005, the results of operations for the three- and nine-month periods ended September 30, 2005 and 2004, and cash flows for the nine-month periods ended September 30, 2005 and 2004. The results of operations for the three- and nine-month periods ended September 30, 2005, are not necessarily indicative of the results to be expected for the entire year ended December 31, 2005. These statements should be read in conjunction with the consolidated financial statements included in Federal Trust 's Annual Report on Form 10-KSB for the year ended December 31, 2004.

(2) Loans

The components of loans are summarized as follows (in thousands):

| | At Sept 30, 2005 | At December 31, 2004 |
|--|---------------------|-------------------------|
| | _____ | _____ |
| Residential lending: | | |
| Mortgages (1) | \$ 392,006 | \$ 374,581 |
| Lot loans | 38,378 | 41,369 |
| Construction | 102,749 | 5,405 |
| | _____ | _____ |
| Total residential lending | 533,133 | 421,355 |
| | _____ | _____ |
| Commercial lending: | | |
| Real estate secured | 70,565 | 56,267 |
| Land, development and construction | 63,098 | 38,091 |
| Commercial loans | 21,615 | 13,257 |
| | _____ | _____ |
| Total commercial lending | 155,278 | 107,615 |
| | _____ | _____ |
| Consumer loans | 557 | 657 |
| | _____ | _____ |
| Total loans | 688,968 | 529,627 |
| | _____ | _____ |
| Add (deduct): | | |
| Allowance for loan losses | (4,326) | (3,835) |
| Net premiums, discounts, deferred fees and costs | 4,374 | 3,524 |
| Undisbursed portion of loans in process | (64,897) | (7,985) |
| | _____ | _____ |
| Loans, net | \$ 624,119 | \$ 521,331 |
| | _____ | _____ |

(1) Includes \$613,000 and \$1,628,000 of loans held for sale at Sept. 30, 2005 and December 31, 2004, respectively.

(continued)

FEDERAL TRUST CORPORATION AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements (Unaudited), Continued

(2) Loans, Continued

The following is a summary of information regarding nonaccrual and impaired loans (in thousands):

| | At | |
|---|------------------|----------------------|
| | Sept 30, 2005 | December 31, 2004 |
| Nonaccrual loans | \$ 2,354 | \$ 2,600 |
| Accruing loans past due ninety days or more | \$ | \$ |
| Recorded investment in impaired loans for which there is a related allowance for loan losses | \$ 2,354 | \$ 2,648 |
| Recorded investment in impaired loans for which there is no related allowance for loan losses | \$ | \$ |
| Allowance for loan losses related to impaired loans | \$ 357 | \$ 290 |

| | Three Months Ended Sept 30, | | Nine Months Ended Sept 30, | |
|---|--------------------------------|----------|-------------------------------|----------|
| | 2005 | 2004 | 2005 | 2004 |
| Interest income recognized and received on impaired loans | \$ 18 | \$ 34 | \$ 111 | \$ 110 |
| Average net recorded investment in impaired loans | \$ 2,254 | \$ 4,129 | \$ 2,285 | \$ 4,714 |

The activity in the allowance for loan losses is as follows (in thousands):

| | Three Months Ended Sept 30, | | Nine Months Ended Sept 30, | |
|--------------------------------|--------------------------------|----------|-------------------------------|----------|
| | 2005 | 2004 | 2005 | 2004 |
| Balance at beginning of period | \$ 4,126 | \$ 3,390 | \$ 3,835 | \$ 2,779 |
| Provision for loan losses | 200 | 150 | 500 | 850 |
| Charge-offs | | (24) | (10) | (108) |
| Recoveries | | 1 | 1 | 5 |
| Balance at end of period | \$ 4,326 | \$ 3,526 | \$ 4,326 | \$ 3,526 |

A provision for loan losses is charged to earnings based upon management's evaluation of the potential losses in its loan portfolio. During the three- and nine-month periods ended September 30, 2005, management made provisions of \$200,000 and \$500,000, respectively, based on its evaluation of the loan portfolio, as compared to the provisions of \$150,000 and \$850,000, respectively, made in the comparable periods in 2004. The decrease in the provision for the nine months ended September 30, 2005 as compared to the first nine months of 2004 is primarily a result of the reduction in non-accrual loans in 2005. At September 30, 2005, management believes that the allowance is adequate, primarily as a result of the overall quality and the high percentage of residential single family home loans in the portfolio.

FEDERAL TRUST CORPORATION AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements (Unaudited), Continued

(3) Regulatory Capital

The Bank is 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 financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of the Bank's assets, liabilities and certain off-balance-sheet items as calculated under regulatory accounting practices. The Bank's 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 Bank to maintain minimum amounts and percentages (set forth in the table below) of total and Tier I capital (as defined in the regulations) to risk-weighted assets and Tier I capital to average adjusted assets (as defined in the regulations). Management believes, as of September 30, 2005, that the Bank exceeds the minimum capital adequacy requirements to which it is subject.

In addition, as of September 30, 2005, the Bank met the requirements to be categorized as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, the Bank must maintain total risk-based capital, Tier I risk-based and Tier I leverage capital percentages as set forth in the table. There are no conditions or events since September 30, 2005, that management believes would change the institution's categorization as well capitalized. The following table summarizes the capital thresholds for each prompt corrective action capital category. A financial institution's capital category is based on whether it meets the threshold for all three capital ratios within the category. The Bank's actual capital amounts and percentages are also presented in the table (\$ in thousands).

| | Actual | | For Capital Adequacy Purposes | | To Be Well Capitalized Under Prompt Corrective Action Provisions | |
|---|-----------|-------|-------------------------------|------|--|-------|
| | Amount | % | Amount | % | Amount | % |
| <i>At September 30, 2005:</i> | | | | | | |
| Total capital (to risk-weighted assets) | \$ 51,625 | 10.9% | \$ 37,933 | 8.0% | \$ 47,416 | 10.0% |
| Tier I capital (to risk-weighted assets) | 47,309 | 10.0% | 18,967 | 4.0% | 28,450 | 6.0% |
| Tier I capital (to average adjusted assets) | 47,309 | 6.6% | 28,555 | 4.0% | 35,694 | 5.0% |

(continued)

FEDERAL TRUST CORPORATION AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements (Unaudited), Continued

(4) Earnings Per Share of Common Stock

The Company follows the provisions of Financial Accounting Standards No. 128, Earnings Per Share (SFAS No. 128). SFAS No. 128 provides accounting and reporting standards for calculating earnings per share. Basic earnings per share of common stock, has been computed by dividing the net earnings for the period by the weighted-average number of shares outstanding. Shares of common stock purchased by the Company's Employee Stock Ownership Plan (ESOP) are considered outstanding when the shares are allocated to participants. Diluted earnings per share is computed by dividing net earnings by the weighted-average number of shares outstanding including the dilutive effect of stock options computed using the treasury stock method. The following table presents the calculation of basic and diluted earnings per share of common stock (in thousands, except per share amounts):

| | Three Months Ended Sept 30, | | Nine Months Ended Sept 30, | |
|--|--------------------------------|--------|-------------------------------|--------|
| | 2005 | 2004 | 2005 | 2004 |
| Weighted-average shares outstanding before adjustment for unallocated ESOP shares | 8,299 | 7,453 | 8,162 | 6,929 |
| Adjustment to reflect the effect of unallocated ESOP shares | (82) | (131) | (105) | (132) |
| Weighted-average shares outstanding for basic earnings per share | 8,217 | 7,322 | 8,057 | 6,797 |
| Basic earnings per share | \$.11 | \$.13 | \$.41 | \$.38 |
| Total weighted-average shares outstanding for basic earnings per share computation | 8,217 | 7,322 | 8,057 | 6,797 |
| Additional dilutive shares using the average market value for the period utilizing the treasury stock method regarding stock options | 135 | 164 | 119 | 162 |
| Weighted-average shares and equivalents outstanding for diluted earnings per share | 8,352 | 7,486 | 8,176 | 6,959 |
| Diluted earnings per share | \$.11 | \$.13 | \$.40 | \$.37 |

(continued)

FEDERAL TRUST CORPORATION AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements (Unaudited), Continued

(5) Stock Compensation Plans

The Company has three stock options plans. The Key Employee Stock Compensation Program (the Employee Plan) is authorized to issue up to 10% of the issued shares up to a maximum of 1,000,000 shares (after being amended at the 2004 Annual Meeting of Shareholders) through the exercise of incentive stock options, compensatory stock options, stock appreciation rights or performance shares. To date, all awards granted under the Employee Plan have been incentive stock options. These options have either five or ten year terms and are vested immediately, or over various terms up to five years. At September 30, 2005, the Company had 267,642 options available for future grants under the Employee Plan.

The 1998 Directors Stock Option Plan (the 1998 Director Plan) approved by the shareholders on May 22, 1998, is authorized to issue up to 140,000 shares. All options granted under the 1998 Director Plan have ten year terms, vest immediately and are not exercisable for a period of six months after the grant date. As of December 31, 2003, all of the allocated options in the 1998 Director Plan had been granted.

At the 2005 Annual Meeting held on May 27, 2005, the shareholders approved the 2005 Directors Stock Plan (2005 Directors Plan), which is authorized to issue up to 90,000 shares. Awards made under the 2005 Directors Plan may be in the form of restricted shares, stock units, or stock options. A stock unit is the right to receive a share of common stock on a date elected by the director. While any stock unit is outstanding the director holding the stock unit will be entitled to receive a dividend in the form of additional stock units, if cash dividends are declared on outstanding shares of common stock. Each stock unit, including fractional stock units, will be converted to one share of common stock on the date which has been selected by the director. Awards of shares or stock units may be awarded to a director as an annual stock retainer, which is dependent upon the amount of the director's annual cash retainer. The 2005 Directors Plan also provides for discretionary awards of restricted shares, stock units or stock options, which may be granted by the Board to recognize additional services provided to the Company. Any stock options granted may not be exercisable for less than fair market value per share on the date of grant, and must be exercised at least 6 months from the date of grant and before the earlier of 10 years after the date of the award, or one year from the date the director's service is terminated by reason of retirement or death. Restricted Stock Units for 6,827 shares were awarded to two Directors under the 2005 Directors Plan. The closing price of the Company's stock on the date of the grant was \$12.03 per share. Under the terms of their respective Agreements, which will be executed at the November Board meeting, the awards vest over three years (in near equal installments), unless there is a change in the control, at which point the awards vest immediately. As a Restricted Stock Unit, no shares will be physically issued on vested units until the Director no longer serves on the Board. The table below reflects the Restricted Stock Unit awards.

A summary of stock option transactions follows (\$ in thousands, except per share data):

| | Number of Options | Range of Per Share Option Price | Aggregate Option Price |
|---|-------------------------|---------------------------------------|------------------------------|
| Options Granted Under the Employee Plan: | | | |
| Outstanding at December 31, 2003 | 377,418 | \$4.00-7.62 | \$ 1,933 |
| Options granted | 3,000 | 7.62 | 23 |
| Options exercised | (6) | 4.00 | |
| Options forfeited | (36) | 4.00 | |
| Outstanding at December 31, 2004 | 380,376 | 4.00-7.62 | 1,956 |
| Options granted | 114,173 | 10.12-12.00 | 1,235 |
| Options exercised | (164,393) | 4.00-7.62 | (664) |
| Options forfeited | (10,046) | 4.00-10.25 | (103) |
| Outstanding at September 30, 2005 | 320,110 | \$4.00-12.00 | \$ 2,424 |

(continued)

FEDERAL TRUST CORPORATION AND SUBSIDIARIES

(5) Stock Compensation Plans, Continued

| | Number of Options | Range of Per Share Option Price | Aggregate Option Price |
|---|--------------------------------|---------------------------------------|------------------------------|
| <i>Options Granted Under the Director Plan:</i> | | | |
| Outstanding at December 31, 2003 and 2004 | 140,000 | \$4.00-7.62 | \$ 694 |
| Options exercised | (73,137) | \$4.00-7.62 | (327) |
| | <hr/> | | <hr/> |
| Outstanding at September 30, 2005 | 66,863 | \$4.00-7.62 | \$ 367 |
| | <hr/> | | <hr/> |
| | Number of Units | | |
| | <hr/> | | |
| <i>Restricted Stock Units under the Director Plan:</i> | | | |
| Units awarded | 6,827 | | |
| | <hr/> | | |
| Outstanding at September 30, 2005 | 6,827 | | |
| | <hr/> | | |

Statement of Financial Accounting Standards No. 123, *Accounting for Stock Based Compensation*, as amended by SFAS No. 148 *Accounting for Stock Based Compensation Transition and Disclosure*, (SFAS No. 123) requires pro forma fair value disclosures if the intrinsic value method is being utilized to calculate the fair value of options. For purposes of pro forma disclosures, the estimated fair value is included in expense in the period vesting occurs. The proforma information has been determined using the Black-Scholes Model as if the Company had accounted for its stock options under the fair value method of SFAS No. 123. The Company accounts for its stock option plans under the recognition and measurement principles of Accounting Principles Board Opinion No. 25. No stock-based employee compensation cost is reflected in net earnings, as all stock options granted under the plans had an exercise price equal to the market value of the underlying common stock on the date of grant.

(continued)

FEDERAL TRUST CORPORATION AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements (Unaudited), Continued

(5) Stock Compensation Plans, Continued

The following table illustrates assumptions used in calculating the grant-date fair value and the effect on net earnings and basic and diluted earnings per share as if the Company had applied the fair value recognition provisions of SFAS No. 123 to stock-based employee compensation (\$ in thousands, except per share amounts):

| | Three Months Ended Sept 30, | | Nine Months Ended Sept 30, | |
|---|--------------------------------|--------|-------------------------------|----------|
| | 2005 | 2004 | 2005 | 2004 |
| Assumptions for grants made during the period: | | | | |
| Weighted-average risk-free rate of return | 4.17 | N/A | 4.24% | 4.68% |
| Annualized dividend yield | 1.00% | N/A | 1.11% | 1.05% |
| Expected life of options granted | 3 years | N/A | 3 years | 10 years |
| Expected stock volatility | 20% | N/A | 20% | 20% |
| Number of options granted during the period | 41,100 | | 114,173 | 3,000 |
| Grant-date fair value of options issued during the period | \$ 86 | \$ | \$ 263 | \$ 8 |
| Grant-date fair value per option of options issued during the period | \$ 2.10 | \$ | \$ 2.53 | \$ 2.68 |
| Net earnings, as reported | \$ 884 | \$ 954 | \$ 3,270 | \$ 2,602 |
| Deduct: Total stock-based employee compensation determined under the fair value based method for all awards, net of related tax benefit | (35) | (45) | (258) | (135) |
| Proforma net earnings | \$ 849 | \$ 909 | \$ 3,012 | \$ 2,467 |
| Basic earnings per share: | | | | |
| As reported | \$.11 | \$.13 | \$.41 | \$.38 |
| Proforma | \$.10 | \$.12 | \$.37 | \$.36 |
| Diluted earnings per share: | | | | |
| As reported | \$.11 | \$.13 | \$.40 | \$.37 |
| Proforma | \$.10 | \$.12 | \$.37 | \$.35 |

(6) Reclassifications

Certain amounts in 2004 condensed consolidated financial statements have been reclassified to conform to the presentation for 2005.

FEDERAL TRUST CORPORATION AND SUBSIDIARIES

Review by Independent Registered Public Accounting Firm

Hacker, Johnson & Smith PA, the Company's independent registered public accounting firm, have made a limited review of the financial data as of September 30, 2005, and for the three- and nine-month periods ended September 30, 2005 and 2004 presented in this document, in accordance with standards established by the Public Company Accounting Oversight Board (United States).

Their report furnished pursuant to Article 10 of Regulation S-X is included herein.

Report of Independent Registered Public Accounting Firm

Federal Trust Corporation
Sanford, Florida:

We have reviewed the accompanying condensed consolidated balance sheet of Federal Trust Corporation and Subsidiaries (the Company) as of September 30, 2005, the related condensed consolidated statements of earnings for the three- and nine-month periods ended September 30, 2005 and 2004 and the related condensed consolidated statements of stockholders' equity and cash flows for the nine-month periods ended September 30, 2005 and 2004. These interim financial statements are the responsibility of the Company's management.

We conducted our reviews in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our reviews, we are not aware of any material modifications that should be made to the accompanying interim financial statements for them to be in conformity with U.S. generally accepted accounting principles.

We have previously audited, in accordance with the standards of the Public Company Accounting Oversight Board, (United States) the consolidated balance sheet as of December 31, 2004, and the related consolidated statements of earnings, stockholders' equity and cash flows for the year then ended (not presented herein); and in our report dated March 15, 2005 we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet as of December 31, 2004, is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

/s/ Hacker, Johnson & Smith PA

HACKER, JOHNSON & SMITH PA
Orlando, Florida
November 1, 2005

FEDERAL TRUST CORPORATION AND SUBSIDIARIES

**Item 2. Management's Discussion and Analysis of
Financial Condition and Results of Operations**

Comparison of September 30, 2005 and December 31, 2004

General

Federal Trust Corporation (Federal Trust) is the sole shareholder of Federal Trust Bank (the Bank). Federal Trust operates as a unitary savings and loan holding company. Federal Trust's business activities primarily include the operation of the Bank. The Bank is federally-chartered as a stock savings bank and the Bank's deposits are insured up to the applicable limits by the Federal Deposit Insurance Corporation. The Bank provides a wide range of banking services to individual and corporate customers through its six offices located in Orange, Seminole and Volusia counties, Florida. Federal Trust Mortgage Company (the Mortgage Company), a wholly-owned subsidiary of Federal Trust, was established in May 2005 to generate residential loans for the Bank, to close mortgage loans on behalf of certain third party purchasers, and to sell mortgage loans in the secondary market. Federal Trust, the Bank and the Mortgage Company are collectively referred to herein as the Company.

Forward Looking Statements

Readers should note, in particular, that this document contains forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act), that involve substantial risks and uncertainties. When used in this document, or in the documents incorporated by reference herein, the words anticipate, believe, estimate, may, intend and expect and similar expressions identify certain of such forward-looking statements. Actual results, performance or achievements could differ materially from those contemplated, expressed or implied by the forward-looking statements contained herein. Actual results may differ materially, depending upon a variety of important factors, including competition, inflation, general economic conditions, changes in interest rates and changes in the value of collateral securing loans we have made, among other things.

Capital Resources

During the nine months ended September 30, 2005, the Company's primary source of funds consisted of net increases in deposits of \$45.1 million and Federal Home Loan Bank advances of \$65.5 million and net principal repayments and sales of loans of \$58.3 million and securities available for sale of \$13.0 million. The Company used its capital resources principally to purchase loans of \$154.8 million and securities available for sale of \$17.4 million.

Off-Balance Sheet Arrangements

The Company is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit, unused lines of credit, standby letters of credit and loans in process. These instruments involve, to varying degrees, elements of credit and interest-rate risk in excess of the amounts recognized in the condensed consolidated balance sheet. The contract amounts of those instruments reflect the extent of the Company's involvement in particular classes of financial instruments.

FEDERAL TRUST CORPORATION AND SUBSIDIARIES**Item 2. Management's Discussion and Analysis
of Financial Condition and Results of Operations, Continued**

The Company's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit, unused lines of credit and loans in process is represented by the contractual amount of those instruments. The Company uses the same credit policies in making commitments as it does for on-balance sheet instruments.

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

Standby letters of credit are conditional 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 loans to customers.

The following is a summary of the amounts of the Company's financial instruments, with off-balance sheet risk at September 30, 2005 (in thousands):

| | Contract Amount |
|------------------------------|----------------------------|
| Commitments to extend credit | \$ 13,015 |
| Unused lines of credit | \$ 12,302 |
| Standby letters of credit | \$ 2,708 |
| Loans in process | \$ 64,897 |

Management believes the Company has adequate resources to fund all its commitments. At September 30, 2005, the Company had approximately \$252 million in time deposits maturing in one year or less. Management also believes that, if so desired, it can adjust the rates on time deposits to retain or obtain new deposits in a changing interest rate environment.

Management believes the Bank was in compliance with all minimum capital requirements, which it was subject to at September 30, 2005. See note 3 to the condensed consolidated financial statements.

Management is not aware of any trends, demands, commitments or uncertainties which are expected to have a material impact on future operating results, liquidity or capital resources.

FEDERAL TRUST CORPORATION AND SUBSIDIARIES

Results of Operations

The following table sets forth, for the periods indicated, information regarding: (i) the total dollar amount of interest income of the Company from interest-earning assets and the resultant average yields; (ii) the total dollar amount of interest expense on interest-bearing liabilities and the resultant average costs; (iii) net interest/dividend income; (iv) interest-rate spread; and (v) net interest margin.

Three Months Ended September 30,

| | 2005 | | | 2004 | | |
|--|-------------------|--------------|---------------------|-------------------|--------------|---------------------|
| | Average Balance | Interest | Average Yield/ Cost | Average Balance | Interest | Average Yield/ Cost |
| (\$ in thousands) | | | | | | |
| Interest-earning assets: | | | | | | |
| Loans (1) | \$ 596,749 | \$ 7,788 | 5.22% | \$ 455,671 | \$ 5,683 | 4.99% |
| Securities | 45,333 | 510 | 4.50 | 36,219 | 334 | 3.69 |
| Other interest-earning assets (2) | 12,073 | 113 | 3.74 | 7,844 | 71 | 3.62 |
| Total interest-earning assets | 654,155 | 8,411 | 5.14 | 499,734 | 6,088 | 4.87 |
| Noninterest-earning assets | 42,922 | | | 32,771 | | |
| Total assets | \$ 697,077 | | | \$ 532,505 | | |
| Interest-bearing liabilities: | | | | | | |
| Noninterest-bearing demand deposits | \$ 16,075 | | | \$ 11,036 | | |
| Interest-bearing demand and money- market deposits | 126,702 | 938 | 2.96 | 115,274 | 529 | 1.84 |
| Savings deposits | 4,832 | 17 | 1.41 | 7,181 | 26 | 1.45 |
| Time deposits | 291,531 | 2,412 | 3.31 | 227,412 | 1,346 | 2.37 |
| Total deposits | 439,140 | 3,367 | 3.07 | 360,903 | 1,901 | 2.11 |
| Other borrowings (3) | 182,490 | 1,828 | 4.01 | 132,007 | 812 | 2.46 |
| Total interest-bearing liabilities | 621,630 | 5,195 | 3.34 | 492,910 | 2,713 | 2.20 |
| Noninterest-bearing liabilities | 34,396 | | | 6,472 | | |
| Stockholders equity | 41,051 | | | 33,123 | | |
| Total liabilities and stockholders equity | \$ 697,077 | | | \$ 532,505 | | |
| Net interest income | | \$ 3,216 | | | \$ 3,375 | |
| Interest-rate spread (4) | | | 1.80% | | | 2.67% |
| Net interest margin (5) | | | 1.97% | | | 2.70% |
| Ratio of average interest-earning assets to average interest-bearing liabilities | 1.05 | | | 1.01 | | |

-
- (1) Includes nonaccrual loans.
 - (2) Includes Federal Home Loan Bank stock and interest-earning deposits.
 - (3) Includes Federal Home Loan Bank advances, other borrowings, junior subordinated debentures and capital lease obligation.
 - (4) Interest-rate spread represents the difference between the average yield on interest-earning assets and the average cost of interest-bearing liabilities.
 - (5) Net interest margin is annualized net interest income divided by average interest-earning assets.

FEDERAL TRUST CORPORATION AND SUBSIDIARIES

The following table sets forth, for the periods indicated, information regarding (i) the total dollar amount of interest and dividend income of the Company from interest-earning assets and the resultant average yields; (ii) the total dollar amount of interest expense on interest-bearing liabilities and the resultant average costs; (iii) net interest/dividend income; (iv) interest-rate spread; and (v) net interest margin.

Nine Months Ended September 30,

| | 2005 | | | 2004 | | |
|--|-------------------|------------------------|-------------|-------------------|------------------------|-------------|
| | Average Balance | Average Yield/Interest | Cost | Average Balance | Average Yield/Interest | Cost |
| (\$ in thousands) | | | | | | |
| Interest-earning assets: | | | | | | |
| Loans (1) | \$ 563,359 | \$ 22,082 | 5.23% | \$ 429,018 | \$ 16,362 | 5.09% |
| Securities | 44,851 | 1,450 | 4.31 | 34,899 | 914 | 3.49 |
| Other interest-earning assets (2) | 11,031 | 350 | 4.23 | 7,179 | 196 | 3.64 |
| Total interest-earning assets | 619,241 | 23,882 | 5.14 | 471,096 | 17,472 | 4.95 |
| Noninterest-earning assets | 35,786 | | | 32,255 | | |
| Total assets | \$ 655,027 | | | \$ 503,351 | | |
| Interest-bearing liabilities: | | | | | | |
| Noninterest-bearing demand deposits | \$ 14,847 | | | \$ 10,408 | | |
| Interest-bearing demand and money- market deposits | 126,944 | 2,510 | 2.64 | 104,831 | 1,400 | 1.78 |
| Savings deposits | 5,392 | 55 | 1.36 | 7,890 | 87 | 1.47 |
| Time deposits | 271,805 | 6,077 | 2.98 | 220,990 | 3,829 | 2.31 |
| Total deposits | 418,988 | 8,642 | 2.75 | 344,119 | 5,316 | 2.06 |
| Other borrowings (3) | 179,712 | 4,695 | 3.48 | 125,537 | 2,307 | 2.45 |
| Total interest-bearing liabilities | 598,700 | 13,337 | 2.97 | 469,656 | 7,623 | 2.16 |
| Noninterest-bearing liabilities | 15,504 | | | 4,717 | | |
| Stockholders equity | 40,823 | | | 28,978 | | |
| Total liabilities and stockholders equity | \$ 655,027 | | | \$ 503,351 | | |
| Net interest income | | \$ 10,545 | | | \$ 9,849 | |
| Interest-rate spread (4) | | | 2.17% | | | 2.79% |
| Net interest margin (5) | | | 2.27% | | | 2.79% |
| Ratio of average interest-earning assets to average interest-bearing liabilities | 1.03 | | | 1.00 | | |

(1) Includes non-accrual loans.

(2) Includes Federal Home Loan Bank stock and interest-earning deposits.

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- (3) Includes Federal Home Loan Bank advances, other borrowings, junior subordinated debentures and capital lease obligation.
- (4) Interest-rate spread represents the difference between the average yield on interest-earning assets and the average cost of interest-bearing liabilities.
- (5) Net interest margin is annualized net interest income divided by average interest-earning assets.

FEDERAL TRUST CORPORATION AND SUBSIDIARIES

Comparison of the Three-Month Periods Ended September 30, 2005 and 2004

General. The Company had net earnings for the three-month period ended September 30, 2005, of \$884,000 or \$.11 per basic and diluted share, compared to \$954,000 or \$.13 per basic and diluted share for the same period in 2004. The \$70,000 decrease in net earnings was primarily due to a \$159,000 decrease in net interest income and a \$50,000 increase in the provision for loan losses, partially offset by a \$133,000 decrease in other expenses.

Interest Income. Interest income increased by \$2.3 million or 38% to \$8.4 million for the three-month period ended September 30, 2005, from \$6.1 million for the same period in 2004. Interest income on loans increased \$2.1 million to \$7.8 million in 2005, primarily as a result of an increase in the average amount of loans outstanding from \$455.7 million in 2004 to \$596.7 million in 2005, together with an increase in the average yield earned on loans from 4.99% for the three-month period ended September 30, 2004, to 5.22% for the comparable period in 2005. Interest income on securities increased by \$176,000 for the three-months ended September 30, 2005, over the same period in 2004 due to a \$9.1 million increase in the average balance and an .81% increase in the average yield of the portfolio. Management expects the rates earned on the portfolio to fluctuate with general market conditions.

Also affecting interest income for the current quarter was a non-recurring \$421,000 adjustment to interest income on loans, which reduced net earnings by \$.03 per share for third quarter of 2005. The adjustment relates to interest recognized on various pools of loans purchased over the past few years, which are serviced by the financial institutions that sold us the loans. Our monthly interest accruals are based on the due dates reported to us from the various financial institutions. In a number of cases it was discovered that the reported due dates were not correct and the accrued interest was overstated. This additional income had been recorded in the period when each pool was originally purchased. Management has determined that the effect on individual prior periods was not significant and therefore did not consider it necessary to restate prior period earnings, electing to record the entire adjustment in the 2005 third quarter.

Interest Expense. Interest expense increased by \$2.5 million or 91% during the three-month period ended September 30, 2005, compared to the same period in 2004. Interest on deposits increased \$1.5 million or 77% to \$3.4 million in 2005 from \$1.9 million in 2004. The increase in interest on deposits was a result of an increase in the average cost of deposits from 2.11% for the three-month period ended September 30, 2004, to 3.07% for the comparable period in 2005, coupled with an increase in average deposits outstanding from \$360.9 million in 2004 to \$439.1 million in 2005. Interest on other borrowings increased to \$1.8 million in 2005 from \$812,000 in 2004, primarily as a result of an increase in the average amount of other borrowings outstanding from \$132.0 million to \$182.5 million. Management expects to continue to use FHLB advances and other borrowings as a liability management tool. Rates paid on transaction and money market deposit accounts as well as short-term FHLB advances will fluctuate with the movement of market interest rates.

Provision for Loan Losses. A provision for loan losses is charged to earnings based upon management's evaluation of the losses in its loan portfolio. During the quarter ended September 30, 2005, a \$200,000 provision for loan losses was recorded based on management's evaluation of the loan portfolio, which was an increase of \$50,000 from the same period in 2004. The allowance for loan losses at September 30, 2005, was \$4.3 million or .69% of total loans outstanding, versus \$3.8 million at December 31, 2004, or .74% of total loans outstanding. Management believes the allowance for loan losses at September 30, 2005 is adequate.

(continued)

FEDERAL TRUST CORPORATION AND SUBSIDIARIES

Comparison of the Three-Month Periods Ended September 30, 2005 and 2004, continued

Other Income. Other income decreased \$33,000 or 5% from \$680,000 for the three-month period ended September 30, 2004, to \$647,000 for the same period in 2005. The decrease was primarily in the gain on sales of loans held for sale, which were \$100,000 lower in 2005 than 2004, partially offset by a \$64,000 increase in the net gains on sales of securities available for sale.

Other Expenses. Other expenses decreased \$133,000 or 5% to \$2.3 million for the three-month period ended September 30, 2005, from \$2.5 million for the same period in 2004. Salaries and employee benefits decreased \$29,000 and other expenses decreased \$117,000 from 2004 to 2005.

Income Taxes. Income taxes for the three months ended September 30, 2005, was \$452,000 (an effective rate of 33.8%), compared to \$491,000 (an effective rate of 34.0%) for the same period in 2004.

Comparison of the Nine-Month Periods Ended September 30, 2005 and 2004

General. The Company had net earnings for the nine-month period ended September 30, 2005, of \$3.3 million or \$.41 per basic share and \$.40 per diluted share, compared to \$2.6 million or \$.38 per basic and \$.37 diluted share for the same period in 2004. The increase in net earnings for the nine-month period was primarily due to increases in net interest income and other income plus a decrease in the provision for loan losses, partially offset by an increase in other expenses.

Interest Income. Interest income increased by \$6.4 million or 37% to \$23.9 million for the nine-month period ended September 30, 2005, from \$17.5 million for the same period in 2004. Interest income on loans increased \$5.7 million or 35% to \$22.1 million in 2005 from \$16.4 million in 2004, primarily as a result of an increase in the average amount of loans outstanding from \$429.0 million in 2004 to \$563.4 million in 2005 and an increase in the average yield earned on loans from 5.09% for the nine-month period ended September 30, 2004, to 5.23% for the comparable period in 2005. Interest income on securities increased by \$536,000 for the nine-month period ended September 30, 2005, over the same period in 2004, primarily as a result of an increase in the average balance of securities owned and an increase in the average yield. Management expects the rates earned on the portfolio to fluctuate with general market conditions.

Interest Expense. Interest expense increased by \$5.7 million or 75% during the nine-month period ended September 30, 2005, compared to the same period in 2004. Interest on deposits increased \$3.3 million or 63% to \$8.6 million in 2005 from \$5.3 million in 2004, as a result of an increase in the average cost of deposits from 2.06% for the nine-month period ended September 30, 2004, to 2.75% for the comparable period in 2005 and an increase in average deposits outstanding from \$344.1 million in 2004 to \$419.0 million in 2005. Interest on other borrowings increased to \$4.7 million in 2005 from \$2.3 million in 2004, primarily as a result of the increase in the average balance of other borrowings from \$125.5 million for the nine-month period ended September 30, 2004 to \$179.7 million for the comparable 2005 period and an increase in the average rate paid on other borrowings from 2.45% in 2004 to 3.48% in 2005. Management expects to continue to use FHLB advances and other borrowings as a liability management tool.

Provision for Loan Losses. A provision for loan losses is charged to earnings based upon management's evaluation of the losses in its loan portfolio. During the nine months ended September 30, 2005, a \$500,000 provision for loan losses was recorded based on management's evaluation of the loan portfolio, which was a decrease of \$350,000 from the same period in 2004, primarily as a result of the decrease in nonaccrual loans. The allowance for loan losses at September 30, 2005, was \$4.3 million or .69% of total loans outstanding, versus \$3.8 million at December 31, 2004, or .74% of total loans outstanding. Management believes the allowance for loan losses at September 30, 2005, is adequate.

(continued)

FEDERAL TRUST CORPORATION AND SUBSIDIARIES

Comparison of the Nine-Month Periods Ended September 30, 2005 and 2004, continued

Other Income. Other income increased \$114,000 or 6% from the nine-month period ended September 30, 2004, to the same period in 2005. The increase in other income was primarily due to an increase of \$148,000 in the net gain on sales of securities available for sale.

Other Expense. Other expense was virtually unchanged at \$7.1 million for the nine-month periods ended September 30, 2005 and 2004. Salary and employee benefits increased \$70,000 and occupancy expense increased \$56,000 due to the staffing and opening of the branch in Deltona, Florida in the second half of 2004 and the overall growth of the Company. The increases in personnel and occupancy expenses were offset by a \$167,000 decrease in other expenses.

Income Taxes. Income taxes for the nine months ended September 30, 2005, was \$1,763,000 (an effective rate of 35.0%), compared to \$1,287,000 (an effective rate of 33.1%) for the same period in 2004.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Market risk is the risk of loss from adverse changes in market prices and rates. The Company's market risk arises primarily from interest-rate risk inherent in its lending, investment and deposit taking activities. The Company has little or no risk related to trading accounts, commodities or foreign exchange.

Management actively monitors and manages its interest-rate risk exposure. The primary objective in managing interest rate risk is to limit, within established guidelines, the adverse impact of changes in interest rates on the Company's net interest income and capital, while adjusting the Company's asset-liability structure to obtain the maximum yield-cost spread on that structure. Management relies primarily on its asset-liability structure to control interest rate risk. However, a sudden and substantial increase in interest rates could adversely impact the Company's earnings, to the extent that the interest rates borne by assets and liabilities do not change at the same speed, to the same extent, or on the same basis. There has been no significant change in the Company's market risk exposure since December 31, 2004.

Item 4. Controls and Procedures

- a. *Evaluation of Disclosure Controls and Procedures.* The Company maintains controls and procedures designed to ensure that information required to be disclosed in the reports that the Company files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the Securities and Exchange Commission. Based upon their evaluation of those controls and procedures performed within 90 days of the filing date of this report, the Chief Executive and Chief Financial Officers of the Company concluded that the Company's disclosure controls and procedures were adequate.
- b. *Changes in Internal Controls.* The Company made no significant changes in its internal controls or in other factors that could significantly affect these controls subsequent to the date of the evaluation of those controls by the Chief Executive and Chief Financial Officers.

FEDERAL TRUST CORPORATION AND SUBSIDIARIES

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

There are no material pending legal proceedings to which Federal Trust Corporation or its subsidiaries are a party, or to which any of their property is subject.

Item 5. Other Information

Federal Trust Corporation (*FTC*) has entered into a new Employment Agreement (*Employment Agreement*) with Chief Executive Officer and President James V. Suskiewich and an Employee Severance Agreement (*Severance Agreement*) with Thomas P. Spatola, the President and Chief Operating Officer of its wholly-owned mortgage company subsidiary, Federal Trust Mortgage Company (*FTMC*). The following is a summary of the terms of the Employment Agreement and the Severance Agreement.

Suskiewich Agreement - On September 29, 2005, *FTC*'s Compensation Committee terminated the employment agreement dated December 18, 1998 (with amendments) by and among *FTC*, Federal Trust Bank, and James V. Suskiewich, and on that same date, Mr. Suskiewich agreed to enter into the new Employment Agreement with *FTC*, which became effective October 1, 2005.

Mr. Suskiewich's new Employment Agreement has significant changes in comparison to the terms of his prior Employment Agreement. Pursuant to its terms, Mr. Suskiewich is to receive his current base salary of \$325,000 (which shall be reevaluated on an annual basis), plus reimbursement of reasonable business expenses. He is also entitled to five weeks paid vacation and is provided with the use of an automobile. In addition, Mr. Suskiewich has a target performance bonus opportunity of 40% of his base salary. The target performance bonus is comprised of three components, which are measured on a separate basis. *FTC*'s Compensation Committee establishes the performance criteria measures at the beginning of each fiscal year. The criteria established for 2006 are quarterly return on assets (37.5%), quarterly net income growth (37.5%), and performance based on defined management objectives (discretionary, up to 25%). The performance bonus is evaluated and paid within 30 days after the release of each quarter's financial statements. In addition, he is eligible to participate in any bonus and incentive programs adopted by *FTC* for its employees.

The original term of the Employment Agreement is three years. As with his prior employment agreement, each day during the term of the Employment Agreement, it automatically renews for one additional day. Therefore, at all times, Mr. Suskiewich's Employment Agreement has a three-year term, until December 31, 2008, which is the last permitted daily renewal date. Mr. Suskiewich's prior employment agreement was automatically renewed until his 65th birthday. The Board is required to meet at least once annually to consider the continuation of the automatic renewals. Any party to the Employment Agreement may cease the automatic renewals, however, by notifying the other party of their intent to not renew. In addition, any party may terminate the Employment Agreement by delivering to the other party a written notice of termination. The date of termination may not be less than 30 days nor more than 45 days after delivery of the notice.

In the event the Employment Agreement is terminated by *FTC* for reasons other than cause or by Mr. Suskiewich for good reason, (as those terms are defined therein) he shall be entitled to a severance payment and to the continuation of benefits for the remaining term of the Employment Agreement.

The severance payment would be equal to his total annual base salary for the remainder of the term of the Employment Agreement (but in no event for a period of less than six months), and would be payable in semi-monthly installments until paid in full.

(continued)

FEDERAL TRUST CORPORATION AND SUBSIDIARIES

PART II. OTHER INFORMATION, continued

In the event of a change in control of FTC, Mr. Suskiewich will be entitled to severance equal to two and a half times his base annual salary and last fiscal year bonus. This severance amount was reduced from the maximum of 2.9 times his total compensation that was provided for in his prior employment agreement. As with his prior employment agreement, Mr. Suskiewich will be entitled to a change-in-control performance bonus. This amount, however, has also been reduced to three times the premium multiple paid for FTC over book value times \$250,000. Furthermore, the Employment Agreement includes a gross up payment clause. In the event severance payments received by Mr. Suskiewich are subject to federal excise taxes under Section 4999 of the Internal Revenue Code of 1986, FTC shall increase Mr. Suskiewich's severance payment so that the excise tax payable and any additional income taxes incurred on the gross-up payment will be apportioned 75% to FTC and 25% to Mr. Suskiewich. The prior employment agreement provided for a 100% gross-up payment by FTC.

The Employment Agreement has a six month non-compete provision, whereby Mr. Suskiewich may not become employed with another financial institution within Seminole County, Florida or any other county in which Federal Trust Bank has a branch office. His prior employment agreement provided for a six month non-compete also, but limited the geographic scope to within 100 miles of FTC's principal office.

Similar to the provisions in Mr. Suskiewich's prior employment agreement, the current Employment Agreement provides for salary continuation in the event of his termination due to retirement, disability, or a change of control of FTC. Such salary continuation provides for differing levels of annual benefits to be paid for life and would be funded by Bank Owned Life Insurance Policies. Likewise, as in the prior Employment Agreement, the Employment Agreement permits Mr. Suskiewich to terminate his employment voluntarily and for FTC to terminate it for cause, as defined in the Employment Agreement. In the event of termination for those reasons, all rights and benefits under the Employment Agreement shall immediately terminate upon the effective date of such termination.

Spatola Agreement - FTC entered into the Severance Agreement with Thomas P. Spatola, the President and Chief Operating Officer of Federal Trust Mortgage Company, on June 13, 2005. The initial term of the Severance Agreement is for two years, subject to additional one year renewals at the discretion of the Board. The Board reviews the Severance Agreement at the end of each fiscal year to determine such renewals.

The Severance Agreement provides for a severance payment in the amount of two times Mr. Spatola's highest annual base salary (within the three years prior to termination) in the event Mr. Spatola's employment is terminated by FTC without cause or by Mr. Spatola for any reason, following a change in control (as defined in the Agreement) of FTC. This severance payment is to be paid in one lump sum payment within 30 days of the termination. In addition, Mr. Spatola would be entitled to continuation of his life, health, and disability coverages until the earlier of his obtaining new employment with similar coverage or one year from the date of termination.

During the term of the Severance Agreement and for a period of three months following his termination for any reason, other than a change in control, Mr. Spatola may not become employed with another financial institution in either Seminole County or Orange County, Florida. The Severance Agreement does not under any circumstances constitute an employment contract, and as such FTC may terminate his employment at any time, for any reason.

(continued)

FEDERAL TRUST CORPORATION AND SUBSIDIARIES

PART II. OTHER INFORMATION, continued

Item 6. Exhibits

(a) Exhibits. The following exhibits are filed with or incorporated by reference into this report. The exhibits which are marked by a (1) were previously filed as a part of, and are hereby incorporated by reference from Registrant's Registration Statement on form SB-1, as effective with the Securities and Exchange Commission (SEC) on October 7, 1997, Registration No. 333-30883. The exhibits which are marked by a (2) were previously filed with the SEC, and are hereby incorporated by reference from Registrant's 1998 Definitive Proxy Statement. The exhibits which are marked with a (3) were previously filed with the SEC, and are hereby incorporated by reference from Registrant's 1999 Definitive Proxy Statement. The exhibits which are marked with a (4) were previously filed with the SEC, and are hereby incorporated by reference from Registrant's 2001 Definitive Proxy Statement. The exhibits which are marked with a (5) were previously filed with the SEC, and are hereby incorporated by reference from Registrant's 1999 Form 10-KSB. The exhibits which are marked with a (6) were previously filed with the SEC and are hereby incorporated by reference from the Registrant's 2004 Form 10-KSB. The exhibit numbers correspond to the exhibit numbers in the referenced documents. The exhibits which are marked with a (7) were previously filed with the SEC, and are hereby incorporated by reference from Registrant's 2005 Definitive Proxy Statement.

| Exhibit No. | Description of Exhibit |
|-------------|---|
| (1) 3.1 | 1996 Amended Articles of Incorporation and the 1995 Amended and Restated Articles of Incorporation of Federal Trust |
| (1) 3.2 | 1995 Amended and Restated Bylaws of Federal Trust |
| (2) 3.3 | 1998 Articles of Amendment to Articles of Incorporation of Federal Trust |
| (3) 3.4 | 1999 Articles of Amendment to Articles of Incorporation of Federal Trust |
| (1) 4.0 | Specimen of Common Stock Certificate |
| (4) 10.1 | Amended Employment Agreement By and Among Federal Trust, the Bank and James V. Suskiewich |
| (4) 10.2 | First Amendment to the Amended Employment Agreement By and Among Federal Trust, the Bank and James V. Suskiewich |
| (6) 10.3 | Employee Severance Agreement with Stephen C. Green |
| (5) 10.4 | Amendment to Federal Trust 1998 Key Employee Stock Compensation Program |
| (5) 10.5 | Amendment to Federal Trust 1998 Directors' Stock Option Plan |
| (6) 10.6 | Employee Severance Agreement with Gregory E. Smith |
| (6) 10.7 | Employee Severance Agreement with Daniel C. Roberts |
| (6) 10.8 | Employee Severance Agreement with Jennifer B. Brodnax |
| (7) 10.9 | 2005 Directors' Stock Plan |
| 10.10 | Employment Agreement by and between Federal Trust Corporation and James V. Suskiewich |
| 10.11 | Employee Severance Agreement with Thomas P. Spatola |
| (6) 14.1 | Code of Ethical Conduct |
| 31.1 | Certification of Chief Executive Officer, pursuant to Rule 13a-14(a) |
| 31.2 | Certification of Chief Financial Officer, pursuant to Rule 13a-14(a) |
| 32.1 | Certification of Chief Executive Officer, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 |
| 32.2 | Certification of Chief Financial Officer, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |

FEDERAL TRUST CORPORATION AND SUBSIDIARIES

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

FEDERAL TRUST CORPORATION
(Registrant)

Date: November 4, 2005

By: /s/ James V. Suskiewich

James V. Suskiewich
President and Chief Executive Officer

Date: November 4, 2005

By: /s/ Gregory E. Smith

Gregory E. Smith
Executive Vice President and
Chief Financial Officer