HERITAGE COMMERCE CORP
Form DEF 14A
April 06, 2007

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

SCHEDULE 14A
(RULE 14A-101)
INFORMATION REQUIRED IN PROXY STATEMENT

Proxy Statement Pursuant to Section 14(a) of
the Securities Exchange Act of 1934 (Amendment No.)

Filed by the Registrant x
Filed by a Party other than the Registrant o
Check the appropriate box:

o	Preliminary Proxy Statement
o	**Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))**
x	Definitive Proxy Statement
o	Definitive Additional Materials
o	Soliciting Material Pursuant to §240.14a-12

HERITAGE COMMERCE CORP
(Name of Registrant as Specified In Its Charter)

(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

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x	No fee required.	
o	Fee computed on table below per Exchange Act Rules 14a-6(i)(1) and 0-11.	
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o	Fee paid previously with preliminary materials.	
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HERITAGE COMMERCE CORP

April 6, 2007

Dear Shareholder:

We are pleased to enclose our 2006 Annual Report on Form 10-K, Notice of 2007 Annual Meeting, Proxy Statement and Form of Proxy.

You are cordially invited to attend the 2007 Annual Meeting of Shareholders, which will be held at 1:00 p.m. on Thursday, May 24, 2007, at Heritage Commerce Corp's offices, located at 150 Almaden Boulevard, San Jose, California, 95113.

The accompanying Notice of Annual Meeting and Proxy Statement provide information pertaining to the matters to be considered and acted upon at the Meeting.

Your continued support is appreciated and we hope you will attend the Annual Meeting. Whether or not you are personally present, it is very important that your shares be represented at the Meeting. Accordingly, please sign, date, and mail the enclosed proxy card promptly. If you wish to vote in accordance with the Board of Directors' recommendations, it is not necessary to specify your choices. You may simply sign, date and return the enclosed proxy card. You may also vote by the internet or telephone by following the instructions on the enclosed proxy card.

Sincerely,

/s/ Jack W. Conner	/s/ Walter T. Kaczmarek
Jack W. Conner	Walter T. Kaczmarek
Chairman of the Board	*President and Chief Executive Officer*

150 Almaden Boulevard, San Jose, California 95113 • Telephone (408) 947-6900 • Fax (408) 947-6910

HERITAGE COMMERCE CORP
Notice of Annual Meeting of Shareholders

The Annual Meeting of Shareholders of Heritage Commerce Corp ("Commerce Corp") will be held at Commerce Corp's offices, located at 150 Almaden Boulevard, San Jose, California 95113 on May 24, 2007, at 1:00 p.m., for the following purposes:

1. To elect the Board of Directors of Commerce Corp for terms expiring at the 2008 Annual Meeting of Shareholders;
2. To consider and transact such other business as may properly be brought before the meeting.

Shareholders of record at the close of business on March 28, 2007 are entitled to notice of and to vote at the meeting.

Provisions of the Bylaws of Commerce Corp govern nominations for election of members of the Board of Directors, as follows:

Nomination for election of directors may be made by the Board of Directors or by any holder of any outstanding class of capital stock of the Corporation entitled to vote for the election of directors. Notice of intention to make any nominations shall be made in writing and shall be delivered or mailed to the President of Commerce Corp not less than 21 days, nor more than 60 days prior to any meeting of shareholders called for the election of directors; provided, however, that if less than 21 days' notice is given to shareholders, such notice of intention to nominate shall be mailed or delivered to the President of Commerce Corp not later than the close of business on the tenth day following the day on which the notice of such meeting is sent by third class mail (if permitted by law), no notice of intention to make nominations shall be required. Such notification shall contain the following information to the extent known to the notifying shareholder: (i) the name and address of each proposed nominee; (ii) the principal occupation of each proposed nominee; (iii) the number of shares of capital stock of Commerce Corp owned by each proposed nominee; (iv) the name and residence address of the notifying shareholder; (v) the number of shares of capital stock of Commerce Corp owned by the notifying shareholder; (vi) the number of shares of capital stock of any bank, bank holding company, savings and loan association or other depository institution owned beneficially by the nominee or by the notifying shareholder and the identities and locations of any such institutions; (vii) whether the proposed nominee has ever been convicted of or pleaded nolo contendere to any criminal offense involving dishonesty or breach of trust, filed a petition in bankruptcy or been adjudged bankrupt; and (viii) a statement regarding the nominee's compliance with Section 2.3 of the Bylaws.

Nominees for the Board of Directors must meet certain qualifications set forth in Section 2.3 of Commerce Corp's Bylaws, which prohibit the election as a director of any person who is a director, executive officer, branch manager or trustee for any unaffiliated commercial bank, savings bank, trust company, savings and loan association, building and loan association, industrial bank or credit union that is engaged in business in (i) any city, town or village in which Commerce Corp or any affiliate or subsidiary thereof has offices, or (ii) any city, town or village adjacent to a city, town or village in which Commerce Corp or any affiliate or subsidiary thereof has offices.

All shareholders are cordially invited to attend the meeting in person. To ensure your representation at the meeting, you are requested to date, execute and return the enclosed proxy card, without delay, in the enclosed postage-paid envelope whether or not you plan to attend the meeting. Any shareholder present at the meeting may vote personally on all matters brought before the meeting. If you elect to vote personally at the meeting, your proxy will not be used.

BY ORDER OF THE BOARD OF DIRECTORS

/s/ Rebecca A. Levey
Rebecca A. Levey
Corporate Secretary
April 6, 2007

San Jose, California

WHETHER OR NOT YOU PLAN TO ATTEND THIS MEETING, PLEASE SIGN AND RETURN THE ENCLOSED PROXY AS PROMPTLY AS POSSIBLE IN THE ENCLOSED POSTAGE-PAID ENVELOPE.

PROXY STATEMENT
OF
HERITAGE COMMERCE CORP

150 Almaden Boulevard • San Jose, California 95113
Telephone (408) 947-6900 • Fax (408) 947-6910

This statement is furnished in connection with the solicitation of proxies to be used by the Board of Directors of Heritage Commerce Corp ("Commerce Corp") at the Annual Meeting of Shareholders of Commerce Corp to be held at Commerce Corp's offices, 150 Almaden Boulevard, San Jose, California, on May 24, 2007, at 1:00 p.m., and at any adjournments or postponements thereof (the "Meeting").

This Proxy Statement and the accompanying form of proxy are being mailed to shareholders on or about April 6, 2007.

The enclosed proxy is being solicited by Commerce Corp's Board of Directors and the cost of the solicitation is being borne by Commerce Corp. The principal solicitation of proxies is being made by mail, although additional solicitation may be made by telephone, email, facsimile or personal visits by directors, officers and employees of Commerce Corp and its subsidiary bank.

PURPOSE OF THE MEETING

The Meeting is being held for the following purposes:

1. To elect the Board of Directors of Commerce Corp for a term expiring at the 2008 Annual Meeting of Shareholders.
2. To consider and transact such other business as may properly be brought before the meeting.

VOTING SECURITIES

Only shareholders of record of our common stock as of March 28, 2007 will be entitled to vote at the Annual Meeting. On March 28, 2007, there were 11,632,828 outstanding shares of common stock, which constituted all of the outstanding voting securities of Commerce Corp.

The presence at the meeting, in person or by proxy, of a majority of the shares of the common stock issued and outstanding on March 28, 2007, will constitute a quorum. Abstentions and broker non-votes (proxies submitted by brokers that do not indicate a vote for a proposal because they do not have discretionary voting authority and have not received instructions as to how to vote on a proposal) are counted as present in determining whether the quorum requirement is satisfied. However, broker non-votes will not be counted in determining the number of shares necessary for approval of any proposal.

All shares represented by each properly executed, unrevoked proxy received by us prior to the vote will be voted in the manner specified. If the manner of voting is not specified, the proxy will be voted FOR election of the Board of Directors nominees named herein. If any other matters are properly presented at the Annual Meeting for consideration, including, among other things, consideration of a motion to adjourn the Annual Meeting to another time or place, the persons named in the proxy will have discretion to vote on these matters in accordance with their best judgment.

You may revoke your proxy at any time before it is actually voted at the meeting by:

- delivering written notice of revocation to our Corporate Secretary at our executive offices as identified in this proxy statement;
- submitting a later dated proxy; or
- attending the meeting and voting in person.

Your attendance at the meeting will not, by itself, constitute revocation of your proxy. You may also be represented by another person present at the meeting by executing a form of proxy designating that person to act on your behalf. Shares may only be voted by or on behalf of the record holder of shares as indicated in our stock transfer records. If you are a beneficial stockholder but your shares are held of record by another person, such as a stock brokerage firm or bank, that person must vote the shares as the record holder.

For the election of directors, a shareholder may withhold authority for the proxy holders to vote for any one or more of the nominees identified herein by so indicating on the enclosed proxy in the manner instructed on the proxy card. Unless authority to vote for the nominees is so withheld, the proxy holders will vote the proxies received by them for the election of the nominees identified herein as directors of Commerce Corp. Proxy holders do not have an obligation to vote for nominees not identified on the preprinted card (that is, write-in candidates). Should any shareholder attempt to "write in" a vote for a nominee not identified on the preprinted card (and described in these proxy materials), the proxy holders will NOT vote the shares represented by that proxy for any such write-in candidate, but will instead vote the shares for any and all other validly indicated candidates. If any of the nominees should be unable or decline to serve, which is not now anticipated, the proxy holders shall have discretionary authority to vote for a substitute who shall be designated by the present Board of Directors to fill the vacancy. In the event that additional persons are nominated for election as directors, the proxy holders intend to vote all of the proxies received by them in such a manner, in accordance with the cumulative voting, as will assure the election of as many of the nominees identified herein as possible. In such event, the specific nominees to be voted for will be determined by the proxy holders, in their sole discretion.

For the election of directors, California law provides that a shareholder of a California corporation, or his/her proxy, may cumulate votes in the election of directors. That is, each shareholder may cast that number of votes equal to the number of shares owned by him/her, multiplied by the number of directors to be elected, and he/she may cumulate such votes for a single candidate or distribute such votes among as many candidates as he/she deems appropriate.

Certain affirmative steps must be taken by the shareholders of Commerce Corp in order to be entitled to vote their shares cumulatively in the election of directors. At the shareholders' meeting at which directors are to be elected, no shareholder shall be entitled to cumulate votes (i.e., cast for any one or more candidates a number of votes greater than the number of the shareholder's shares) unless the candidates' names have been placed in nomination prior to the commencement of the voting and at least one shareholder has given notice prior to commencement of the voting of the shareholder's intention to cumulate votes. If any shareholder has given such notice, then every shareholder entitled to vote may cumulate votes for candidates in nomination and give one candidate a number of votes equal to the number of directors to be elected multiplied by the number of votes to which that shareholder's shares are entitled, or distribute the shareholder's votes on the same principle among any or all of the candidates, as the shareholder thinks appropriate. The candidates receiving the highest number of votes, up to the number of directors to be elected, shall be elected.

It is intended that shares represented by proxies in the accompanying form will be voted for the election of persons nominated by management. Although the Board of Directors does not know whether there will be any nominations for directors other than those nominated by management, as set forth below, if any such nomination is made, or if votes are cast for any candidates other than those nominated by the Board of Directors, the persons authorized to vote shares represented by executed proxies in the enclosed form (if authority to vote for the election of directors or for any particular nominee is not withheld) will have full discretion and authority to vote cumulatively and allocate votes among any or all of the nominees of the Board of Directors in such order and in such number as they may determine in their sole discretion, provided all the above-listed requirements are met.

CORPORATE GOVERNANCE

Board of Directors

Annual Meeting Attendance

All directors are expected to attend each annual meeting of Commerce Corp's shareholders, unless attendance is prevented by an emergency. All of Commerce Corp's directors who were in office at that time attended Commerce Corp's 2006 annual meeting of shareholders with the exception of Jack L. Peckham.

Board Independence

Each of the following members of our Board of Directors has been determined by the Board to be independent under the rules of NASDAQ governing the independence of directors, as follows:

Frank G. Bisceglia
James R. Blair
Jack W. Conner
Robert T. Moles
Louis ("Lon") O. Normandin
Jack L. Peckham
Humphrey P. Polanen
Charles J. Toeniskoetter
Ranson W. Webster

Therefore, a majority of the directors are independent, as required by the rules of NASDAQ.

Contacting the Board

Shareholders may address inquiries to any of Commerce Corp's directors or the full Board by writing to the Corporate Secretary, Heritage Commerce Corp, 150 Almaden Boulevard, San Jose, California 95113-9940. Each communication from a shareholder should include the following information in order to permit shareholder status to be confirmed and to provide an address to forward a response if deemed appropriate:

- The name, mailing address and telephone number of the shareholder sending the communication;

- If the shareholder is not a record holder of our common stock, the name of the record holder of our common stock beneficially owned must be identified along with the shareholder.

Our Corporate Secretary will forward all appropriate communications to the Board or individual members of the Board specified in the communication. Our Corporate Secretary may (but is not required to) review all correspondence addressed to the Board or any individual member of the Board, for any inappropriate correspondence more suitably directed to management. Communications may be deemed inappropriate for this purpose if it is reasonably apparent from the face of the correspondence that it relates principally to a customer dispute. Our policies regarding the handling of security holder communications were approved by a majority of our independent directors.

Nomination of Directors

Commerce Corp has a Corporate Governance and Nominating Committee. The duties of the Corporate Governance and Nominating Committee include the recommendation of candidates for election to Commerce Corp's Board of Directors.

The Corporate Governance and Nominating Committee's minimum qualifications for a director are persons of high ethical character and who have both personal and professional integrity, which are consistent with the image and values of Commerce Corp. In addition, Section 2.3 of Commerce Corp's Bylaws provides that no person shall be a member of the Board of Directors who is a director, executive officer, branch manager or trustee for any unaffiliated commercial bank, savings bank, trust company, savings and loan association, building and loan association, industrial bank or credit union that is engaged in business in (i) any city, town or village in which the corporation or any affiliate or subsidiary thereof has offices, or (ii) any city, town or village adjacent to a city, town or village in which the corporation or any affiliate or subsidiary thereof has offices. The Corporate Governance and Nominating Committee also considers some or all of the following criteria in considering candidates to serve as directors:

· commitment to ethical conduct and personal and professional integrity as evidenced through the person's business associations, service as a director or executive officer or other commitment to ethical conduct and personal and professional integrity as evidenced organizations and/or education;

· objective perspective and mature judgment developed through business experiences and/or educational endeavors;

· the candidate's ability to work with other members of the Board of Directors and management to further our goals and increase stockholder value; the ability and commitment to devote sufficient time to carry out the duties and responsibilities as a director;

· demonstrated experience at policy making levels in various organizations and in areas that are relevant to our activities;

· the skills and experience of the potential nominee in relation to the capabilities already present on the Board of Directors; and

· such other attributes, including independence, relevant in constituting a board that also satisfies the requirements imposed by the SEC and the NASDAQ Stock Market.

The Corporate Governance and Nominating Committee does not have a separate policy for consideration of any director candidates recommended by shareholders. Instead, the Corporate Governance and Nominating Committee considers any candidate meeting the requirements for nomination by a shareholder set forth in Commerce Corp's Bylaws (as well as applicable laws and regulations) in the same manner as any other director candidate. The Corporate Governance and Nominating Committee believes that requiring shareholder recommendations for director candidates to comply with the requirements for nominations in accordance with Commerce Corp's Bylaws ensures that the Corporate Governance and Nominating Committee receives at least the minimum information necessary for it to begin an appropriate evaluation of any such director nominee.

Commerce Corp will consider director nominees recommended by shareholders who adhere to the following procedure. Commerce Corp's Bylaws provide that any shareholder must give written notice to the President of Commerce Corp of an intention to nominate a director at a shareholder meeting. Generally, notice of intention to make any nominations shall be made in writing and must be delivered or mailed to the President of Commerce Corp not less than 21 days nor more than 60 days prior to any meeting of shareholders called for the election of directors. Nominees for the Board of Directors must meet the qualifications set forth in Section 2.3 of Commerce Corp's Bylaws as noted above. The Bylaws contain additional requirements for nominations. A copy of the requirements is available upon request directed to the Corporate Secretary, Heritage Commerce Corp, 150 Almaden Boulevard, San Jose, California 95113-9940.

The Corporate Governance and Nominating Committee's goal is to recommend candidates for the Board of Directors that bring a variety of perspectives and skill derived from high quality business and professional experience. Each candidate should be prepared to represent the best interests of all shareholders and not just one particular constituency or interest group.

Commerce Corp identifies new director candidates through recommendations from existing directors and through other business associates of Commerce Corp and considers nominees of shareholders in the same manner as other nominees.

Code of Ethics

Commerce Corp has adopted an Executive and Principal Financial Officers Code of Ethics governing the conduct of its Chief Executive Officer, Chief Financial Officer, and Controller. Commerce Corp has posted the Executive and Principal Financial Officers Code of Ethics on its website and it may be accessed at the following address: http://www.heritagecommercecorp.com. Also, Commerce Corp has adopted a separate Code of Ethics which governs the conduct of all directors, officers and employees and which also may be accessed at the internet address referenced above.

ELECTION OF DIRECTORS

The Bylaws of Commerce Corp provide that the number of directors shall not be less than 11 nor more than 21. By resolution, the Board of Directors has fixed the number of directors at 11. The Bylaws of Commerce Corp provide the procedure for nominations and election of the Board of Directors. This procedure is printed in full in the Notice of Annual Meeting of Shareholders accompanying this Proxy Statement. Nominations not made in accordance with the procedures may be disregarded by the Chairman of the Meeting, and upon his instructions, the Inspector of Election shall disregard all votes cast for such nominees.

The Board of Directors, upon recommendation of the Corporate Governance and Nominating Committee, has nominated eleven persons for election at the 2007 Annual Meeting. Each of the nominees is currently a director of Commerce Corp serving a one year term that expires at the 2007 Annual Meeting. The Commerce Corp Corporate Governance and Nominating Committee and the Board of Directors have nominated the following persons to serve on the Board of Directors. If any nominee should become unable or unwilling to serve as a director, the proxies will be voted at the Meeting for such substitute nominees as shall be designated by the Board. The Board presently has no knowledge that any of the nominees will be unable or unwilling to serve.

The following table provides information with respect to each person nominated and recommended to be elected by the Board of Directors.

Name	Age	PositionWith CommerceCorp	Director Since	Principal Occupation, Business Experience During Past Five Years and Other Information
Frank G. Bisceglia	61	Director	1994	Senior Vice President - Investments, Advisory and Brokerage Services, Senior Portfolio Manager, Portfolio Management Program at UBS Financial Services, Inc., a full service securities firm.
James R. Blair	62	Director	1994	President of Renco Properties, Inc., a real estate development company. CFO and Director of San Jose Jet Center, a full service FBO Company at San Jose International Airport.
Jack W. Conner	67	Chairman of the Board	2004	Elected Chairman of the Board in July, 2006. Chairman and CEO of Comerica California from 1991 until his retirement in 1998 and continued as a Director at Comerica California until 2002; Founder, President and Director of Plaza Bank of

				Commerce from 1979 to 1991.
William J. Del Biaggio, Jr.	66	Founding Chairman of the Board and Executive Vice President	1994	Elected Founding Chairman of the Board and Executive Vice President in July, 2006 and prior thereto served as Chairman of the Board from 2004; Interim Chief Executive Officer of Commerce Corp from 2004 to 2005; Business Development Officer of Heritage Commerce Corp since 2002.
Walter T. Kaczmarek	55	President, CEO and Director	2005	Heritage Commerce Corp CEO and director since March, 2005. Executive Vice President of Comerica Bank from 2002 to 2005. Held various other positions with Comerica Bank and Plaza Bank of Commerce from 1990 to 2002. Prior thereto served in various positions with Union Bank of California and The Martin Group, a real estate investment-development company.

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Robert T. Moles	52	Director	2004	Chairman of Intero Real Estate Services, Inc., a full-service real estate firm, since 2002. Prior to joining Intero, served as President and CEO of the Real Estate Franchise Group of Cendant Corporation, the largest franchiser of residential and commercial real estate brokerage offices in the world. Prior to joining Cendant, served as President & CEO of Contempo Realty, Inc. in Santa Clara, California.
Louis ("Lon") O. Normandin	72	Director	1994	Owner and Chairman of the Board of Normandin Chrysler Jeep. President and CEO of the Catholic Foundation of Santa Clara County since 2004. Trustee and Chairman of the Board of Regents at Bellarmine College Preparatory since 2005.
Jack L. Peckham	65	Director	1994	CEO of Elastic Workspace Software, Inc. since January 2003; President and CEO of Alpine Microsystems since November 2001; President and CEO of Timpani Networks, Inc. from 1999 to 2002; President and CEO of Lightspeed Semiconductor from 1998 to 2000; Vice President and General Manager of Atmel Corporation, a semiconductor

				manufacturing company, from 1985 to 1998.
Humphrey P. Polanen	57	Director	1994	CEO of Sandhill IT Security Acquisition Corp, a publicly listed company, since 2004. Managing Director of Internet Venture Partners BV, an investment firm, from 2000 to 2004; President and CEO of Trustworks Systems, a network security company, from 1998 to 1999; General Manager of Network Security Products and Internet Commerce Groups, Sun Microsystems, a computer systems company, from 1995 to 1998.
Charles J. Toeniskoetter	62	Director	2002	Chairman of Toeniskoetter & Breeding, Inc., Development, a Silicon Valley real estate development and investment company. Chairman of TBI Construction & Construction Management, Inc., a Silicon Valley commercial construction company. Member of the Board of Directors of Redwood Trust, Inc. and SJW Corp. (Both are listed on the New York Stock Exchange).
Ranson W. Webster	62	Director	2004	Founded Computing Resources, Inc. (“CRI”) in 1978, a privately held general purpose service bureau specializing in automating accounting functions. In 1999 CRI merged with Intuit, Inc., the maker of QuickBooks and Quicken financial software. In 1998 founded Evergreen Capital, LLC, an early stage investment company focused on Internet and biotech companies.

There are no family relationships among the Commerce Corp’s Executive Officers, or Director Nominees.

RECOMMENDATION OF THE BOARD OF DIRECTORS

THE PROXY HOLDERS INTEND TO VOTE ALL PROXIES THEY HOLD IN FAVOR OF ELECTION OF EACH OF THE NOMINEES. IF NO INSTRUCTION IS GIVEN, THE PROXY HOLDERS INTEND TO VOTE FOR EACH NOMINEE LISTED.

EXECUTIVE OFFICERS OF HERITAGE COMMERCE CORP

Set forth below is certain information with respect to the Executive Officers of Commerce Corp:

Name	Age	Position
William J. Del Biaggio, Jr.	66	Executive Vice President and Founding Chairman of the Board
Richard Hagarty	54	Executive Vice President and Chief Credit Officer
Walter T. Kaczmarek	55	President and Chief Executive Officer
Lawrence D. McGovern	52	Executive Vice President and Chief Financial Officer
Raymond Parker	57	Executive Vice President/Banking Division Heritage Bank of Commerce

Lawrence D. McGovern has served as Executive Vice President and Chief Financial Officer of Commerce Corp since July, 1998.

Richard Hagarty was promoted to Executive Vice President and Chief Credit Officer in July, 2006. Mr. Hagarty has served on the credit administration team for Heritage Bank of Commerce for almost 10 years. He has extensive experience in the greater Silicon Valley banking community. Prior to joining the bank, he worked for Greater Bay Bank, California Business Bank, San Jose National Bank and Crocker National Bank. A native of San Mateo, California, Hagarty earned a Bachelor of Arts Degree from the University of San Francisco.

Raymond Parker has served as Executive Vice President of Heritage Bank of Commerce since May, 2005. From January, 2005 until joining Heritage Bank of Commerce, Mr. Parker served as a Consultant, and then a Director, to Exadel, Inc. From February, 2000 through May, 2002, Mr. Parker served as the President and Chief Executive Officer of Loan Excel, Inc. From 1974 through 1999, he was employed in various capacities by Union Bank of California including Executive Vice President of the commercial banking group.

Biographical information for William J. Del Biaggio, Jr. and Walter T. Kaczmarek are found under "Election of Directors."

SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The following table sets forth information as of February 15, 2007 pertaining to beneficial ownership of Commerce Corp's common stock by persons known to Commerce Corp to own five percent or more of Commerce Corp's common stock, current directors of Commerce Corp, nominees to be elected to the Board of Directors, the officers named in the Summary Compensation Table presented in this Proxy Statement and all directors and officers of Commerce Corp as a group. This information has been obtained from Commerce Corp's records, or from information furnished directly by the individual or entity to Commerce Corp.

For purposes of the following table, shares issuable pursuant to stock options which may be exercised within 60 days of February 15, 2007 are deemed to be issued and outstanding and have been treated as outstanding in determining the amount and nature of beneficial ownership and in calculating the percentage of ownership of those individuals possessing such interest, but not for any other individuals.

Name of Beneficial Owner [1]	**Position**	**Shares Beneficially Owned** [2][3]	**Exercisable Options**	**Percent of Class**[3]
Frank G. Bisceglia	Director	117,904[4]	24,109	1.01%
James R. Blair	Director	67,605[5]	9,259	0.58%
Jack W. Conner	Director and Chairman of the Board	14,382	6,382	0.12%
William J. Del Biaggio, Jr.	Executive Vice President, Director and Founding Chairman	154,210[6]	24,495	1.32%
Richard Hagarty	Chief Credit Officer of Heritage Bank of Commerce	12,884[7]	10,542	0.11%
Walter T. Kaczmarek	President, CEO and Director	90,530[8]	29,530	0.77%
Lawrence D. McGovern	Executive Vice President & CFO	64,675[9]	63,025	0.55%
Robert T. Moles	Director	84,965[10]	6,382	0.73%
Louis ("Lon") O. Normandin	Director	129,364[11]	654	1.11%
Raymond Parker	Executive Vice President/Banking Division Heritage Bank of Commerce	17,187	16,187	0.15%
Jack Peckham	Director	136,043[12]	24,109	1.16%
Humphrey P. Polanen	Director	32,547[13]	19,159	0.28%
Charles J. Toeniskoetter	Director	30,923[14]	16,759	0.26%
Ransom W. Webster	Director	439,316	7,173	3.77%
All directors and executive officers (14 individuals)		1,392,535	257,765	11.69%
OZ Management L.L.C. [15]		701,879	0	6.02%

1. The address for all persons is c/o Heritage Commerce Corp, 150 Almaden Boulevard, San Jose, California, 95113.
2. Subject to applicable community property laws and shared voting and investment power with a spouse, the persons listed have sole voting and investment power with respect to such shares unless otherwise noted. Listed amounts reflect all previous stock splits and stock dividends.
3. Includes shares beneficially owned (including options exercisable within 60 days of February 15, 2007, as shown in the "Exercisable Options" column), both directly and indirectly together with associates.
4. Includes 4,286 shares held as trustee of the Edith Lico Simoni Trust, 79,009 shares as one of two trustees of the Bisceglia Family Trust, and 10,500 shares held in a personal Individual Retirement Account
5. Includes 31,102 shares held in a personal Individual Retirement Account, and 27,244 shares held as trustee for the Blair Family Trust.
6.

Includes 74,999 shares held in a personal Individual Retirement Account, 49,000 shares held as one of two trustees of the Del Biaggio Family Trust, and 5,716 shares held in the name of Helen N. Del Biaggio, his spouse.

7. Includes 2,342 shares held in a personal Individual Retirement Account.

8. Includes 51,000 shares held by Mr. Kaczmarek and 10,000 shares held in a personal Individual Retirement Account. Mr. Kaczmarek was awarded 51,000 restricted shares of Commerce Corp common stock pursuant to the terms of a Restricted Stock Agreement, dated March 17, 2005. Under the terms of the Restricted Stock Agreement, the restricted shares will vest 25% per year at the end of years three, four, five and six, provided Mr. Kaczmarek is still with Commerce Corp, subject to accelerated vesting upon termination, termination by Mr. Kaczmarek for (as defined by his employment agreement), death or disability. Mr. Kaczmarek has the right to vote the shares prior to the time they vest.

9. Includes 1,650 shares held in a personal Individual Retirement Account.

10. Includes 18,295 shares held by Mr. Moles' spouse.

11. Includes 128,710 shares as trustee of the Louis and Margaret Normandin Trust.

12. Includes 111,934 shares as one of two trustees for the Peckham Revocable Trust.

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13. Includes 12,765 shares held in a personal Individual Retirement Account and 623 shares held by Azieb Nicodimos, his spouse.

14. Includes 150 shares held by Linda O. Toeniskoetter, Mr. Toeniskoetter's spouse, and 12,764 shares in the Toeniskoetter & Breeding, Inc. Profit Sharing Plan.

15. OZ Management L.L.C., a Delaware limited liability company, is the investment manager for OZ Master Fund and exercises voting and dispositive power over the shares held by OZ Master Fund. Daniel S. Och serves as principal investment manager to a number of investments funds and discretionary accounts to which he has voting and dispositive authority including such an account for OZ Management Master Fund, Ltd. and OZ Management L.L.C. OZ Master Fund holds 667,283 shares. In addition to the 667,283 shares held by OZ Master Fund, OZ Management L.L.C. also has beneficial ownership of 34,596 additional shares. The address for Daniel S. Och and OZ Management L.L.C. is 9 West 57th Street, 39th Floor, New York, NY 10019. The address for OZ Master Fund is Goldman Sachs (Caymen) Trust, Trust, Limited, P.O. Box 896, G.T. Harbour Centre, Second Floor, North Church Street, George Town, Grand Cayman, Cayman Islands. All of the foregoing information has been obtained from Schedule 13/G filed with the SEC on February 14, 2007 by OZ Management L.L.C.

COMMITTEES OF THE BOARD OF DIRECTORS OF HERITAGE COMMERCE CORP

AUDIT COMMITTEE

The members of the Audit Committee in 2006 were Jack W. Conner, Louis (“Lon”) O. Normandin, Jack L. Peckham and Humphrey P. Polanen, Committee Chair. All Audit Committee members are independent as specified by NASDAQ’s listing standards.

The Audit Committee provides oversight of our financial, accounting and reporting process, our system of internal accounting and financial controls, and our compliance with related legal and regulatory requirements, the appointment, engagement, termination and oversight of our independent auditors, including conducting a review of their independence, reviewing and approving the planned scope of our annual audit, overseeing the independent auditor’s work, reviewing and pre-approving any audit and non-audit services that may be performed by them, reviewing with management and our independent auditors the adequacy of our internal financial controls, and reviewing our critical accounting policies and the application of accounting principles. Each member of the Audit Committee meets the independence criteria prescribed by applicable law and the rules of the Securities and Exchange Commission for audit committee membership and is independent within the meaning of the NASDAQ listing standards. Each Audit Committee member meets the NASDAQ’s financial knowledge requirements. The Audit Committee operates pursuant to a written charter, which complies with the applicable provisions of the Sarbanes-Oxley Act of 2002 and the related rules of the SEC and NASDAQ. A copy of the Audit Committee Charter is attached as Exhibit A to this Proxy Statement. The Audit Committee met 6 times during 2006.

Audit Committee Financial Expert

The Board of Directors has determined that Mr. Jack W. Conner has: (i) an understanding of generally accepted accounting principles and financial statements; (ii) the ability to assess the general application of such principles in connection with the accounting for estimates, accruals and reserves; (iii) experience preparing, auditing, analyzing or evaluating financial statements that present a breadth and level of complexity of accounting issues that are generally comparable to the breadth and complexity of issues that can reasonably be expected to be raised by the registrant’s financial statements, or experience actively supervising one or more persons engaged in such activities; (iv) an understanding of internal control over financial reporting; and (v) an understanding of audit committee functions.

Therefore, the Board has determined that Mr. Jack W. Conner meets the definition of “audit committee financial expert” under the rules of the SEC and is “financially sophisticated” under NASDAQ rules. The designation of a person as an audit committee financial expert does not result in the person being deemed an expert for any purpose, including under Section 11 of the Securities Act of 1933. The designation does not impose on the person any duties, obligations or liability greater than those imposed on any other audit committee member or any other director and does not affect the duties, obligations or liability of any other member of the Audit Committee or Board of Directors.

CORPORATE GOVERNANCE AND NOMINATING COMMITTEE

The members of the Corporate Governance and Nominating Committee in 2006 were Robert T. Moles, Louis ("Lon") O. Normandin, Humphrey P. Polanen, Charles J. Toeniskoetter, and Ranson W. Webster, Committee Chair. All Committee members are independent under the rules of NASDAQ.

The principal duties of the Corporate Governance and Nominating Committee are the development of corporate governance principles for Commerce Corp, the establishment of requirements and qualifications for Board membership, and the recommendation of candidates for election to Commerce Corp's Board of Directors. The Corporate Governance and Nominating Committee has a charter which is available on the Commerce Corp website and it may be accessed at the following address: www.heritagecommercecorp.com. The Corporate Governance and Nominating Committee met 4 times during 2006.

COMPENSATION AND BENEFITS COMMITTEE

The members of the Compensation and Benefits Committee in 2006 were Frank G. Bisceglia, Robert T. Moles, Jack L. Peckham, Committee Chair, and Ranson W. Webster. All committee members are independent under the rules of NASDAQ.

The Committee is primarily responsible for determining the compensation of directors, executive officers and other officers of Commerce Corp and Heritage Bank of Commerce. For executive officers and directors, the Committee is responsible for evaluating, reviewing and recommending to the Board compensation levels, equity and non-equity incentive compensation, and performance based compensation plans. The Committee also oversees the Commerce Corp welfare benefit plans, retirement benefit plans, all employment and personnel policies and procedures including employment contracts. The Compensation and Benefits Committee met 6 times during 2006.

LOAN COMMITTEE

The members of the Loan Committee in 2006 were Frank G. Bisceglia, Committee Chair, James R. Blair, Robert T. Moles, Louis ("Lon") O. Normandin, and Charles J. Toeniskoetter. The Loan Committee is responsible for the approval and supervision of loans and the development of Commerce Corp's loan policies and procedures. The Loan Committee met 17 times during 2006.

FINANCE AND INVESTMENT COMMITTEE

The Finance and Investment Committee is responsible for the development of policies and procedures related to liquidity and asset-liability management, supervision of Commerce Corp's investments and preparation of Commerce Corp's annual budget. The Finance and Investment Committee met 12 times during 2006.

The members of the Finance and Investment Committee in 2006 were Frank G. Bisceglia, James R. Blair, Jack W. Conner, Committee Chair, William J. Del Biaggio, Jr. and Walter T. Kaczmarek.

STRATEGIC ISSUES COMMITTEE

The members of the Strategic Issues Committee in 2006 were Jack W. Conner, Walter T. Kaczmarek, Charles J. Toeniskoetter, Committee Chair, and Ranson W. Webster.

The principal duties of the Strategic Issues Committee are to provide oversight and guidance to Senior Management regarding the strategic direction of Commerce Corp, including development of the overall Strategic Business Plan. The Strategic Issues Committee met 2 times during 2006.

DIRECTOR ATTENDANCE AT BOARD MEETINGS

During 2006, Commerce Corp's Board of Directors held twelve regular meetings and one special meeting. Each director attended at least 75 percent of the aggregate of: (1) the total number of meetings of the Board of Directors; and (2) the total number of meetings of Board committees on which that director served.

COMPLIANCE WITH SECTION 16(a) OF THE SECURITIES EXCHANGE ACT OF 1934

Section 16(a) of the Securities Exchange Act of 1934 requires Commerce Corp's directors, executive officers and persons who own more than ten percent of a registered class of Commerce Corp's equity securities, to file with the Securities and Exchange Commission initial reports of ownership and reports of changes in ownership of common stock and other equity securities of Commerce Corp Officers, directors and greater than ten percent shareholders are required by SEC regulations to furnish Commerce Corp with copies of all Section 16(a) forms they file.

To Commerce Corp's knowledge, based solely on review of the copies of such reports furnished to Commerce Corp and written representations that no other reports were required, all Section 16(a) filing requirements applicable to its officers, directors and greater than ten percent beneficial owners were complied with during the year ended December 31, 2006.

TRANSACTIONS WITH MANAGEMENT AND OTHERS

There are no existing or proposed material transactions between Commerce Corp and any of Commerce Corp's directors, executive officers, nominees for election as a director, or the immediate family or associates of any of the foregoing persons.

In 2006, the Commerce Corp Board of Directors adopted a written Statement of Policy with Respect to Related Party Transactions. Under this policy, any "related party transaction" shall be consummated or shall continue only if the board of directors audit committee shall approve or ratify such transaction in accordance with the guidelines set forth in the policy and if the transaction is on terms comparable to those that could be obtained in arm's length dealings with an unrelated third party. For purposes of this policy, a "related person" means: (i) any person who is, or at any time since the beginning of Commerce Corp's last fiscal year was, a director or executive officer of Commerce Corp or a nominee to become a director of Commerce Corp; (ii) any person who is known to be the beneficial owner of more than 5% of any class of Commerce Corp's voting securities; (iii) any immediate family member of any of the foregoing persons, which means any child, stepchild, parent, stepparent, spouse, sibling, mother-in-law, father-in-law, son-in-law, daughter-in-law, brother-in-law, or sister-in-law of the director, executive officer, nominee or more than 5% beneficial owner, and any person (other than a tenant or employee) sharing the household of such director, executive officer, nominee or more than 5% beneficial owner; and (iv) any firm, corporation or other entity in which any of the foregoing persons is employed or is a partner or principal or in a similar position or in which such person has a 10% or greater beneficial ownership interest.

A "related party transaction" is a transaction between Commerce Corp and any related person (including any transactions requiring disclosure under Item 404 of Regulation S-K under the Securities Exchange Act of 1934), other than transactions involving less than $5,000 when aggregated with all similar transactions.

The Board of Directors has determined that the Audit Committee of the Board is best suited to review and approve related party transactions. Accordingly, at each calendar year's first regularly scheduled Audit Committee meeting, management shall recommend related party transactions to be entered into by Commerce Corp for that calendar year, including the proposed aggregate value of such transactions if applicable. After review, the Committee shall approve or disapprove such transactions and at each subsequently scheduled meeting, management shall update the Committee as to any material change to those proposed transactions. The Committee shall consider all of the relevant facts and circumstances available to the Committee, including (if applicable) but not limited to the benefits to Commerce Corp; the impact on a director's independence in the event the related person is a director, an immediate family member of a director or an entity in which a director is a partner, shareholder or executive officer; the availability of other sources for comparable products or services; the terms of the transaction; and the terms available to unrelated third parties or to employees generally. No member of the Audit Committee may participate in any review, consideration or approval of any related person transaction with respect to which such member or any of his or her immediate family members is the related person. The Committee shall approve only those related person transactions that are in, or are not inconsistent with, the best interests of the Company and its stockholders, as the Committee determines in good faith. The Audit Committee, as applicable, shall convey the decision to the Chief Executive Officer, who shall convey the decision to the appropriate persons within the Company. In the event management recommends any further related party transactions subsequent to the first calendar year meeting, such transactions may be presented to the Audit Committee for approval or preliminarily entered into by management subject to ratification by the Audit Committee; provided that if ratification shall not be forthcoming, management shall make all reasonable efforts to cancel or annul such transaction.

INDEBTEDNESS OF MANAGEMENT

Some of Commerce Corp's directors and executive officers, as well as their immediate family and associates, are customers of, and have had banking transactions with, Commerce Corp's subsidiary, Heritage Bank of Commerce (the "Bank"), in the ordinary course of business, and the Bank expects to have such ordinary banking transactions with these persons in the future. In the opinion of the management of Commerce Corp and the Bank, all loans and commitments to lend included in such transactions were made in the ordinary course of business on the same terms, including interest rates and collateral, as those prevailing for comparable transactions with other persons of similar creditworthiness, and do not involve more than the normal risk of collectibility or present other unfavorable features. Loans to individual directors and officers must comply with the Bank's lending policies and statutory lending limits. In addition, prior approval of the Bank's Board of Directors is required for all such loans.

EXECUTIVE COMPENSATION

COMPENSATION DISCUSSION AND ANALYSIS

Overview of Compensation Program

The Compensation Committee (for purposes of this analysis, the "*Committee*") of the Board of Directors has responsibility for establishing, implementing and continually monitoring adherence with the Heritage Commerce Corp ("*Commerce Corp*") compensation philosophy. The Committee ensures that the total compensation paid to executive officers and elected officers is fair, reasonable and competitive. Throughout this proxy statement, the individuals who served as our chief executive officer and chief financial officer during fiscal 2006, as well as the other individuals included in the Summary Compensation Table on page 35, are referred to as the "named executive officers".

Compensation Philosophy

In 2005, the Committee undertook a comprehensive review of Commerce Corp's compensation programs for executive officers, other elected officers, selected staff and the Board of Directors. The Committee engaged the compensation consulting firm of Carl D. Jacobs Group LLC ("Jacobs Group") to assist in formulating an overall compensation strategy. The Committee believes that the most effective executive compensation program is one that is designed to reward the achievement of specific annual, long-term and strategic goals, and which aligns executives' interests with those of the shareholders by rewarding achievement of pre- established performance goals, with the ultimate objective of improving shareholder value.

The Committee evaluates both performance and compensation to ensure that Commerce Corp maintains its ability to attract and retain superior employees in key positions and that compensation provided to key employees remains competitive relative to the compensation paid to similarly situated executives of our peer companies. To that end, the Committee believes executive compensation packages provided by Commerce Corp to its executives, including the named executive officers, should include base salary, variable performance-based cash incentives and stock-based compensation.

We believe our base salaries are competitive. We provide our executives the opportunity to significantly increase their annual cash compensation through our cash incentive program by improving Commerce Corp's performance in each of the relevant financial areas on an annual basis. We also expect that as those improvements are maintained and built upon, Commerce Corp's stock price will reflect these improvements, and we therefore use equity awards to reward the long-term efforts of management. These equity awards serve as additional purpose of increasing the ownership stake of our management in Commerce Corp, further aligning their interests with those of our other shareholders. Compensation decisions are generally made during the first quarter of each fiscal year. Once compensation decisions are made for a fiscal year they are not generally readjusted for the fiscal year.

Compensation Program Objectives and Rewards

Commerce Corp's compensation and benefits programs are driven by our business environment and are designed to enable us to achieve our mission and adhere to company values. The programs' objectives are to:

- Reflect our position as a leading community bank in our service areas;
- Attract, engage and retain the workforce that helps ensure our future success;
- Motivate and inspire employee behavior that fosters a high-performance culture;
- Support a one-company culture;
- Support overall business objectives; and
- Provide shareholders with a superior rate of return.

Consequently the guiding principles of our programs are:

- Promote and maintain a high performance banking organization;
- Remain competitive in our marketplace for talent; and
- Balance our compensation costs with our desire to provide value to our shareholders.

To this end, we will measure success of our programs by:

- Overall business performance and employee engagement;
- Ability to attract and retain key talent;
- Costs and business risks that are limited to levels that maximize return and minimize risk; and
- Employee understanding and perceptions that ensure program value equals or exceeds program cost.

All of our compensation and benefits for our named executive officers described below have as a primary purpose our need to attract, retain and motivate the highly talented individuals who will engage in the behaviors necessary to enable us to succeed in creating shareholder value in a highly competitive marketplace. Beyond that, different elements have specific purposes designed to reward different behaviors.

· *Base salary and benefits* are designed to:

· Reward core competence in the executive role relative to skills, position and contributions to Commerce Corp; and

· Provide fixed cash compensation competitive with the market place merit increases to retain desired competitive position and recognize contribution.

· *Annual incentive variable cash awards* are designed to:

· Focus employees on annual financial objectives derived from the business plan that lead to long-term success;

· Provide annual variable performance-based cash awards that are not subject to the volatility of the stock market to reward and motivate achievement of critical annual performance metrics selected by the Committee; and

· Foster a pay for performance culture that aligns our compensation programs with our overall business strategy.

· *Equity-based compensation awards* are designed to:

· Link compensation rewards to the creation of shareholder wealth;

· Promote teamwork by tying compensation significantly to the value of our common stock;

· Attract the next generation of management by providing significant capital accumulation opportunities;

· Conserve cash outlay through the use of stock based vehicles in addition to cash compensation to reward executives; and

· Retain executives by providing a long term oriented program whose value could only be achieved by remaining with and performing with Commerce Corp.

· A s*upplemental executive retirement plan* facilitates our ability to attract and retain executives, as we compete for talented employees in a marketplace where such retirement programs are commonly offered.

· *Change of control and separation benefits with certain officers:*

· Individual employment contracts with certain executives provide for change of control and separation benefits.

· Separation benefits provide benefits to ease an employee's transition due to an unexpected employment termination by Commerce Corp due to on-going changes in the Commerce Corp's employment needs.

· Change in control benefits encourage key executives to remain focused on the Commerce Corp's business in the event of rumored or actual fundamental corporate changes which will enhance shareholder value.

The use of these programs enables us to reinforce our pay for performance philosophy, as well as strengthen our ability to attract and retain highly qualified executives. We believe that this combination of programs provides an appropriate mix of fixed and variable pay, balances short-term operational performance with long-term shareholder value, and encourages executive recruitment and retention.

Compensation Consultant

In 2005, the Committee retained Jacobs Group as its independent compensation consultant to advise the Compensation Committee on all matters related to the executive compensation. This relationship continued through 2006 into 2007.

Jacobs Group assists the Committee by providing comparative market data on compensation practices and programs based on an analysis of peer competitors. Jacobs Group also provides guidance on industry best practices. From time to time Jacobs Group provides advice to the Committee with respect to reviewing and structuring our policy regarding fees paid to our directors as well as other equity and non-equity compensation awarded to non-management directors, including designing and determining individual grant levels for the 2004 Stock Option Plan.

Compensation Benchmarking Relative to Market

In 2005, Jacobs Group provided the Committee with the survey data to assist in the review and comparison of each element of compensation for executives and the board of directors. The Jacobs Group selected a compensation peer group of companies consisting of 19 publicly-traded banking organizations of similar asset size and business focus, 16 of which were located in California with the majority located in the San Francisco Bay area. The Jacobs Group also reviewed publicly available survey data. Published survey data included California banks located in our service areas as well as local area data drawn from national surveys. The comparative data was used to benchmark executive compensation levels against banks that have executive positions with responsibilities similar in breadth and scope to ours and that compete with us for executive talent. With such information, the Committee reviewed and analyzed compensation for each executive and made adjustments as appropriate. The Jacobs Group updated the comparative data for the board of directors in 2006.

Role of Executive Officers in Compensation Decisions

The chief executive officer annually reviews the performance of each executive officer and elected officer (other than the chief executive officer whose performance is reviewed by the board of directors). The conclusions reached and recommendations based on these reviews, including with respect to salary adjustments and annual incentive cash award amounts, are presented to the Committee. The Committee exercises its discretion in modifying any recommended adjustments or awards to executives, officers and elected officers. The Committee makes all compensation decisions and approves recommendations regarding equity awards to all executive officers (which includes the named executive officers) of Commerce Corp.

The Commerce Corp Compensation Program

Base Salary

The Committee targets the base salary level at the 60th percentile of its comparative data for the base salaries of the chief executive officer and executive officers including the named executive officers. Adjustments to the base salary level may be made based on comparisons to the comparative data and evaluation of the executive's level of responsibility and experience as well as company-wide performance. The Committee also considers the executive's success in achieving business results, promoting our core values and demonstrating leadership. Previous compensation levels and awards are not taken into account in setting base salary, rather the Committee considers appropriate ranges of compensation given the level of position, and performance of the individual and Commerce Corp for the period under consideration.

Base salaries for individual executive officers are compared to the banking industry by reference to comparative data provided by our independent consulting firm. Mr. Kaczmarek's base salary was $300,000 when he first joined Commerce Corp, pursuant to the terms of his employment agreement. In February 2006 the Committee approved an increase in Mr. Kaczmarek's base salary to $313,300. The Committee approved the increase in recognition of Mr. Kaczmarek's impact on the strategic direction of Commerce Corp and our improved operating results.

The Committee determines base salaries annually for other executive officers, including the named executive officers. Our chief executive officer proposed new base salary amounts based on:

- his evaluation of individual performance and expected future responsibilities and contribution to the achievement of the business objectives;
- a review of comparative data to ensure competitive compensation against the external market; and
- comparison of the base salaries of the executive officers who report directly to the chief executive officer to ensure internal equity.

In February 2006, Mr. Kaczmarek recommended, and the Committee approved base salary increases of approximately 4.40% to 6.15% for the other named executive officers. In approving the increase in the base salaries for these named executive officers, the Committee reviewed the minimum, mid-range and maximum salaries paid to similarly situated positions at peer banks and selected salary levels that placed the executives modestly over the mid-range.

Base salary drives the formula used in the Heritage Commerce Corp Management Incentive Plan as discussed below under "Management Incentive Plan." Base salary is the only element of compensation that is used in determining the amount of contributions permitted under the Commerce Corp 401(k) plan. Base salary is also a component used in determining benefits under our supplemental executive retirement plan.

Management Incentive Plan

The Managing Incentive Plan (the "Incentive Plan") is an annual variable performance-based cash incentive program. The Incentive Plan provides guidelines for the calculation of annual non-equity incentive performance based compensation, subject to Committee oversight and modification. At its February meeting each year, the Committee considers whether an incentive program authorized by Incentive Plan should be established for the succeeding year and, if so, approves the group of employees eligible to participate in the Incentive Plan for that year. Each year the Committee with recommendations from the chief executive officer establishes financial objectives that must be met in order for awards to be paid.

The Committee sets threshold, target and maximum levels for each financial objective. Payment of awards under the Incentive Plan are based upon the achievement of such financial objectives relative to the weight assigned to each financial objective for the current year. A minimum hurdle of expected performance must be satisfied before any payments are made under the program. In 2006, the hurdle level of performance was a minimum return on assets of 1.20%. Once the hurdle is satisfied, executive officers participating in the Incentive Plan are eligible for the awards based on meeting specified measures. The Incentive Plan includes various incentive levels with award opportunities established as a percentage of base salary. For 2006 those levels were as follows:

	As a percent of base salary		
Position	**Threshold**	**Target**	**Maximum**
Chief Executive Officer	30%	65%	110%
Executive Vice-President / Banking Division	25%	50%	85%
Executive Vice-President	25%	50%	75%
Chief Credit Officer	25%	50%	75%
Chief Financial Officer	25%	50%	75%
Senior Vice-President / Sales	25%	50%	75%

These award opportunities were derived in part from comparative data provided by our independent consultant and in part by the Committee's judgment on internal equity of the positions, their relative value to Commerce Corp and the desire to maintain a consistent annual incentive target for the chief executive officer and the named officer positions.

The payouts for executives under the Incentive Plan are targeted at the 75^{th} percentile of comparative data provided by our independent consultant in years when we reach the planned annual financial performance. If we reach, but do not exceed, the financial plan for any given year, the incentive payout, given current salary levels should approximate the 70th percentile of comparative data. However, the Incentive Plan is designed so that in years that financial performance significantly exceeds our financial plan, the payouts of the short-term incentive program should reach approximately the 80th percentile of the comparative data. Actual relative compensation levels will vary based on their salary levels and relative market position.

Management recommends and the Committee reviews and approves the financial objectives. These financial objectives as weighted are intended to motivate and reward eligible executives to strive for continued financial improvement of Commerce Corp, consistent with increasing shareholder value. The Committee has initially identified up to five key measures from which the financial objectives are drawn which may be revised to reflect current business situations.

The financial objectives selected for 2006 were net income, efficiency ratio, total average assets and return on assets (the fifth measure, return on equity was not deployed). The Committee believes net income is a very good measurement in assessing how well or how poorly Commerce Corp is performing from a financial standpoint. Net income is an accepted accounting measure that drives earnings per share and shareholder returns over the long-term. The Committee in consultation with the chief executive officer recognized for 2006 that management should also focus on total average assets, return on assets and efficiency ratio to improve performance toward the top quarter of our peer banks. Average assets and the return on those assets are accepted measures of profitability in the banking industry. The efficiency ratio is also a commonly used measure in the banking industry that measures success in controlling non interest expenses that contribute to overall profitability.

Financial objectives for the performance results are generally developed through our annual financial planning process, whereby, we assess the future operating environment and establish a financial plan for financial outcomes. Based on the strategic direction of the Board of Directors, management develops a detailed financial plan which is reviewed and approved by the Board of Directors.

The Committee determines the weighting of financial objective goals each year based upon recommendations from the chief executive officer. For 2006, the compensation committee weighted the financial objectives as follow:

Net Income	55%
Total Average Assets	15%
Efficiency Ratio	15%
Return on Assets	15%

Upon completion of the fiscal year, the Committee assesses the performance of Commerce Corp for each financial objective comparing the actual fiscal year results to the pre-determined threshold, target and maximum levels for each financial objective calculated with reference to the pre-determined weight accorded the financial objective and an overall percentage amount for the award is calculated. In addition, the Committee may include qualitative subjective measures which may increase an award up to an additional 15% of base salary.

The “target” level equates to the approved financial plan. The “threshold” performance level is set at 95% of the target level, and maximum level is set at 105% of the target level. In making the annual determination of the threshold, target and maximum levels, the Committee may consider the specific circumstances facing Commerce Corp during the coming year. Generally, the Committee sets the threshold, target and maximum levels such that the relative difficulty of achieving the target level is consistent from year to year. The Committee believed that targets established for the Incentive Plan in 2006 were sufficiently challenging, given the level of growth and improvement in the various financial objectives that would have to occur to meet the various performance levels.

For 2006, the hurdle requirement for return on assets exceeded 1.20% permitting payments as follows:

· Net income and efficiency ratio reached financial objectives that permitted the payment of "target" (or midrange) level of bonus payments;

· Return on assets reached financial objectives that permitted the payment of the "maximum" level of bonus payments; and

· The total average assets financial objective did not reach the "threshold" (or minimum) level therefore no bonus payment was allocated for this financial objective.

Awards paid to named executive officers under the Incentive Plan for performance in 2006 are reflected in column (g) of the Summary Compensation Table on page 21.

Stock Options

Stock options provide for financial gain derived from the potential appreciation in stock price from the date that the option is granted until the date that the option is exercised. The exercise price of stock option grants is set at fair market value on grant date. Under the stockholder-approved 2004 Stock Plan, we may not grant stock options at a discount to fair market value or reduce the exercise price of outstanding stock options except in the case of a stock split or other similar event. We do not grant stock options with a so-called “reload” feature, nor do we loan funds to employees to enable them to exercise stock options. Our long-term performance ultimately determines the value of stock options, because gains from stock option exercises are entirely dependent on the long-term appreciation of our stock price. Stock options generally vest pro rata daily over four years and expire ten years from the grant date.

Because a financial gain from stock options is only possible after the price of our common stock has increased, we believe grants encourage executives and other employees to focus on behaviors and initiatives that should lead to an increase in the price of our common stock, which benefits our shareholders.

The Committee established a stock option policy in 2006 which recognizes that stock options have an impact on the profits of the company under current accounting rules and also have a dilutive effect on the company’s shareholders. Accordingly, they are recognized as a scarce resource and option grants are given the same consideration as any other form of compensation. As a result of the 2005 compensation study, the Committee has established ranges for the amount of options that may be granted that depend on the individual’s position with Commerce Corp and whether the option is awarded as an incentive to attract an individual, to retain an individual or to reward performance. Stock option award levels are determined based on market data. The Committee has targeted the 75th percentile of the comparative data with respect to these long-term incentive awards.

We do not backdate options or grant options retroactively. In addition, we do not plan to coordinate grants of options so that they are made before announcement of favorable information, or after announcement of unfavorable information. Commerce Corp options are granted at fair market value on a fixed date or event (the first day of service for new hires and the date of Committee approval for existing employees), with all required approvals obtained in advance of or on the actual grant date. All grants to executive officers require the approval of the Committee and the Board of Directors. Beginning in April 2007, Commerce Corp’s general practice will be to grant options only on the annual grant date at a Committee and Board of Directors’ regular meeting in the second quarter for current staff, and at any other Committee meeting (whether a regular meeting or otherwise) held on the same date as regularly scheduled board meeting (which meets monthly) as required to attract new staff, retain staff or recognize key specific achievements. In 2006, and prior years, there were occasions when grants have been made on other dates. We are working to eliminate “off cycle” grants to the extent possible.

Except as noted below, fair market value has been consistently determined as the closing price on the NASDAQ Global Select market on the grant date. In order to ensure that its exercise price fairly reflects all material information without regard to whether the information seems positive or negative - every grant of options is contingent upon an assurance by management and legal counsel that Commerce Corp is not in possession of material undisclosed information. If Commerce Corp is in a “black-out” period for trading under its trading policy or otherwise in possession of inside information, date of grant is suspended until the second business day after public dissemination of the information.

Grants made to the chief executive officer, the chief financial officer and the other named executive officers are reflected in the Summary Compensation Table on page 21and in the Grant of Plan-Based Awards Table on page 25.

Stock Ownership Policy

Commerce Corp does not have a stock ownership policy for our executives or the board of directors.

Prohibition on Speculation in Commerce Corp Stock

Our stock trading guidelines prohibit executives from speculating in our stock, which includes, but is not limited to, short selling (profiting if the market price of the securities decreases); buying or selling publicly traded options, including writing covered calls; and hedging or any other type of derivative arrangement that has a similar economic effect.

Compensation Recovery Policy

The Committee does not have a specific policy on seeking reimbursement of compensation awards, however it will evaluate on a case by case basis whether to seek the reimbursement of certain compensation awards paid to an executive officer if such executive engages in material misconduct that caused, or partially caused, a restatement of financial results, in accordance with section 304 of the Sarbanes-Oxley Act of 2002. If circumstances warrant, we will seek to claw back appropriate portions of the executive officer’s compensation for the relevant period, as provided by law.

Change of Control Provisions

Commerce Corp does not have company-wide change of control agreements with its executive officers and other elected officers. The chief executive officer and certain named executive officers have specific change of control and severance provisions in their contracts. The Committee to date has considered the use of change of control provisions and severance provisions on a case by case basis, depending on the individual’s position with Commerce Corp and the need to attract and/or retain the individuals. See “Executive Employment Contracts” on page 22.

Summary Compensation Table

The following table provides for the periods shown, summary information concerning compensation of our Chief Executive Officer, Chief Financial Officer, and three other highly compensated executive officers and one former executive officer (collectively referred to as the "named executive officers"):

Name and Principal Position (a)	Year (b)	Salary ($)	Bonus ($)	Stock Awards ($)	Option Awards ($)	Non-Equity Incentive Plan Compensation ($)	Change in Pension Value and Nonqualified Deferred Compensation Earnings ($)	All Other Comp. ($)	Total ($)