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PATHFINDER BANCORP INC
Form 10-Q
August 16, 2004

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT UNDER SECTION 13 OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE
QUARTER ENDED JUNE 30, 2004

SEC Exchange Act No. 000-23601

Pathfinder Bancorp, Inc.
(Exact name of Company as specified in its charter)

Federal
(State or jurisdiction of incorporation or organization)

16-1540137
(I.R.S. Employer Identification Number)

214 W. 1st Street
Oswego, New York 13126

(Address of principal executive office) (Zip Code)

Company's telephone number, including area code: (315) 343-0057

Not Applicable
(Former name, former address and former fiscal year, if changed since last
report)

Indicate by check mark whether the Company (1) has filed all reports
required to be filed by Section 13 of the Securities Exchange Act of 1934 during
the preceding 12 months (or for such shorter period that the Registrant was
required to file such reports), and (2) has been subject to such filing
requirements for the past 90 days. Yes No

Indicate by check mark whether the Registrant is an accelerated filer (as
defined in Rule 12b-2 of the Act). Yes No

Indicate the number of shares outstanding of each of the issuer's classes
of common stock, as of the latest practicable date: There were 2,448,132 shares
of the Company's common stock outstanding as of August 6, 2004.

PATHFINDER BANCORP, INC.
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SIGNATURES

PATHFINDER BANCORP, INC.
CONSOLIDATED STATEMENTS OF CONDITION
JUNE 30, 2004 (UNAUDITED) AND DECEMBER 31, 2003

	June 30, 2004
ASSETS	

(dollars in thousands, except per share data)	
Cash and due from banks	\$ 7,426
Interest earning deposits	7,083

Total cash and cash equivalents	14,509
Investment securities, at fair value	75,280
Federal Home Loan Bank stock, at cost	1,873
Mortgage loans held-for-sale	665
Loans	186,210
Less: Allowance for loan losses	1,835

Loans receivable, net	184,375
Premises and equipment, net	7,238
Accrued interest receivable	1,491
Foreclosed real estate	305
Goodwill	3,840
Intangible asset, net	738
Bank owned life insurance	5,689
Other assets	3,929

Total assets	\$299,932
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LIABILITIES AND SHAREHOLDERS' EQUITY

Deposits:	
Interest-bearing	\$215,276
Noninterest-bearing	18,577
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Total deposits	233,853
Short-term borrowings	2,100
Long-term borrowings	34,260
Junior subordinated debentures	5,155
Company obligated mandatorily redeemable preferred securities of subsidiary, Pathfinder Statutory Trust I, holding solely junior subordinated debentures of the Company	-
Other liabilities	3,489
<hr/>	
Total liabilities	278,857
Shareholders' equity:	
Preferred stock, authorized shares 1,000,000; no shares issued or outstanding	
Common stock, par value \$.01; authorized 10,000,000 shares;	
2,935,419 and 2,919,386 shares issued; and 2,448,132 and 2,432,099	
shares outstanding, respectively	
Additional paid in capital	7,397
Retained earnings	21,262
Accumulated other comprehensive (loss) income	(1,056)
Unearned ESOP shares	(55)
Treasury Stock, at cost; 487,287 shares	(6,502)
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Total shareholders' equity	21,075
<hr/>	
Total liabilities and shareholders' equity	\$299,932

The accompanying notes are an integral part of the consolidated financial statements.

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PATHFINDER BANCORP, INC. CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)

	For the three months ended June 30, 2004	For the three months ended June 30, 2003
<hr/>		
(Dollars in thousands, except per share data)		
INTEREST INCOME:		
Loans	\$2,981	\$3,214
Debt securities:		
Taxable	585	538
Tax-exempt	59	59
Dividends	35	53
Other	22	13
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Total interest income	3,682	3,877

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INTEREST EXPENSE:

Interest on deposits	915	980
Interest on short-term borrowings	7	3
Interest on long-term borrowings	474	549
Total interest expense	1,396	1,532

Net interest income	2,286	2,345
Provision for loan losses	107	260

Net interest income after provision for loan losses	2,179	2,085
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OTHER INCOME:

Service charges on deposit accounts	227	216
Loan servicing fees	77	77
Increase in value of bank owned life insurance	48	43
Net gain on sales of securities	330	355
Net gain on sales of loans/real estate	41	136
Other charges, commissions & fees	129	147

Total other income	852	974
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OTHER EXPENSES:

Salaries and employee benefits	1,180	1,083
Building occupancy	257	249
Data processing expenses	229	218
Professional and other services	182	194
Amortization of intangible asset	56	56
Other expenses	423	540

Total other expenses	2,327	2,340
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Income before income taxes	704	719
Provision for income taxes	182	202

NET INCOME	\$ 522	\$ 517
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NET INCOME PER SHARE - BASIC	\$ 0.21	\$ 0.21
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NET INCOME PER SHARE - DILUTED	\$ 0.21	\$ 0.21
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DIVIDENDS PER SHARE	\$ 0.10	\$ 0.10
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The accompanying notes are an integral part of the consolidated financial statements.

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	For the six months ended June 30, 2004	For the six months ended June 30, 2003
(Dollars in thousands, except per share data)		
INTEREST INCOME:		
Loans	\$ 5,971	\$ 6,480
Debt securities:		
Taxable	1,057	1,145
Tax-exempt	107	121
Dividends	71	107
Other	37	25
Total interest income	7,243	7,878
INTEREST EXPENSE:		
Interest on deposits	1,767	2,007
Interest on short-term borrowings	16	6
Interest on long-term borrowings	970	1,119
Total interest expense	2,753	3,132
Net interest income	4,490	4,746
Provision for loan losses	295	366
Net interest income after provision for loan losses	4,195	4,380
OTHER INCOME:		
Service charges on deposit accounts	462	377
Loan servicing fees	118	127
Increase in value of bank owned life insurance	96	86
Net gain on sales of securities	484	521
Net gain on sales of loans/real estate	121	178
Other charges, commissions & fees	249	249
Total other income	1,530	1,538
OTHER EXPENSES:		
Salaries and employee benefits	2,383	2,196
Building occupancy	534	506
Data processing expenses	454	416
Professional and other services	328	357
Amortization of intangible asset	112	112
Other expenses	766	954
Total other expenses	4,577	4,541
Income before income taxes	1,148	1,377
Provision for income taxes	303	367
NET INCOME	\$ 845	\$ 1,010
NET INCOME PER SHARE - BASIC	\$ 0.35	\$ 0.42

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NET INCOME PER SHARE - DILUTED	\$	0.34	\$	0.41
DIVIDENDS PER SHARE.	\$	0.20	\$	0.20

The accompanying notes are an integral part of the consolidated financial statements.

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PATHFINDER BANCORP, INC.
STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY
SIX MONTHS ENDED JUNE 30, 2004 AND JUNE 30, 2003
(unaudited)

	Common Shares	Stock Amount	Issued Paid in Capital	Additional Retained Earnings	Accumulated Other Comprehensive Income (Loss)
BALANCE, DECEMBER 31, 2003	2,919	\$ 29	\$7,225	\$20,747	\$ 364
Comprehensive income					
Net income				845	
Other comprehensive loss, net of tax					
Unrealized net gains on securities					(1,420)
Total Comprehensive loss					
ESOP shares earned			47		
Stock option exercised	16	0	125		
Dividends declared (\$.20 per share).				(330)	
BALANCE, JUNE 30, 2004	2,935	\$ 29	\$7,397	\$21,262	\$(1,056)

	Common Shares	Stock Amount	Issued Paid in Capital	Additional Retained Earnings	Accumulated Other Comprehensive Income (Loss)
BALANCE, DECEMBER 31, 2002	2,915	\$ 29	\$7,114	\$19,746	\$281
Comprehensive income					
Net income				1,010	
Other comprehensive income, net of tax					
Unrealized net gains on securities					312
Total Comprehensive income					
ESOP shares earned			34		
Stock option exercised	2	-	15		
Treasury stock purchased					

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Dividends declared (\$.20 per share)				(484)	
BALANCE, JUNE 30, 2003	2,917	\$ 29	\$7,163	\$20,272	\$593

The accompanying notes are an integral part of the consolidated financial statements.

PATHFINDER BANCORP, INC.
STATEMENTS OF CASH FLOWS
(Unaudited)

	June 30 2004	June 30, 2003
(Dollars in thousands)		
OPERATING ACTIVITIES:		
Net income	\$ 845	\$ 1,010
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	295	366
ESOP and other stock-based compensation earned	70	57
Deferred income tax expense	32	-
Proceeds from sale of loans	7,263	6,577
Originations of loans held-for-sale	(4,317)	(8,514)
Net gain on sales of:		
Real estate loans through foreclosure	(30)	(86)
Loans	(91)	(92)
Available-for-sale investment securities	(484)	(521)
Depreciation	282	248
Amortization of intangible	112	112
Amortization of deferred financing costs	15	15
Amortization of mortgage servicing rights	81	-
Increase in surrender value of life insurance	(96)	(86)
Net amortization of premiums on investment securities	158	83
(Increase) decrease in interest receivable	(218)	15
Net change in other assets and liabilities	(981)	671
NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES	2,936	(145)
INVESTING ACTIVITIES		
Purchase of investment securities available-for-sale	(28,842)	(22,238)
Proceeds from maturities and principal reductions of investment securities available-for-sale	4,906	11,079
Proceeds from sales:		
Real estate acquired through foreclosure	100	415
Available-for-sale investment securities	4,350	7,676
Purchase of life insurance	(1,100)	-
Net decrease (increase) in loans	2,159	(4,939)
Purchase of premises and equipment	(870)	(750)
NET CASH USED IN INVESTING ACTIVITIES	(19,297)	(8,757)

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FINANCING ACTIVITIES

Net increase in demand deposits, NOW accounts		
savings accounts, money market deposit accounts		
and escrow deposits.	26,595	1,362
Net increase (decrease) in time deposits	364	(1,361)
Payments on long-term borrowings	(4,600)	-
Proceeds from long-term borrowings	-	5,300
Proceeds from exercise of stock options.	125	15
Cash dividends paid.	(328)	(325)
Treasury stock purchased	-	(2,652)
<hr/>		
NET CASH PROVIDED BY FINANCING ACTIVITIES.	22,156	2,339
<hr/>		
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS . . .	5,795	(6,563)
Cash and cash equivalents at beginning of period. . . .	8,714	13,740
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CASH AND CASH EQUIVALENTS AT END OF PERIOD	\$ 14,509	\$ 7,177
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The accompanying notes are an integral part of the consolidated financial statements

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PATHFINDER BANCORP, INC.

Notes to Financial Statements

(1) BASIS OF PRESENTATION

The accompanying unaudited financial statements were prepared in accordance with the instructions for Form 10-Q and Regulation S-X and, therefore, do not include information for footnotes necessary for a complete presentation of financial position, results of operations, and cash flows in conformity with generally accepted accounting principles. The following material under the heading "Management's Discussion and Analysis of Financial Condition and Results of Operations" is written with the presumption that the users of the interim financial statements have read, or have access to, the Company's latest audited financial statements and notes thereto, together with Management's Discussion and Analysis of Financial Condition and Results of Operations as of December 31, 2003 and for the three year period then ended. Therefore, only material changes in financial condition and results of operations are discussed in the remainder of Part 1.

Operating results for the three and six months ended June 30, 2004 are not necessarily indicative of the results that may be expected for the year ending December 31, 2004.

(2) EARNINGS PER SHARE

Basic earnings per share has been computed by dividing net income by the weighted average number of common shares outstanding throughout the three months and six months ended June 30, 2004 and 2003, using 2,436,878 and 2,416,888 weighted average common shares outstanding for the three months ended, and 2,430,468 and 2,431,556 for the six months ended, respectively. Diluted earnings per share for the three months and six months ended June 30, 2004 and 2003 have been computed using 2,478,570 and 2,463,962 for the three months ended and 2,477,102 and 2,477,236 for the six months ended, respectively. Diluted

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earnings per share gives effect to weighted average shares that would be outstanding assuming the exercise of issued stock options using the treasury stock method.

(3) STOCK-BASED COMPENSATION

The Company's stock-based compensation plan is accounted for based on the intrinsic value method set forth in Accounting Principles Board (APB) Opinion No. 25, "Accounting for Stock Issued to Employees", and related provisions. Compensation expense for employee stock options is generally not recognized if the exercise price of the option equals or exceeds the fair value of the stock on the date of the grant. Compensation expense for restricted share awards is ratably recognized over the period of vesting, usually the restricted period, based on the fair value of the stock on the grant date.

As of December 31, 2003, the stock options previously issued by the Company were fully vested. As such, there was no effect on pro forma net income for 2004. The following table illustrates the effect on net income and earnings per share for the three and six month period ended June 30, 2003, as if the Black-Scholes fair value method described in SFAS No. 123, "Accounting for Stock-Based Compensation", as amended, had been applied to the Company's stock-based compensation plan:

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	For the three Months ended June 30, 2003	For the six months ended June 30, 2003

(In thousands, except per share data)		
Net Income:		
As reported	\$ 517	\$ 1,010
Less: Total stock-based employee compensation expense determined under Black-Scholes option pricing model, net of tax effect	7	14

Pro forma net income	\$ 510	\$ 996

	For the three Months ended June 30, 2003		For the six months ended June 30, 2003	

Earnings per share:	Basic	Diluted	Basic	Diluted

As reported	\$ 0.21	\$ 0.21	\$ 0.42	\$ 0.41
Pro forma	\$ 0.21	\$ 0.21	\$ 0.41	\$ 0.40

For purposes of pro forma disclosures, the estimated fair value of the options is amortized to expense over the options vesting period. Since changes in the subjective input assumptions can materially affect the fair value estimates, the

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existing model, in management's opinion does not necessarily provide a single reliable measure of the fair value of its stock options. In addition, the pro forma effect on reported net income and earnings per share for the periods presented should not be considered representative of the pro forma effects on reported net income and earnings per share for future periods.

(4) PENSION BENEFITS

The composition of net periodic benefit plan cost for the three and six months ended June 30, is as follows:

	FOR THE MONTHS JUNE 2004	THREE ENDED 30, 2003	FOR THE MONTHS JUNE 2004	SIX ENDED 30, 2003

(In thousands)				
Service cost	\$ 43	\$ 38	\$ 86	\$ 76
Interest cost	52	50	104	100
Expected return on plan assets	(63)	(57)	(126)	(114)
Amortization of net losses	24	26	48	52

Net periodic benefit cost	\$ 56	\$ 57	\$ 112	\$ 114
=====				

The Company previously disclosed in its financial statements for the year ended December 31, 2003, that it expected to contribute \$250,000 to its pension plan in 2004. As of June 30, 2004, \$128,000 had been contributed to this pension plan. The Company presently anticipates contributing an additional \$64,000 to fund its pension plan in 2004. The reduction in the anticipated contribution resulted from a reduction in the plan's accrual formula effective May 1, 2004.

(5) DIVIDEND RESTRICTIONS

The Company maintains a restricted capital account with a \$1.0 million balance, representing Pathfinder Bancorp, M.H.C.'s portion of dividends waived as of June 30, 2004.

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(6) COMPREHENSIVE INCOME

The components of other comprehensive (loss) income and related tax effects for the three and six month period ended June 30, 2004 and 2003 are as follows:

	For the three Months ended June 30, 2004	2003	For the six months ended June 30, 2004	2003

(In thousands)				
Gross change in unrealized gains on securities available for sale	\$(2,388)	\$1,110	\$(1,882)	\$1,047

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Reclassification adjustment for gains included in net income	(330)	(355)	(484)	(521)
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	(2,718)	755	(2,366)	526
Tax effect	1,087	(305)	946	(214)
<hr/>				
Net of tax amount	\$(1,631)	\$ 450	\$(1,420)	\$ 312
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(7) GUARANTEES

The Company does not issue any guarantees that would require liability recognition or disclosure, other than its standby letters of credit. Standby letters of credit written are conditional commitments issued by the Company to guarantee the performance of a customer to a third party. Generally, all letters of credit, when issued have expiration dates within one year. The credit risk involved in issuing letters of credit is essentially the same as those that are involved in extending loan facilities to customers. The Company, generally, holds collateral and/or personal guarantees supporting these commitments. The Company had \$998,000 of standby letters of credit as of June 30, 2004. Management believes that the proceeds obtained through a liquidation of collateral and the enforcement of guarantees would be sufficient to cover the potential amount of future payment required under the corresponding guarantees. The current amount of the liability as of June 30, 2004 for guarantees under standby letters of credit issued is not material.

(8) NEW ACCOUNTING PRONOUNCEMENTS

In January 2003, the Financial Accounting Standards Board issued FASB Interpretation No. 46, "Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51" which was revised in December 2003. This Interpretation provides guidance for the consolidation of variable interest entities (VIEs). Pathfinder Statutory Trust I qualifies as a variable interest entity under FIN 46. Pathfinder Statutory Trust I issued mandatorily redeemable preferred securities (Trust Preferred Securities) to third-party investors and loaned the proceeds to the Company. Pathfinder Statutory Trust I holds, as its sole asset, subordinated debentures issued by the Company. FIN 46 required the Company to deconsolidate Pathfinder Statutory Trust I from the consolidated financial statements as of March 31, 2004. There has been no restatement of prior periods. The impact of this deconsolidation was to increase junior subordinated debentures by \$5,155,000 and reduce the mandatory redeemable preferred securities line item by \$5,000,000, which represented the trust preferred securities of the trust. The Company's equity interest in the trust subsidiary of \$155,000, which had previously been eliminated in consolidation, is now reported in "Other assets". For regulatory reporting purposes, the Federal Reserve Board has indicated that the preferred securities will continue to qualify as Tier 1 Capital subject to previously specified limitations, until further notice. If regulators make a determination that Trust Preferred Securities can no longer be considered in regulatory capital, the securities become callable and the Company may redeem them. The adoption of FIN 46 did not have an impact on the Company's results of operations or liquidity.

ITEM 2 - MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

GENERAL

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Throughout the Management's Discussion and Analysis ("MD&A") the term, "the Company", refers to the consolidated entity of Pathfinder Bancorp, Inc. Pathfinder Bank and Pathfinder Statutory Trust I are wholly owned subsidiaries of Pathfinder Bancorp, Inc. Pathfinder Commercial Bank, Pathfinder REIT, Inc. and Whispering Oaks Development Corp. represent wholly owned subsidiaries of Pathfinder Bank. Pathfinder Statutory Trust I is not included in the consolidated financial statements for the period ended June 30, 2004. At June 30, 2004, Pathfinder Bancorp, M.H.C., the Company's mutual holding company parent, whose activities are not included in the M.D.&A held 64.7% of the Company's common stock and the public held 35.3%.

The following discussion reviews the Company's financial condition at June 30, 2004 and the results of operations for the three and six months ended June 30, 2004 and June 30, 2003.

This Quarterly Report contains certain "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. Such statements are subject to certain risks and uncertainties, including, among other things, changes in economic conditions in the Company's market area, changes in policies by regulatory agencies, fluctuations in interest rates, demand for loans in the Company's market areas and competition, that could cause actual results to differ materially from historical earnings and those presently anticipated or projected. The Company wishes to caution readers not to place undue reliance on any such forward-looking statements, which speak only as of the date made. The Company wishes to advise readers that the factors listed above could affect the Company's financial performance and could cause the Company's actual results for future periods to differ materially from any opinions or statements expressed with respect to future periods in any current statements.

The Company does not undertake, and specifically declines any obligation, to publicly release the result of any revisions that may be made to any forward-looking statements to reflect events or circumstances after the date of such statements or to reflect the occurrence of anticipated or unanticipated events.

The Company's net income is primarily dependent on its net interest income, which is the difference between interest income earned on its investments in mortgage loans, investment securities and other loans, and its cost of funds consisting of interest paid on deposits and borrowed funds. The Company's net income is also affected by its provision for loan losses, as well as by the amount of noninterest income, including income from fees and service charges, net gains and losses on sales of securities, loans and foreclosed real estate, and non interest expense such as employee compensation and benefits, occupancy and equipment costs, data processing and income taxes. Earnings of the Company also are affected significantly by general economic and competitive conditions, particularly changes in market interest rates, government policies and actions of regulatory authorities, which events are beyond the control of the Company. In particular, the general level of market rates tends to be highly cyclical.

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APPLICATION OF CRITICAL ACCOUNTING POLICIES

The Company's consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States and follow practices within the banking industry. Application of these principles requires management to make estimates, assumptions and judgments that affect the amounts reported in the financial statements and accompanying notes. These estimates, assumptions and judgments are based on information available as of the date of the financial statements; accordingly, as this information changes, the financial statements could reflect different estimates, assumptions and

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judgments. Certain policies inherently have a greater reliance on the use of estimates, assumptions and judgments and as such have a greater possibility of producing results that could be materially different than originally reported. Estimates, assumptions and judgments are necessary when assets and liabilities are required to be recorded at fair value or when an asset or liability needs to be recorded contingent upon a future event. Carrying assets and liabilities at fair value inherently results in more financial statement volatility. The fair values and information used to record valuation adjustments for certain assets and liabilities are based on quoted market prices or are provided by other third-party sources, when available. When third party information is not available, valuation adjustments are estimated in good faith by management.

The most significant accounting policies followed by the Company are presented in Note 1 to the consolidated financial statements included in the 2003 Annual Report on Form 10-K ("the Consolidated Financial Statements"). These policies, along with the disclosures presented in the other financial statement notes and in this discussion, provide information on how significant assets and liabilities are valued in the financial statements and how those values are determined. Based on the valuation techniques used and the sensitivity of financial statement amounts to the methods, assumptions and estimates underlying those amounts, management has identified the determination of the allowance for loan losses to be the accounting area that requires the most subjective and complex judgments, and as such could be the most subject to revision as new information becomes available.

The allowance for loan losses represents management's estimate of probable loan losses inherent in the loan portfolio. Determining the amount of the allowance for loan losses is considered a critical accounting estimate because it requires significant judgment and the use of estimates related to the amount and timing of expected future cash flows on impaired loans, estimated losses on pools of homogeneous loans based on historical loss experience, and consideration of current economic trends and conditions, all of which may be susceptible to significant change. The loan portfolio also represents the largest asset type on the consolidated balance sheet. Note 1 to the Consolidated Financial Statements describes the methodology used to determine the allowance for loan losses, and a discussion of the factors driving changes in the amount of the allowance for loan losses is included in this report.

The Company carries all of its investments at fair value with any unrealized gains or losses reported net of tax as an adjustment to shareholders' equity. Based on management's assessment, at June 30, 2004, the Company did not hold any security that had a fair value decline that is currently expected to be other than temporary. Consequently, any declines in a specific security's fair value below amortized cost have not been provided for in the income statement. The Company's ability to fully realize the value of its investment in various securities, including corporate debt securities, is dependent on the underlying creditworthiness of the issuing organization.

RESULTS OF OPERATIONS

Net income for the second quarter of 2004 was \$522,000 as compared to net income of \$517,000 for the same quarter in 2003. Basic earnings per share was \$0.21 per share for the quarters ended June 30, 2004 and 2003. The return on average

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assets and return on shareholders' equity were 0.69% and 9.85%, respectively, for the three months ended June 30, 2004, compared with 0.73% and 9.71%, respectively, for the three months ended June 30, 2003. During the second quarter of 2004 when compared to the second quarter of 2003, provision for loan losses and other expenses decreased \$153,000 and \$13,000, respectively,

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partially offset by decreases in net interest income and other income of \$59,000 and \$122,000, respectively. Management expects continued margin compression to challenge earnings growth over the near term.

For the six months ended June 30, 2004, net income was \$845,000, a decrease of \$165,000, or 16%, as compared to net income of \$1.0 million in 2003. The decrease in net income was primarily a result of a decline in net interest income of \$256,000, partially offset by declines in provisions for loan losses and income taxes. Basic earnings per share decreased to \$0.35 per share for the six months ended June 30, 2004 from \$0.42 for the same period in 2003. The return on average assets and return on shareholders' equity were 0.57% and 7.79%, respectively for the six months ended June 30, 2004, compared with 0.72% and 9.56% for the same period in 2003.

NET INTEREST INCOME

Net interest income is the Company's primary source of operating income for payment of operating expenses and providing for loan losses. It is the amount by which interest earned on interest-earning deposits, loans and investment securities, exceeds the interest paid on deposits and other interest-bearing liabilities. Changes in net interest income and net interest margin ratio result from the interaction between the volume and composition of earning assets, interest-bearing liabilities, related yields and associated funding costs.

Net interest income, on a tax-equivalent basis, remained consistent at \$2.3 million for the three months ended June 30, 2004, as compared to the same period during 2003. The Company's net interest margin ratio for the second quarter of 2004 decreased to 3.34% from 3.74% when compared to the same quarter in 2003. The decline in net interest income is attributable to lower market interest rates which decreased earning asset yields to 5.36% from 6.16% when compared to the same period during 2003. Average interest-earning assets increased 9% to \$276.7 million at June 30, 2004 as compared to \$253.1 million at June 30, 2003. The increase in average earning assets is primarily attributable to a \$16.4 million increase in investment securities, a \$6.5 million increase in interest-earning deposits and a \$669,000 increase in loans receivable. Average interest-bearing liabilities increased \$20.9 million, while the cost of funds decreased 41 basis points to 2.15% from 2.56% for the same period in 2003. The increase in the average balance of interest-bearing liabilities resulted primarily from a \$24.2 million growth in average deposits, offset by a \$3.4 million decrease in borrowed funds. The growth in deposits was primarily in money management accounts and resulted from the Company's focus on attracting new municipal deposit customers.

For the six months ended June 30, 2004, net interest income, on a tax-equivalent basis, decreased \$254,000, or 5%, as compared to the same period during 2003. Net interest margin decreased 46 basis points, to 3.39% at June 30, 2004 from 3.85% at June 30, 2003. Average interest-earning assets increased 8% to \$268.0 million at June 30, 2004 as compared to \$249.2 million at June 30, 2003, while the yield on interest earning assets declined 92 basis points to 5.44% from 6.36% for the comparable periods. The increase in average earning assets is primarily attributable to a \$10.7 million increase in investment securities, a \$5.0 million increase in interest-earning deposits and a \$3.1 million increase in loans receivable. Average interest-bearing liabilities increased \$15.6 million, while the cost of funds decreased 47 basis points to 2.19% from 2.66% for the same period in 2003. The increase in the average balance of interest-bearing liabilities resulted primarily from a \$13.1 million growth in average deposits and a \$2.6 million increase in borrowed funds. The growth in deposits was primarily in money management accounts and resulted primarily from the Company's focus on attracting new municipal deposit customers.

INTEREST INCOME

Total interest income for the quarter ended June 30, 2004 decreased \$195,000, or 5%, to \$3.7 million from \$3.9 million at the quarter ended June 30, 2003. Average loans increased \$669,000, with yields declining 52 basis points to 6.37% for the second quarter of 2004. Average commercial loans increased \$3.7 million, and experienced a decline in the average tax-equivalent yield of 41 basis points, to 5.87% from 6.28%, in 2003. The decrease in the yield on commercial loans was affected, in part, by the offering of short-term notes to municipalities beginning in 2003. The average balance of loans to municipal entities was \$3.0 million, having a tax-equivalent yield of 2.94%. The Company's residential mortgage loan portfolio decreased \$4.0 million, or 3%, when comparing the second quarter of 2004 to the same period in 2003. The average yield on the residential mortgage loan portfolio decreased 54 basis points to 6.07% in 2004 from 6.61% in 2003. New loans were originated at lower rates than in the prior period and a large volume of existing mortgages had their rates modified downward or were refinanced at lower rates. An increase in the average balance of consumer loans of \$1.4 million, or 9%, resulted from an increase in home equity loans. The average yield declined 105 basis points, to 6.76% from 7.81% in 2003.

Average investment securities (taxable and tax-exempt) for the quarter ended June 30, 2004 increased by \$16.4 million, compared to the same period a year ago, with an increase in tax-equivalent interest income from investments of \$30,000, or 4%, compared to 2003. The average tax-equivalent yield of the portfolio declined 10 basis points, to 3.55% from 3.65%. The increase in the average balance of investment securities is reflective of the expanded deposit growth with local municipalities.

Total interest income for the six months ended June 30, 2004 decreased \$635,000, or 8%, when compared to the six months ended June 30, 2003. Average loans increased \$3.1 million, with yields declining 65 basis points to 6.33% from 6.98%. Average commercial loans increased \$3.7 million, while the yield decreased to 5.39% from 6.47% at June 30, 2003.

For the six months ended June 30, 2004, tax-equivalent interest income from investment securities decreased \$145,000, or 10%, compared to the same period in 2003. The average tax-equivalent yield of the portfolio declined 114 basis points, to 3.62% from 4.76% and was offset by a \$10.7 million increase in the average balance of investment securities.

INTEREST EXPENSE

For the three months ended June 30, 2004, total interest expense decreased \$136,000, or 9%, to \$1.4 million from \$1.5 million for the same quarter in 2003. Interest expense on deposits decreased \$65,000, or 7%, as lower interest rates favorably impacted the average rate paid on deposits, reducing it 36 basis points to 1.69% in 2004 from 2.04% in 2003. The decrease in the cost of deposits was partially offset by an increase in the average deposit balance to \$216.4 million in 2004, from \$192.1 million for the same period in 2003. In addition to the decrease in the cost of deposits, interest expense on borrowings also decreased by \$71,000, or 13%, from the prior period.

For the six months ended June 30, 2004, interest expense decreased \$379,000, or 12%, to \$2.8 million from \$3.1 million for the same period in 2003. This decrease was partially offset by a \$13.1 million increase in the average balance of deposits and a \$2.6 million increase in borrowed funds. Deposit expense for the comparable periods declined \$240,000, or 12%, as the average rate on deposits decreased 37 basis points, to 1.71% from 2.08%. Interest expense on

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borrowings declined 92 basis points to 4.38% from 5.30%.

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PROVISION FOR LOAN LOSSES

The provision for loans losses was \$107,000 for the second quarter of 2004 as compared to \$260,000 for the same period in 2003. The decrease in the provision for the quarter primarily resulted from a decrease in commercial charge-offs for the period. Non-performing loans totaled \$3.0 million at June 30, 2004 and December 31, 2003. Allowance for loan losses, as a percentage of loans, increased slightly to 0.99% at June 30, 2004 compared to 0.91% as December 31, 2003.

For the six months ended June 30, 2004, the provision for loan losses was \$295,000 as compared to \$366,000 for the same period in 2003.

NONINTEREST INCOME

The Company's noninterest income is primarily comprised of fees on deposit account balances and transactions, loan servicing, commissions, and net gains on securities, loans and foreclosed real estate.

The following table sets forth certain information on noninterest income for the quarters indicated:

	Three Months Ended June 30,				Six Months	
	2004	2003	Change		2004	2003

(Dollars in thousands)						
Service charges on deposit accounts	\$ 227	\$ 216	\$ 11	5.1%	\$ 462	\$ 3
Loan servicing fees	77	77	-	0.0%	118	1
Increase in value of bank owned life insurance . .	48	43	5	11.6%	96	
Net gains on sale of loans/foreclosed real estate.	41	136	(95)	-69.9%	121	1
Other operating income	129	147	(18)	-12.2%	249	2

Core noninterest income	522	619	(97)	-15.7%	1,046	1,0
Net gain on sales of securities	330	355	(25)	-7.1%	484	5

Total other income	\$ 852	\$ 974	\$ (122)	-12.5%	\$1,530	\$ 1,5
=====						

For the three months ended June 30, 2004, core noninterest income decreased \$97,000, or 16%, when compared with the three months ended June 30, 2003, primarily due to a reduction in net gains on foreclosed real estate resulting from the sale of a significant foreclosed real estate property in the second quarter of 2003. The decrease in other operating income was associated with the reduction in volume of investment services in comparable quarters. Income on service charges on deposit accounts increased as the number of deposit accounts increased, combined with an increase in income generated from the new consumer overdraft protection program.

For the six months ended June 30, 2004, core noninterest income increased primarily due to increased income generated on deposit accounts as new services were introduced and consulting fees associated with those new services was eliminated. This increase was offset by a decrease in net gains on sale of foreclosed real estate.

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The decrease in net gains on sales of investment securities for the three and six months ended June 30, 2004, was the result of gains associated with the sale of corporate debt securities in 2003.

NONINTEREST EXPENSE

The following table sets forth certain information on noninterest expense for the quarters indicated:

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	Three Months Ended June 30,			Six Months Ended June 30,			
	2004	2003	Change		2004	2003	Change
(Dollars in thousands)							
Salaries and employee benefits	\$1,180	\$1,083	\$ 97	8.96%	\$2,383	\$ 2,196	\$ 187
Building occupancy	257	249	8	3.21%	534	506	28
Data processing	229	218	11	5.05%	454	416	38
Professional and other services	182	194	(12)	-6.19%	328	357	(29)
Amortization of intangible assets	56	56	-	0.00%	112	112	-
Other operating	423	540	(117)	-21.67%	766	954	(188)
Total noninterest expense	\$2,327	\$2,340	\$ (13)	-0.56%	\$4,577	\$ 4,541	\$ 36

Total noninterest expense remained relatively consistent for the three and six months ended June 30, 2004 and 2003. The decrease in professional and other services and other operating expenses primarily resulted from operational costs associated with a foreclosed real estate property in 2003 and personnel realignment expenses in 2003, not recurring in 2004. The increase in salaries and employee benefits resulted from increased pension and health insurance costs and overall personnel costs due to increased staffing. The Company had 110 full time equivalent employees at June 30, 2004 compared to 104 at June 30, 2003. Building occupancy expense increases primarily resulted from depreciation expenses associated with the new Fulton branch which opened in August of 2003. The increase in data processing charges was due to depreciation expense resulting from system hardware and software acquisitions, increased ATM servicing charges and check processing charges incurred by the Commercial Bank.

INCOME TAX EXPENSE

Income taxes decreased \$20,000 for the quarter ended June 30, 2004 as compared to the same period in 2003, which was primarily attributable to a decrease in the Company's pre-tax income. For the six months ended June 30, 2004, income taxes decreased \$64,000 when compared to the same period in 2003 which was primarily attributable to a decrease in the Company's pre-tax income. The effective tax rate for the first six months of 2004 was 26.4%, compared to 26.7% for the year ended December 31, 2003.

CHANGES IN FINANCIAL CONDITION

ASSETS

Total assets increased approximately \$22.0 million, or 8%, to \$299.9 million at

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June 30, 2004, from \$277.9 million at December 31, 2003. The increase in total assets was primarily the result of an increase in investment securities of \$17.7 million, or 31%, a \$5.8 million, or 67%, increase in cash and cash equivalents and a \$3.3 million, or 53%, increase in other assets. These increases were partially offset by a decrease in net loans of \$2.6 million, or 1%. The growth in investment securities was primarily funded by the increase in municipal deposits. The increase in cash and cash equivalents was primarily the result of the increased deposit levels and loans sales to the secondary market. The excess liquidity is expected to be invested primarily in the commercial real estate portfolio and investment securities. The increase in other assets was due to a \$1.1 million purchase of life insurance policies relating to the new executives and directors deferred compensation plan which was effective December 31, 2003.

LIABILITIES

Total liabilities increased \$22.7 million, or 9%, to \$278.9 million at June 30, 2004 from \$256.2 million at December 31, 2003. The increase in liabilities is primarily due to a \$24.2 million growth in interest-bearing deposits, a \$4.6 million decrease in long-term borrowings and a \$2.8 million growth in noninterest-bearing deposits. The growth in deposits primarily resulted from the Company's focus on attracting new municipal deposit customers.

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LOAN AND ASSET QUALITY AND ALLOWANCE FOR LOAN LOSSES

The following table represents information concerning the aggregate amount of nonperforming assets:

	For the Period Ending		
	June 30, 2004	December 31, 2003	June 30, 2003

(Dollars in thousands)			
Nonaccrual loans:			
Commercial	\$1,876	\$1,677	\$ 144
Consumer	152	172	129
Real estate - Construction	0	270	0
Mortgage	986	873	999

Total nonaccrual loans	3,014	2,992	1,272
Loans past due 90 days or more and still accruing	0	0	0

Total non-performing loans	3,014	2,992	1,272
Foreclosed real estate	305	202	1,582

Total non-performing assets	3,319	3,194	2,854

Non-performing loans to total loans	1.61%	1.59%	0.67%
Non-performing assets to total assets	1.11%	1.15%	1.01%

Total nonperforming loans at June 30, 2004 were \$3.0 million, or 1.61%, of total loans as compared to \$3.0 million, or 1.59%, of total loans at December 31, 2003. Foreclosed real estate increased to \$305,000 at June 30, 2004 compared to

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\$202,000 at December 31, 2003. Nonperforming loans continue to be addressed primarily through foreclosure proceedings. Management believes that adequate reserves exist for any potential losses that may occur from the remediation process.

The allowance for loan losses at June 30, 2004 was \$1.8 million, or 0.99% of period end loans, compared to \$1.7 million, or 0.91% of period end loans, at December 31, 2003. The increase as a percentage of loans is primarily the result of the decline in gross loans.

CAPITAL

Shareholders' equity decreased \$710,000, or 3%, to \$21.0 million at June 30, 2004. The decrease in shareholders' equity primarily resulted from a \$1.4 million increase in accumulated other comprehensive loss, offset by a \$515,000 increase in retained earnings and a \$172,000 increase in additional paid in capital. The Company added \$845,000 to retained earnings through net income and returned \$330,000 to its shareholders in the form of cash dividends. The Company's mutual holding company parent, Pathfinder Bancorp, M.H.C, waived the dividend for the quarter ended June 30, 2004. (See Footnote 5).

Risk-based capital provides the basis for which all banks are evaluated in terms of capital adequacy. Capital adequacy is evaluated primarily by the use of ratios which measure capital against total assets, as well as against total assets that are weighted based on defined risk characteristics. The Company's goal is to maintain a strong capital position, consistent with the risk profile of its subsidiary banks that supports growth and expansion activities while at the same time exceeding regulatory standards. At June 30, 2004, Pathfinder Bank exceeded all regulatory required minimum capital ratios and met the regulatory definition of a "well-capitalized" institution, i.e. a leverage capital ratio exceeding 5%, a Tier 1 risk-based capital ratio exceeding 6% and a total risk-based capital ratio exceeding 10%.

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LIQUIDITY

Liquidity management involves the Company's ability to generate cash or otherwise obtain funds at reasonable rates to support asset growth and reduce assets to meet deposit withdrawals, to maintain reserve requirements, and to otherwise operate the Company on an ongoing basis. The Company's primary sources of funds are deposits, borrowed funds, amortization and prepayment of loans and maturities of investment securities and other short-term investments, and earnings and funds provided from operations. While scheduled principal repayments on loans are a relatively predictable source of funds, deposit flows and loan prepayments are greatly influenced by general interest rates, economic conditions and competition. The Company manages the pricing of deposits to maintain a desired deposit balance. In addition, the Company invests excess funds in short-term interest-earning and other assets, which provide liquidity to meet lending requirements.

The Company's liquidity has been enhanced by its membership in the Federal Home Loan Bank of New York, whose competitive advance programs and lines of credit provide the Company with a safe, reliable and convenient source of funds. A significant decrease in deposits in the future could result in the Company having to seek other sources of funds for liquidity purposes. Such sources could include, but are not limited to, additional borrowings, trust preferred security offerings, brokered deposits, negotiated time deposits, the sale of "available-for-sale" investment securities, the sale of securitized loans, or the sale of whole loans. Such actions could result in higher interest expense costs and/or losses on the sale of securities or loans.

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The Asset Liability Management Committee (ALCO) of the Company is responsible for implementing the policies and guidelines for the maintenance of prudent levels of liquidity. As of June 30, 2004, management believes that liquidity as measured by the Company is in compliance with its policy guidelines.

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ITEM 3 - QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company's risk of loss arising from adverse changes in the fair value of financial instruments, or market risk, is composed primarily of interest rate risk. The management of interest rate sensitivity seeks to avoid fluctuating net interest margins and to provide consistent net interest income through periods of changing interest rates. The primary objective of the Company's asset-liability management activities is to maximize net interest income while maintaining acceptable levels of interest rate risk. The Company has an Asset-Liability Management Committee (ALCO) which is responsible for establishing policies to limit exposure to interest rate risk, and to ensure procedures are established to monitor compliance with those policies. Those procedures include reviewing the Company's assets and liability policies, setting prices and terms on rate-sensitive products, and monitoring and measuring the impact of interest rate changes on the Company's earnings and capital. The Company's Board of Directors reviews the guidelines established by ALCO.

During the past three years, the Federal Reserve lowered interest rates thirteen times by a total of 550 basis points. These interest rate reductions have caused significant repricing of the bank's interest-earning assets and interest-bearing liabilities. Efforts have been made to shorten the repricing duration of its rate sensitive assets by purchasing investment securities with maturities within the next 3 to 5 years and promoting portfolio ARM (adjustable rate mortgage) and hybrid ARM products. In addition, the Company has extended the duration of its rate sensitive liabilities by lengthening the maturities of its existing borrowings and offering certificates of deposit with three and four year terms which allow depositors to make a one-time election, at any time during the term of the certificate of deposit, to adjust the rate of the instrument to the then prevailing rate for the certificate of deposit with the same term.

In June of 2004, the Federal Reserve raised their key interest rate one quarter of one percent for the first time in four years. An additional 25 basis point increase was announced by the Federal Reserve in early August. Management anticipates that the Federal Reserve will continue to raise its target interest rate over the foreseeable future. Management will continue to seek to minimize any reduction in net interest income in a period of rising interest rates to the extent that it can resist raising its cost of funds during this period. The Company is continuing to explore transactions and strategies to both increase its net interest income and minimize its interest rate risk.

GAP ANALYSIS. At June 30, 2004, the total interest bearing liabilities maturing or repricing within one year exceeded total interest-earning assets maturing or repricing in the same period by \$39.3 million, representing a cumulative one-year gap ratio of a negative 13.07%.

EARNINGS AT RISK AND VALUE AT RISK. Management believes the simulation of net interest income (Earnings at Risk) and net portfolio value (Value at Risk) in different interest rate environments provides a more meaningful measure of interest rate risk. Income simulation analysis captures both the potential of all assets and liabilities to mature or reprice and the probability that they will do so. Income simulation also attends to the relative interest rate

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sensitivities of these items, and projects their behavior over an extended period of time. Finally, income simulation permits management to assess the probable effects on the balance sheet not only of changes in interest rates, but also of proposed strategies for responding to them. Net portfolio value represents the fair value of net assets (determined as the market value of assets minus the market value of liabilities using a discounted cash flow technique).

The following table measures the Company's interest rate risk exposure in terms of the percentage change in its net interest income and net portfolio value as a result of hypothetical changes in 100 basis point increments in market interest rates. The table quantifies the changes in net interest income and net portfolio value to parallel shifts in the yield curve. The column "Percentage Change in Net Interest Income" measures the change to the next twelve month's projected net interest income, due to parallel shifts in the yield curve. The column "Percentage Change in Net Portfolio Value" measures changes in the current fair value of assets and liabilities to parallel shifts in the yield curve. The column "NPV Capital Ratio" measures the ratio of the fair value of net assets to the fair value of total assets at the base case and in 100 basis point incremental interest rate shocks. Currently, the Company's model projects a 300 basis point increase and a 100 basis point decrease during the next year.

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With the federal funds rate at a record low, the Company's ALCO believed it was a better measure of current risk assuming a minus 100 point scenario, as a minus 300 basis point reduction would be unlikely given that current short-term market interest rates are already below 3.00%. The Company uses these percentage changes as a means to measure interest rate risk exposure and quantifies those changes against guidelines set by the Board of Directors as part of the Company's Interest Rate Risk policy. The Company's current interest rate risk exposure is within those guidelines set forth.

Change in Interest Rates	NPV Capital Ratio	Earnings at Risk	Value as Risk
-----	-----	-----	-----
300 . . .	7.14%	-12.97%	-33.23%
200 . . .	8.13%	-8.51%	-21.88%
100 . . .	9.08%	-4.12%	-10.37%
0	9.87%	----	----
-100 . . .	10.14%	1.68%	4.96%

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ITEM 4 - CONTROLS AND PROCEDURES

Under the supervision and with the participation of the Company's management, including our Chief Executive Officer and Chief Financial Officer, the Company has evaluated the effectiveness of the design and operation of its disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d-15(e) under the Exchange Act) as of the end of the period covered by this quarterly report. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that, as of the end of the period covered by this report, the Company's disclosure controls and procedures are effective to ensure that information required to be disclosed in the reports that the Company files or

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submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission's rules and forms. There has been no change in the Company's internal control over financial reporting during the most recent fiscal quarter that has materially affected, or is reasonable likely to materially affect, the Company's internal control over financial reporting.

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PART II - OTHER INFORMATION

ITEM 1 - LEGAL PROCEEDINGS

None

ITEM 2 - CHANGES IN SECURITIES, USE OF PROCEEDS AND ISSUE OR PURCHASES OF EQUITY

SECURITIES

Not applicable

ITEM 3 - DEFAULTS UPON SENIOR SECURITIES

Not applicable

ITEM 4 - SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

The Company's Meeting of Shareholders was held on April 28, 2004. The following are the items voted on and the results of the shareholder voting:

1. The election of Corte J. Spencer, Janette Resnick and Steven W. Thomas to serve as directors of the Company, each for a term of three years or until his successor has been elected and qualified.

Name	For	Withheld
Corte J. Spencer	2,134,262	916
Janette Resnick	2,134,395	783
Steven W. Thomas	2,134,262	916

Set forth below are the names of the other directors of the Company and their terms of office.

Name	Term Expires
Chris C. Gagas	2005
Thomas W. Schneider	2005
Chris R. Burritt	2005
Raymond W. Jung	2005
Bruce Manwaring	2006
L. William Nelson	2006
George P. Joyce	2006

2. The ratification of the appointment of Beard Miller Company LLP as auditors for the Company.

For Against Abstain

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Number of Votes 2,134,095 633 450

ITEM 5 - OTHER INFORMATION

On June 30, 2004, the Board of Directors declared a \$.10 cash dividend to shareholders of record as of June 30, 2004, payable on July 15, 2004.

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ITEM 6 - EXHIBITS AND REPORTS ON FORM 8-K

(a)

Exhibit No.	Description
-------------	-------------

- | | |
|------|--|
| 10.1 | Employment Agreement between the Bank and Thomas W. Schneider, President and Chief Executive Officer |
| 10.2 | Employment Agreement between the Bank and Edward Mervine, Vice- President and General Counsel |
| 31.1 | Rule 13a-14(a) / 15d-14(a) Certification of the Chief Executive Officer |
| 31.2 | Rule 13a-14(a) / 15d-14(a) Certification of the Chief Financial Officer |
| 32.1 | Section 1350 Certification of the Chief Executive and Chief Financial Officer |

(b) Reports on Form 8-K

The Company has two Current Reports on Form 8-K during the second quarter of the fiscal year ended June 30, 2004 dated April 28, and June 30, 2004 reporting press releases relating to the first quarter earnings release and the announcement of the second quarter cash dividends, respectively.

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SIGNATURES

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

PATHFINDER BANCORP, INC.

August 16, 2004	/s/ Thomas W. Schneider

Date:	Thomas W. Schneider President, Chief Executive Officer

August 16, 2004	/s/ James A. Dowd
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Date: James A. Dowd
Vice President, Chief Financial Officer

EXHIBIT 10.1

PATHFINDER BANCORP, INC.
PATHFINDER BANK
EMPLOYMENT AGREEMENT

This Agreement is made effective as of the 28th day of June, 2004, by and between Pathfinder Bank (the "Bank"), a New York chartered stock savings bank, with its principal administrative office at 214 West First Street, Oswego, New York 13126-2547, jointly with Pathfinder Bancorp, Inc, the sole stockholder of the Bank, and Thomas W. Schneider (the "Executive"). Any reference to "Company" herein shall mean Pathfinder Bancorp, Inc. or any successor thereto. Any reference to "Employer" herein shall mean both the Bank and the Company or any successors thereto

WHEREAS, the Employer wishes to assure itself of the services of Executive for the period provided in this Agreement; and

WHEREAS, Executive is willing to serve in the employ of the Employer on a full-time basis for said period.

NOW, THEREFORE, in consideration of the mutual covenants herein contained, and upon the other terms and conditions hereinafter provided, the parties hereby agree as follows:

1. POSITION AND RESPONSIBILITIES

During the period of his employment hereunder, Executive agrees to serve as President and Chief Executive Officer of the Bank and as President and Chief Executive Officer of the Company. During said period, Executive also agrees to serve, if elected, as an officer and director of the Bank, the Company and of any subsidiary or affiliate of the Employer. Failure to reelect Executive as President and Chief Executive Officer of the Bank and the Company without the consent of the Executive during the term of this Agreement shall constitute a breach of this Agreement.

2. TERMS AND DUTIES

- (a) The period of Executive's employment under this Agreement shall begin as of the date first above written and shall continue for a period of thirty-six (36) full calendar months thereafter. Commencing on the first anniversary date of this Agreement, and continuing at each anniversary date thereafter, the Agreement shall renew for an additional year such that the remaining term shall be three (3) years unless written notice is provided to Executive, at least ten (10) days and not more than thirty (30) days prior to any such anniversary date, that his employment shall cease at the end of thirty-six (36) months following such anniversary date. Prior to each notice period for non-renewal, the disinterested members of the Board of Directors of the Bank ("Board") will conduct a comprehensive performance evaluation and review of the Executive for purposes of determining whether to extend the Agreement, and the results thereof shall be included in the minutes of the Board's meeting.

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- (b) During the period of his employment hereunder, except for periods of absence occasioned by illness, reasonable vacation periods, and reasonable leaves of absence, Executive shall devote substantially all his business time, attention, skill, and efforts to the faithful performance of his duties hereunder including activities and services related to the organization, operation and management of the Employer; provided, however, that, with the approval of the Board, as evidenced by a resolution of such Board, from time to time, Executive may serve, or continue to serve, on the boards of directors of, and hold any other offices or positions in, companies or organizations, which, in such Board's judgment, will not present any conflict of interest with the Bank, or materially affect the performance of Executive's duties pursuant to this Agreement.

- (c) During the period of his employment hereunder, if Executive's term as a director of the Bank or the Company expires, the Employer shall nominate Executive to be re-elected to the Board of Directors of the Bank and the Company. If re-elected by shareholders, Executive shall serve as director.

3. COMPENSATION AND REIMBURSEMENT

- (a) The compensation specified under this Agreement shall constitute the salary and benefits paid for the duties described in Section 2(b). The Bank shall pay Executive as compensation a salary of not less than \$185,000 per year ("Base Salary"). Such Base Salary shall be payable biweekly. During the period of this Agreement, Executive's Base Salary shall be reviewed at least annually; the first such review will be made no later than December 31, 2004. Such review shall be conducted by a Committee designated by the Board, and the Board may increase Executive's Base Salary. In addition to the Base Salary provided in this Section 3(a), the Bank shall provide Executive at no cost to Executive with all such other benefits as are provided uniformly to permanent full-time employees of the Bank.

- (b) The Bank will provide Executive with employee benefit plans, arrangements and perquisites substantially equivalent to those in which Executive was participating or otherwise deriving benefit from immediately prior to the beginning of the term of this Agreement, and the Bank will not, without Executive's prior written consent, make any changes in such plans, arrangements or perquisites which would adversely affect Executive's rights or benefits thereunder. Without limiting the generality of the foregoing provisions of this Subsection (b), Executive will be entitled to participate in or receive benefits under any employee benefit plans including but not limited to, retirement plans, supplemental retirement plans, pension plans, profit-sharing plans, health-and-accident plans, medical coverage or any other employee benefit plan or arrangement made available by the Bank in the future to its senior executives and key management employees, subject to and on a basis consistent with the terms, conditions and overall administration of such plans and arrangements. Executive will be entitled to incentive compensation and bonuses as provided in any plan of the Bank in which Executive is eligible to participate. Nothing paid to the Executive under any such plan or arrangement will be deemed to be in lieu of other compensation to which the Executive is entitled under this Agreement.

- (c) In addition to the Base Salary provided for by paragraph (a) of this Section 3, the Employer shall pay or reimburse Executive for all reasonable travel and other reasonable expenses incurred by Executive performing his obligations under this Agreement and may provide such

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additional compensation in such form and such amounts as the Board may from time to time determine.

- (d) Compensation and reimbursement to be paid pursuant to paragraphs (a), (b) and (c) of this Section 3 shall be paid by the Bank and the Company, respectively on a pro rata basis based upon the amount of service the Executive devotes to the Bank and Company, respectively.

4. PAYMENTS TO EXECUTIVE UPON AN EVENT OF TERMINATION

The provisions of this Section shall in all respects be subject to the terms and conditions stated in Sections 8 and 15.

- (a) The provisions of this Section shall apply upon the occurrence of an Event of Termination (as herein defined) during the Executive's term of employment under this Agreement. As used in this Agreement, an "Event of Termination" shall mean and include any one or more of the following: (i) the termination by the Bank or the Company of Executive's full-time employment hereunder for any reason other than, (A) Disability or Retirement as defined in Section 6 below, (B) a Change in Control, as defined in Section 5(a) hereof, or (C) Termination for Cause as defined in Section 7 hereof; or (ii) Executive's resignation from the Bank's or the Company's employ, upon any (A) failure to elect or reelect or to appoint or reappoint Executive as President and Chief Executive Officer, (B) material change in Executive's function, duties, or responsibilities, which change would cause Executive's position to become one of lesser responsibility, importance, or scope from the position and attributes thereof described in Section 1, above, (C) a relocation of Executive's principal place of employment by more than 30 miles from its location at the effective date of this Agreement, or a material reduction in the benefits and perquisites to the Executive from those being provided as of the effective date of this Agreement, (D) liquidation or dissolution of the Bank or Company other than liquidations or dissolutions that are caused by reorganizations that do not affect the status of Executive, (E) failure of the Employer to nominate Executive to be elected or re-elected as a director of the Bank or the Company, or (F) breach of this Agreement by the Bank or the Company. Upon the occurrence of any event described in clauses (ii) (A), (B), (C), (D), (E) or (F), above, Executive shall have the right to elect to terminate his employment under this Agreement by resignation upon sixty (60) days prior written notice given within a reasonable period of time not to exceed four calendar months after the initial event giving rise to said right to elect. Notwithstanding the preceding sentence, in the event of a continuing breach of this Agreement by the Employer, the Executive, after giving due notice within the prescribed time frame of an initial event specified above, shall not waive any of his rights solely under this Agreement and this Section 4 by virtue of the fact that Executive has submitted his resignation but has remained in the employment of the Employer and is engaged in good faith discussions to resolve any occurrence of an event described in clauses (A), (B), (C), (D), (E) and (F) above.
- (b) Upon the occurrence of an Event of Termination, on the Date of Termination, as defined in Section 8, the Employer shall pay Executive, or, in the event of his subsequent death, his beneficiary or beneficiaries, or his estate, as the case may be, as severance pay or liquidated damages, or both, a sum equal to three (3) times the sum of (i) Base Salary and (ii) the highest rate of bonus awarded to the Executive during the prior three years, , provided, however, that if the Employer is not in compliance with its minimum capital

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requirements or if such payments would cause the Employer's capital to be reduced below its minimum capital requirements, such payments shall be deferred until such time as the Employer is in capital compliance. At the election of the Executive, which election is to be made on an annual basis during the month of January, and which election is irrevocable for the year in which made and upon the occurrence of an Event of Termination, such payments shall be made in a lump sum or paid monthly during the remaining term of the Agreement following the Executive's termination. In the event that no election is made, payment to the Executive will be made on a monthly basis during the remaining term of the Agreement. Such payments shall not be reduced in the event the Executive obtains other employment following termination of employment.

- (c) Notwithstanding the provisions of Sections 4(a) and (b), and in the event that there has not been a Change in Control as defined in Section 5(a) nor an Event of Termination, as defined in Section 4(a), upon the voluntary termination by the Executive upon giving sixty days notice to the Employer (which itself shall not be deemed to constitute an "Event of Termination" as defined), the Employer, at the discretion of the Board of Directors, shall pay Executive, or in the event of his subsequent death, his beneficiary or beneficiaries, or his estate, as

the case may be, a severance payment in an amount to be determined by the Board of Directors at the time of such voluntary termination by the Executive. Such severance payment shall not exceed three (3) times the average of the three preceding years' Base Salary, including bonuses and any other cash compensation paid to the Executive during such years, and the amount of any benefits received pursuant to any employee benefit plans, on behalf of the Executive, maintained by the Employer during such years; provided, however, that if the Employer is not in compliance with its minimum capital requirements or if such payments would cause the Employer's capital to be reduced below its minimum capital requirements, such payments shall be deferred ---- until such time as the Employer is in capital compliance, and provided further, that in no event shall total severance compensation from all sources exceed three times the Executive's Base Salary for the immediately preceding year. At the election of the Executive, which election is to be made on an annual basis during the month of January, and which election is irrevocable for the year in which made and upon the Executive's voluntary termination, any payments shall be made in a lump sum or paid monthly during the remaining term of the Agreement following the Executive's termination. In the event that no election is made, any payment to the Executive will be made on a monthly basis during the remaining term of the agreement. Such payments shall not be reduced in the event the Executive obtains other employment following termination of employment.

- (d) Upon the occurrence of an Event of Termination, the Employer will cause to be continued life, medical, dental and disability coverage substantially identical to the coverage maintained by the Employer for Executive prior to his termination, provided that such benefits shall not be provided in the event they should constitute an unsafe or unsound banking practice relating to executive compensation and employment contracts pursuant to applicable regulations, as is now or hereafter in effect. Such coverage shall cease upon the expiration of the remaining term of this Agreement.
- (e) Upon the occurrence of an Event of Termination, Executive shall become fully vested in and entitled to all benefits granted to him pursuant to any Stock Option Plan of the Bank or Company.

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- (f) Upon the occurrence of an Event of Termination, Executive shall become fully vested in and entitled to all benefits granted to him pursuant to the Supplemental Executive Retirement Plan of the Bank or Company.
- (g) Upon the occurrence of an Event of Termination, the Executive shall become fully vested in and entitled to all benefits awarded to him under the Bank's or the Company's Recognition and Retention Plan or any restricted stock plan in effect.

5. CHANGE IN CONTROL

- (a) No benefit shall be payable under this Section 5 unless there shall have been a Change in Control of the Bank or Company. For purposes of this Agreement, a "Change in Control" of the Bank or Company shall mean a change in control of a nature that (i) would be required to be reported in response to Item 1(a) of the current report on Form 8-K, as in effect on the date hereof, pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 (the "Exchange Act"); or (ii) results in a Change in Control of the Bank or the Company within the meaning of the Home Owners Loan Act, as amended, and applicable rules and regulations promulgated thereunder, as in effect at the time of the Change in Control (collectively, the "HOLA"); or (iii) without limitation such a Change in Control shall be deemed to have occurred at such time as (a) any "person" (as the term is used in Sections 13(d) and 14(d) of the Exchange Act) is or becomes the "beneficial owner" (as defined in Rule 13d-3 under the Exchange Act), directly or indirectly, of securities of the Company representing 25% or more of the combined voting power of Company's outstanding securities except for any securities purchased by the Employer's employee stock ownership plan or trust; or (b) individuals who constitute the Company's Board of Directors on the date hereof (the "Incumbent Board") cease for any reason to constitute at least a majority thereof, provided that any person becoming a director subsequent to the date hereof whose election was approved by a vote of at least three-quarters of the directors comprising the Incumbent Board, or whose nomination for election by the Company's stockholders was

approved by the same Nominating Committee serving under an Incumbent Board, shall be, for purposes of this clause (b), considered as though he were a member of the Incumbent Board; or (c) a plan of reorganization, merger, consolidation, sale of all or substantially all the assets of the Bank or the Company or similar transaction in which the Bank or Company is not the surviving institution occurs; or (d) a proxy statement soliciting proxies from stockholders of the Company, by someone other than the current management of the Company, seeking stockholder approval of a plan of reorganization, merger or consolidation of the Company or similar transaction with one or more corporations or financial institutions, and as a result such proxy solicitation a plan of reorganization, merger consolidation or similar transaction involving the Company is approved by the requisite vote of the Company's stockholders; or (e) a tender offer is made for 25% or more of the voting securities of the Company and the shareholders owning beneficially or of record 25% or more of the outstanding securities of the Company have tendered or offered to sell their shares pursuant to such tender offer and such tendered shares have been accepted by the tender offeror. Notwithstanding anything to the contrary herein, a "Change in Control" of the Bank or the Company shall not be deemed to have occurred in the event of a conversion of Pathfinder Bancorp, MHC to stock holding company form.

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- (b) If any of the events described in Section 5(a) hereof constituting a Change in Control have occurred, Executive shall be entitled to the benefits provided in paragraphs (c), (d), (e), (f), (g) and (h) of this Section 5 upon his subsequent termination of employment at any time during the term of this Agreement, regardless of whether such termination results from (i) his resignation or (ii) his dismissal upon the Change in Control.
- (c) Upon the occurrence of a Change in Control followed by the Executive's termination of employment, the Employer shall pay Executive, or in the event of his subsequent death, his beneficiary or beneficiaries, or his estate, as the case may be, as severance pay or liquidated damages, or both, a sum equal to the greater of the payments due for the remaining term of the Agreement or 2.99 times the average of the five preceding years' Base Salary, including bonuses and any other cash compensation paid to the Executive during such years, and the amount of any contributions made to any employee benefit plans, on behalf of the Executive, maintained by the Employer during such years, (hereinafter referred to as "Payment". Such Payment shall be made by the Employer on the Date of Termination. At the election of the Executive, which election shall be made on an annual basis during the month of January, and which election is irrevocable for the year in which made and upon the occurrence of a Change in Control, such Payment may be made in a lump sum or paid in equal monthly installments during the thirty-six (36) months following the Executive's termination. In the event that no election is made, payment of the Payment to the Executive will be made pro-rata on a monthly basis during the remaining term of the Agreement.
- (d) Upon the occurrence of a Change in Control followed by the Executive's termination of employment, the Employer will cause to be continued life, medical, dental and disability coverage substantially identical to the coverage maintained by the Employer for Executive prior to his severance. Such coverage and payments shall cease upon the expiration of thirty-six (36) months.
- (e) Upon the occurrence of a Change in Control, Executive shall become fully vested in and entitled to all benefits granted to him pursuant to any Stock Option Plan of the Bank or Company.
- (f) Upon the occurrence of a Change in Control, Executive shall become fully vested in and entitled to all benefits granted to him pursuant to the Supplemental Executive Retirement Plan of the Bank or Company.
- (g) Upon the occurrence of a Change in Control, the Executive shall become fully vested in and entitled to all benefits awarded to him under the Bank's or the Company's Recognition and Retention Plan or any restricted stock plan in effect.
- (h) Notwithstanding the preceding paragraphs of this Section 5, in the event that:
- (i) the aggregate payments or benefits to be made or afforded to Executive under said paragraphs (the "Termination Benefits") would be deemed to include an "excess parachute payment" under Section 280G of the Internal Revenue Code or any successor thereto, and
 - (ii) if such Termination Benefits were reduced to an amount (the "Non-Triggering Amount"), the value of which is one dollar (\$1.00) less than an amount equal to the total amount of payments

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permissible under Section 280G of the Internal Revenue Code or any successor thereto, then the Termination Benefits to be paid to Executive shall be so reduced so as to be a Non-Triggering Amount.

- (i) Notwithstanding the foregoing, there will be no reduction in the Payment otherwise payable to Executive during any period during which Executive is incapable of performing his duties hereunder by reason of temporary disability.
- (j) Any Payment made to Executive pursuant to this Agreement or otherwise, are subject to and conditioned upon their compliance with 12 U.S.C. 1818(k) and any applicable regulations promulgated thereunder.
- (k) The Executive shall not be entitled to immediately receive Payment pursuant to this Section 5 if the Employer is not in compliance with its minimum capital requirements or if such Payment would cause the Employer's capital to be reduced below its minimum capital requirements. In such event, Payment shall be deferred until such times as the Employer is in capital compliance and provided further, that in such event the Payment shall not exceed three times the Executive's Base Salary for the immediately preceding year.

6. TERMINATION UPON RETIREMENT OR DISABILITY

Termination by the Employer of the Executive based on "Retirement" shall mean termination in accordance with the Employer's retirement policy or in accordance with any retirement arrangement established with Executive's consent with respect to him. Upon termination of Executive upon Retirement, Executive shall be entitled to all benefits under any retirement plan of the Employer and other plans to which Executive is a party.

In the event Executive is unable to perform his duties under this Agreement on a full-time basis for a period of six (6) consecutive months by reason of illness or other physical or mental disability, the Employer may terminate this Agreement, provided that the Employer shall continue to be obligated to pay the Executive his Base Salary for one year, and provided further that any amounts actually paid to Executive pursuant to any disability insurance or other similar such program which the Employer has provided or may provide on behalf of its employees or pursuant to any workman's or social security disability program shall not reduce the compensation to be paid to the Executive pursuant to this paragraph.

In the event of Executive's death during the term of the Agreement, his estate, legal representatives or named beneficiaries (as directed by Executive in writing) shall be paid Executive's Base Salary as defined in Paragraph 3(a) at the rate in effect at the time Executive's death for the remaining term of the Agreement.

7. TERMINATION FOR CAUSE

The term "Termination for Cause" shall mean termination because of the Executive's personal dishonesty, incompetence, willful misconduct, any breach of

fiduciary duty involving personal profit, intentional failure to perform stated duties, willful violation of any law, rule, or regulation (other than traffic violations or similar offenses) or final cease-and-desist order, or material breach of any provision of this Agreement. In determining incompetence, the acts or omissions shall be measured against standards generally prevailing in the financial services industry. For purposes of this paragraph, no act or failure to act on the part of Executive shall be considered "willful" unless

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done, or omitted to be done, by the Executive not in good faith and without reasonable belief that the Executive's action or omission was in the best interest of the Employer. Notwithstanding the foregoing, Executive shall not be deemed to have been Terminated for Cause unless and until there shall have been delivered to him a copy of a resolution duly adopted by the affirmative vote of not less than three-fourths of the members of the Boards of Directors of the Company and the Bank at a meeting of said Boards called and held for that purpose (after reasonable notice to Executive and an opportunity for him, together with counsel, to be heard before the Boards), finding that in the good faith opinion of the Boards, Executive was guilty of conduct justifying Termination for Cause and specifying the particulars thereof in detail. The Executive shall not have the right to receive compensation or other benefits for any period after Termination for Cause. Any unexercised stock options granted to Executive under any stock option plan of the Bank, the Company or any subsidiary or affiliate thereof, shall become null and void effective upon Executive's receipt of Notice of Termination for Cause pursuant to Section 8 hereof, and shall not be exercisable by Executive at any time subsequent to such Termination for Cause.

8. NOTICE

- (a) Any purported termination by the Employer or by Executive shall be communicated by Notice of Termination to the other party hereto. For purposes of this Agreement, a "Notice of Termination" shall mean a written notice which shall indicate the specific termination provision in this Agreement relied upon and shall set forth in reasonable detail the facts and circumstances claimed to provide a basis for termination of Executive's employment under the provision so indicated.
- (b) "Date of Termination" shall mean the date specified in the Notice of Termination (which, in the case of a Termination for Cause, shall not be less than thirty (30) days from the date such Notice of Termination is given).
- (c) If, within thirty (30) days after any Notice of Termination is given, the party receiving such Notice of Termination notifies the other party that a dispute exists concerning the termination, except upon the occurrence of a Change in Control and voluntary termination by the Executive in which case the Date of Termination shall be the date specified in the Notice, the Date of Termination shall be the date on which the dispute is finally determined, either by mutual written agreement of the parties, by a binding arbitration award, or by a final judgment, order or decree of a court of competent jurisdiction (the time for appeal having expired and no appeal having been perfected) and provided further that the Date of Termination shall be extended by a notice of dispute only if such notice is given in good faith and the party giving such notice pursues the resolution of such dispute with reasonable diligence. Notwithstanding the pendency of any such dispute, the Employer will continue to pay Executive his full compensation in effect when the notice giving rise to the dispute was given (including, but not limited to, Base Salary) and continue Executive as a participant in all compensation, benefit and insurance plans in which he was participating when the notice of dispute was given, until the dispute is finally resolved in accordance with this Agreement, provided such dispute is resolved within nine months after the Date of Termination specified in the Notice of Termination; notwithstanding the foregoing no compensation or benefits shall be paid to Executive in the event the Executive is Terminated for Cause. In the event that such Termination for Cause is found to have been wrongful or such dispute is otherwise decided in Executive's favor, the Executive shall be entitled to receive all compensation and benefits which accrued for up to a period of nine months after the

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Termination for Cause. If such dispute is not resolved within such nine-month period, the Employer shall not be obligated, upon final resolution of such dispute, to pay Executive compensation and other payments accruing more than nine months from the Date of the Termination specified in the Notice of Termination. Amounts paid under this Section are in addition to all other amounts due under this Agreement and shall not be offset against or reduce any other amounts due under this Agreement.

9. POST-TERMINATION OBLIGATIONS

- (a) All payments and benefits to Executive under this Agreement shall be subject to Executive's compliance with paragraph (b) of this Section 9 during the term of this Agreement and for one (1) full year after the expiration or termination hereof.
- (b) Executive shall, upon reasonable notice, furnish such information and assistance to the Bank as may reasonably be required by the Bank in connection with any litigation in which it or any of its subsidiaries or affiliates is, or may become, a party.
- (c) The Employer's obligation to tender the payment of Payment and Termination Benefits pursuant to Sections 4 and 5 hereof shall be conditioned upon the Executive's prior written resignations from membership in the Boards of Directors of the Bank and the Company.

10. NON-COMPETITION

- (a) Upon any termination of Executive's employment hereunder pursuant to Section 4(c) hereof, Executive agrees not to compete with the Bank and/or the Company for a period of one (1) year following such termination in any city, town or county in which the Bank and/or the Company has an office or has filed an application for regulatory approval to establish an office, determined as of the effective date of such termination, except as agreed to pursuant to a resolution duly adopted by the Board. Executive agrees that during such period and within said cities, towns and counties, Executive shall not work for or advise, consult or otherwise serve with, directly or indirectly, any entity whose business materially competes with the depository, lending or other business activities of the Bank and/or the Company. The parties hereto, recognizing that irreparable injury will result to the Bank and/or the Company, its business and property in the event of Executive's breach of this Subsection 10(a) agree that in the event of any such breach by Executive, the Bank and/or the Company will be entitled, in addition to any other remedies and damages available, to an injunction to restrain the violation hereof by Executive, Executive's partners, agents, servants, employers, employees and all persons acting for or with Executive. Nothing herein will be construed as prohibiting the Bank and/or the Company from pursuing any other remedies available to the Bank and/or the Company for such breach or threatened breach, including the recovery of damages from Executive.
- (b) Executive recognizes and acknowledges that the knowledge of the business activities and plans for business activities of the Employer and affiliates thereof, as it may exist from time to time, is a valuable, special and unique asset of the business of the Employer. Executive will not, during or after the term of his employment, disclose any knowledge of the past, present, planned or considered business activities of the Employer or affiliates thereof to any person, firm, corporation, or other entity for any reason or purpose whatsoever. Notwithstanding the foregoing, Executive may disclose any

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knowledge of banking, financial and/or economic principles, concepts or ideas which are not solely and exclusively derived from the business plans and activities of the Employer, and Executive may disclose any information regarding the Bank or the Company which is otherwise publicly available. In the event of a breach or threatened breach by the Executive of the Provisions of this Section 10, the Employer will be entitled to an injunction restraining Executive from disclosing, in whole or in part, the knowledge of the past, present, planned or considered business activities of the Employer or affiliates thereof, or from rendering any services to any person, firm, corporation, other entity to whom such knowledge, in whole or in part, has been disclosed or is threatened to be disclosed. Nothing herein will be construed as prohibiting the Employer from pursuing any other remedies available to the Bank for such breach or threatened breach, including the recovery of damages from Executive.

11. SOURCE OF PAYMENTS

All payments provided in this Agreement shall be timely paid in cash or check from the general funds of the Bank. The Company, however, guarantees payment and provision of all amounts and benefits due hereunder to Executive and, if such amounts and benefits due from the Bank are not timely paid or provided by the Bank, such amounts and benefits shall be paid or provided by the Company.

12. EFFECT ON PRIOR AGREEMENTS AND EXISTING BENEFITS PLANS

- (a) This Agreement contains the entire understanding between the parties hereto and supersedes any prior employment agreement between the Employer or any predecessor of the Employer and Executive, except that this Agreement shall not affect or operate to reduce any benefit or compensation inuring to the Executive of a kind elsewhere provided. No provision of this Agreement shall be interpreted to mean that Executive is subject to receiving fewer benefits than those available to him without reference to this Agreement.
- (b) In the event that the provisions of this Agreement are in conflict with the provisions of the Bank's or the Company's Stock Option Plan, Supplemental Executive Retirement Plan, or Recognition and Retention Plan (or any such restricted stock plan in effect) in which Executive participates, this Agreement shall govern; provided further, however, that this Agreement shall not supercede provisions that specifically received prior approval by vote of shareholders of the Company.

13. NO ATTACHMENT

- (a) Except as required by law, no right to receive payments under this Agreement shall be subject to anticipation, commutation, alienation, sale, assignment, encumbrance, charge, pledge, or hypothecation, or to execution, attachment, levy, or similar process or assignment by operation of law, and any attempt, voluntary or involuntary, to affect any such action shall be null, void, and of no effect.
- (b) This Agreement shall be binding upon, and inure to the benefit of, Executive and the Employer and their respective successors and assigns.

14. MODIFICATION AND WAIVER

- (a) This Agreement may not be modified or amended except by an instrument in writing signed by the parties hereto.

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- (b) No term or condition of this Agreement shall be deemed to have been waived, nor shall there be any estoppel against the enforcement of any provision of this Agreement, except by written instrument of the party charged with such waiver or estoppel. No such written waiver shall be deemed a continuing waiver unless specifically stated therein, and each such waiver shall operate only as to the specific term or condition waived and shall not constitute a waiver of such term or condition for the future as to any act other than that specifically waived.

15. REQUIRED PROVISIONS

- (a) The Employer may terminate the Executive's employment at any time, but any termination by the Employer, other than Termination for Cause, shall not prejudice Executive's right to compensation or other benefits under this Agreement. Executive shall not have the right to receive compensation or other benefits for any period after Termination for Cause as defined in Section 7 hereinabove.
- (b) If the Executive is suspended from office and/or temporarily prohibited from participating in the conduct of the Employer's affairs by a notice served under Section 8(e)(3) (12 U.S.C. 1818(e)(3)) or 8(g) (12 U.S.C. 1818(g)) of the Federal Deposit Insurance Act, as amended by the Financial Institutions Reform, Recovery and Enforcement Act of 1989, the Employer's obligations under this Agreement shall be suspended as of the date of service, unless stayed by appropriate proceedings. If the charges in the notice are dismissed, the Employer may in its discretion (i) pay the Executive all or part of the compensation withheld while their Agreement obligations were suspended and (ii) reinstate (in whole or in part) any of the obligations which were suspended.
- (c) If the Executive is removed and/or permanently prohibited from participating in the conduct of the Employer's affairs by an order issued under Section 8(e) (12 U.S.C. 1818(e)) or 8(g) (12 U.S.C. 1818(g)) of the Federal Deposit Insurance Act, as amended by the Financial Institutions Reform, Recovery and Enforcement Act of 1989, all obligations of the Employer under this Agreement shall terminate as of the effective date of the order, but vested rights of the contracting parties shall not be affected.
- (d) If the Employer is in default as defined in Section 3(x) (12 U.S.C. 1813(x)(1)) of the Federal Deposit Insurance Act, as amended by the Financial Institutions Reform, Recovery and Enforcement Act of 1989, all obligations of the Employer under this Agreement shall terminate as of the date of default, but this paragraph shall not affect any vested rights of the contracting parties.
- (e) All obligations of the Employer under this Agreement shall be terminated, except to the extent determined that continuation of the Agreement is necessary for the continued operation of the institution, (i) by the Federal Deposit Insurance Corporation ("FDIC"), at the time FDIC enters into an agreement to provide assistance to or on behalf of the Employer under the authority contained in Section 13(c) (12 U.S.C. 1823(c)) of the Federal Deposit Insurance Act, as amended by the Financial Institutions Reform, Recovery and Enforcement Act of 1989; or (ii) when the Employer is determined by the FDIC to be in an unsafe or unsound condition. Any rights of the parties that have already vested, however, shall not be affected by such action.

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16. SEVERABILITY

If, for any reason, any provision of this Agreement, or any part of any provision, is held invalid, such invalidity shall not affect any other provision of this Agreement or any part of such provision not held so invalid, and each such other provision and part thereof shall to the full extent consistent with law continue in full force and effect.

17. HEADINGS FOR REFERENCE ONLY

The headings of sections and paragraphs herein are included solely for convenience of reference and shall not control the meaning or interpretation of any of the provisions of this Agreement.

18. GOVERNING LAW

This Agreement shall be governed by the laws of the State of New York, but only to the extent not superseded by federal law.

19. ARBITRATION

Any dispute or controversy arising under or in connection with this Agreement shall be settled exclusively by arbitration in accordance with the rules of the American Arbitration Association then in effect. Judgment may be entered on the arbitrator's award in any court having jurisdiction; provided, however, that Executive shall be entitled to seek specific performance of his right to be paid until the Date of Termination during the pendency of any dispute or controversy arising under or in connection with this Agreement.

20. PAYMENT OF LEGAL FEES

All reasonable legal fees paid or incurred by Executive pursuant to any dispute or question of interpretation relating to this Agreement shall be paid or reimbursed by the Employer, provided that the dispute or interpretation has been settled by Executive and the Employer or resolved in the Executive's favor.

21. INDEMNIFICATION

The Employer shall provide Executive (including his heirs, executors and administrators) with coverage under a standard directors' and officers' liability insurance policy at its expense, or in lieu thereof, shall indemnify Executive (and his heirs, executors and administrators) to the fullest extent permitted under federal law against all expenses and liabilities reasonably incurred by him in connection with or arising out of any action, suit or proceeding in which he may be involved by reason of his having been a director or officer of the Employer (whether or not he continues to be a director or officer at the time of incurring such expenses or liabilities), such expenses and liabilities to include, but not be limited to, judgments, court costs and attorneys' fees and the cost of reasonable settlements (such settlements must be approved by the Boards of Directors of the Employer). If such action, suit or proceeding is brought against Executive in his capacity as an officer or director of the Employer, however, such indemnification shall not extend to matters as to which Executive is finally adjudged to be liable for willful misconduct in the performance of his duties. No Indemnification shall be paid that would violate 12 U.S.C. 1828(K) or any regulations promulgated thereunder.

22. SUCCESSOR TO THE EMPLOYER

The Employer shall require any successor or assignee, whether direct or indirect, by purchase, merger, consolidation or otherwise, to all or

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substantially all the business or assets of the Bank or the Company, expressly and unconditionally to assume and agree to perform the Employer's obligations under this Agreement, in the same manner and to the same extent that the Employer would be required to perform if no such succession or assignment had taken place.

SIGNATURES

IN WITNESS WHEREOF, the Employer has caused this Agreement to be executed and its seal to be affixed hereunto by its duly authorized officer, and Executive has signed this Agreement, on the day and date first above written.

ATTEST: PATHFINDER BANK

/s/ Melissa A. Miller

Secretary

By: /s/ Janette Resnick

Janette Resnick
Chairman

ATTEST: PATHFINDER BANCORP, INC.

/s/ Melissa A. Miller

Secretary

By: /s/ Janette Resnick

Janette Resnick
Chairman

WITNESS: EXECUTIVE

/s/ Tonya Crisafulli

By: /s/ Thomas W. Schneider

Thomas W. Schneider

EXHIBIT 10.2

PATHFINDER BANCORP, INC.
PATHFINDER BANK
EMPLOYMENT AGREEMENT

This Agreement is made effective as of the 28th day of June, 2004, by and between Pathfinder Bank (the "Bank"), a New York chartered stock savings bank, with its principal administrative office at 214 West First Street, Oswego, New York 13126-2547, jointly with Pathfinder Bancorp, Inc, the sole stockholder of the Bank, and Edward A. Mervine (the "Executive"). Any reference to "Company" herein shall mean Pathfinder Bancorp, Inc. or any successor thereto. Any reference to "Employer" herein shall mean both the Bank and the Company or any successors thereto

WHEREAS, the Employer wishes to assure itself of the services of Executive for the period provided in this Agreement; and

WHEREAS, Executive is willing to serve in the employ of the Employer on a full-time basis for said period.

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NOW, THEREFORE, in consideration of the mutual covenants herein contained, and upon the other terms and conditions hereinafter provided, the parties hereby agree as follows:

1. POSITION AND RESPONSIBILITIES

During the period of his employment hereunder, Executive agrees to serve as Vice-President and General Counsel of the Bank and as President and Vice-President and General Counsel of the Company. During said period, Executive also agrees to serve, if elected, as an officer and director of the Bank, the Company and of any subsidiary or affiliate of the Employer. Failure to reelect Executive as Vice-President and General Counsel of the Bank and the Company without the consent of the Executive during the term of this Agreement shall constitute a breach of this Agreement.

2. TERMS AND DUTIES

- (a) The period of Executive's employment under this Agreement shall begin as of the date first above written and shall continue for a period of thirty-six (36) full calendar months thereafter. Commencing on the first anniversary date of this Agreement, and continuing at each anniversary date thereafter, the Agreement shall renew for an additional year such that the remaining term shall be three (3) years unless written notice is provided to Executive, at least ten (10) days and not more than thirty (30) days prior to any such anniversary date, that his employment shall cease at the end of thirty-six (36) months following such anniversary date. Prior to each notice period for non-renewal, the disinterested members of the Board of Directors of the Bank ("Board") will conduct a comprehensive performance evaluation and review of the Executive for purposes of determining whether to extend the Agreement, and the results thereof shall be included in the minutes of the Board's meeting.
- (b) During the period of his employment hereunder, except for periods of absence occasioned by illness, reasonable vacation periods, and reasonable leaves of absence, Executive shall devote substantially all his business time, attention, skill, and efforts to the faithful performance of his duties hereunder including activities and services related to the legal needs of the Employer; provided, however, that, Executive, , hold any offices or positions in, companies or organizations, which, in such Board's judgment, will not present any conflict of interest with the Bank, or materially affect the performance of Executive's duties pursuant to this Agreement. Moreover, the Executive may continue to practice law independently of his employment provided (1) said practice does not routinely require in excess of 10 hours per week of the executive's time and (2) does not present a conflict of interest to the Bank unless said conflict is waived by the Bank or Employer.

3. COMPENSATION AND REIMBURSEMENT

- (a) The compensation specified under this Agreement shall constitute the salary and benefits paid for the duties described in Section 2(b). The Bank shall pay Executive as compensation a salary of not less than \$115,500 per year ("Base Salary"). Such Base Salary shall be payable biweekly. During the period of this Agreement, Executive's Base Salary shall be reviewed at least annually. Such review shall be conducted by a Committee designated by the Board, and the Board may increase Executive's Base Salary. In addition to the Base Salary provided in this Section 3(a), the Bank shall provide Executive at no cost to

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Executive with all such other benefits as are provided uniformly to permanent full-time employees of the Bank.

- (b) The Bank will provide Executive with employee benefit plans, arrangements and perquisites substantially equivalent to those in which Executive was participating or otherwise deriving benefit from immediately prior to the beginning of the term of this Agreement, and the Bank will not, without Executive's prior written consent, make any changes in such plans, arrangements or perquisites which would adversely affect Executive's rights or benefits thereunder. Without limiting the generality of the foregoing provisions of this Subsection (b), Executive will be entitled to participate in or receive benefits under any employee benefit plans including but not limited to, retirement plans, supplemental retirement plans, pension plans, profit-sharing plans, health-and-accident plans, medical coverage or any other employee benefit plan or arrangement made available by the Bank in the future to its senior executives and key management employees, subject to and on a basis consistent with the terms, conditions and overall administration of such plans and arrangements. Executive will be entitled to incentive compensation and bonuses as provided in any plan of the Bank in which Executive is eligible to participate. Nothing paid to the Executive under any such plan or arrangement will be deemed to be in lieu of other compensation to which the Executive is entitled under this Agreement.
- (c) In addition to the Base Salary provided for by paragraph (a) of this Section 3, the Employer shall pay or reimburse Executive for all reasonable travel and other reasonable expenses incurred by Executive performing his obligations under this Agreement and may provide such additional compensation in such form and such amounts as the Board may from time to time determine.
- (d) Compensation and reimbursement to be paid pursuant to paragraphs (a), (b) and (c) of this Section 3 shall be paid by the Bank and the Company, respectively on a pro rata basis based upon the amount of service the Executive devotes to the Bank and Company, respectively.

4. PAYMENTS TO EXECUTIVE UPON AN EVENT OF TERMINATION

The provisions of this Section shall in all respects be subject to the terms and conditions stated in Sections 8 and 15.

- (a) The provisions of this Section shall apply upon the occurrence of an Event of Termination (as herein defined) during the Executive's term of employment under this Agreement. As used in this Agreement, an "Event of Termination" shall mean and include any one or more of the following: (i) the termination by the Bank or the Company of Executive's full-time employment hereunder for any reason other than, (A) Disability or Retirement as defined in Section 6 below, (B) a Change in Control, as defined in Section 5(a) hereof, or (C) Termination for Cause as defined in Section 7 hereof; or (ii) Executive's resignation from the Bank's or the Company's employ, upon any (A) failure to elect or reelect or to appoint or reappoint Executive as Vice-President and General Counsel, (B) material change in Executive's function, duties, or responsibilities, which change would cause Executive's position to become one of lesser responsibility, importance, or scope from the position and attributes thereof described in Section 1, above, (C) a relocation of Executive's principal place of employment by more than 30 miles from its location at the effective date of this Agreement, or a material reduction in the benefits and perquisites to the Executive from those being

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provided as of the effective date of this Agreement, (D) liquidation or dissolution of the Bank or Company other than liquidations or dissolutions that are caused by reorganizations that do not affect the status of Executive, (E, or (E) breach of this Agreement by the Bank. Upon the occurrence of any event described in clauses (ii) (A), (B), (C), (D), or (E), above, Executive shall have the right to elect to terminate his employment under this Agreement by resignation upon sixty (60) days prior written notice given within a reasonable period of time not to exceed four calendar months after the initial event giving rise to said right to elect. Notwithstanding the preceding sentence, in the event of a continuing breach of this Agreement by the Employer, the Executive, after giving due notice within the prescribed time frame of an initial event specified above, shall not waive any of his rights solely under this Agreement and this Section 4 by virtue of the fact that Executive has submitted his resignation but has remained in the employment of the Employer and is engaged in good faith discussions to resolve any occurrence of an event described in clauses (A), (B), (C), (D), () and (E) above.

(b) Upon the occurrence of an Event of Termination, on the Date of Termination, as defined in Section 8, the Employer shall pay Executive, or, in the event of his subsequent death, his beneficiary or beneficiaries, or his estate, as the case may be, as severance pay or liquidated damages, or both, a sum equal to three (3) times the sum of (i) Base Salary and (ii) the highest rate of bonus awarded to the Executive during the prior three years, , provided, however, that if the Employer is not in compliance with its minimum capital requirements or if such payments would cause the Employer's capital to be reduced below its minimum capital requirements, such payments shall be deferred until such time as the Employer is in capital compliance. At the election of the Executive, which election is to be made on an annual basis during the month of January, and which election is irrevocable for the year in which made and upon the occurrence of an Event of Termination, such payments shall be made in a lump sum or paid monthly during the remaining term of the Agreement following the Executive's termination. In the event that no election is made, payment to the Executive will be made on a monthly basis during the remaining term of the Agreement. Such payments shall not be reduced in the event the Executive obtains other employment following termination of employment.

(c) Notwithstanding the provisions of Sections 4(a) and (b), and in the event that there has not been a Change in Control as defined in Section 5(a) nor an Event of Termination, as defined in Section 4(a), upon the voluntary termination by the Executive upon giving sixty days notice to the Employer (which itself shall not be deemed to constitute an "Event of Termination" as defined), the Employer, at the discretion of the Board of Directors, shall pay Executive, or in the event of his

subsequent death, his beneficiary or beneficiaries, or his estate, as the case may be, a severance payment in an amount to be determined by the Board of Directors at the time of such voluntary termination by the Executive. Such severance payment shall not exceed three (3) times the average of the three preceding years' Base Salary, including bonuses and any other cash compensation paid to the Executive during such years, and the amount of any benefits received pursuant to any employee benefit plans, on behalf of the Executive, maintained by the Employer during such years; provided, however, that if the Employer is not in compliance with its minimum capital requirements or if such payments would cause the Employer's capital to be reduced below its minimum capital requirements, such payments shall be deferred until

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such time as the Employer is in capital compliance, and provided further, that in no event shall total severance compensation from all sources exceed three times the Executive's Base Salary for the immediately preceding year. At the election of the Executive, which election is to be made on an annual basis during the month of January, and which election is irrevocable for the year in which made and upon the Executive's voluntary termination, any payments shall be made in a lump sum or paid monthly during the remaining term of the Agreement following the Executive's termination. In the event that no election is made, any payment to the Executive will be made on a monthly basis during the remaining term of the agreement. Such payments shall not be reduced in the event the Executive obtains other employment following termination of employment.

- (d) Upon the occurrence of an Event of Termination, the Employer will cause to be continued life, medical, dental and disability coverage substantially identical to the coverage maintained by the Employer for Executive prior to his termination, provided that such benefits shall not be provided in the event they should constitute an unsafe or unsound banking practice relating to executive compensation and employment contracts pursuant to applicable regulations, as is now or hereafter in effect. Such coverage shall cease upon the expiration of the remaining term of this Agreement.
- (e) Upon the occurrence of an Event of Termination, Executive shall become fully vested in and entitled to all benefits granted to him pursuant to any Stock Option Plan of the Bank or Company.
- (f) Upon the occurrence of an Event of Termination, Executive shall become fully vested in and entitled to all benefits granted to him pursuant to Supplemental Executive Retirement Plan of the Bank or Company applicable to him, if any
- (g) Upon the occurrence of an Event of Termination, the Executive shall become fully vested in and entitled to all benefits awarded to him under the Bank's or the Company's Recognition and Retention Plan or any restricted stock plan in effect.

5. CHANGE IN CONTROL

- (a) No benefit shall be payable under this Section 5 unless there shall have been a Change in Control of the Bank or Company. For purposes of this Agreement, a "Change in Control" of the Bank or Company shall mean a change in control of a nature that (i) would be required to be reported in response to Item 1(a) of the current report on Form 8-K, as in effect on the date hereof, pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 (the "Exchange Act"); or (ii) results in a Change in Control of the Bank or the Company within the meaning of the Home Owners Loan Act, as amended, and applicable rules and regulations promulgated thereunder, as in effect at the time of the Change in Control (collectively, the "HOLA"); or (iii) without limitation such a Change in Control shall be deemed to have occurred at such time as (a) any "person" (as the term is used in Sections 13(d) and 14(d) of the Exchange Act) is or becomes the "beneficial owner" (as defined in Rule 13d-3 under the Exchange Act), directly or indirectly, of securities of the Company representing 25% or more of the combined voting power of Company's outstanding securities except for any securities purchased by the Employer's employee stock ownership plan or trust; or (b) individuals who constitute the Company's Board of Directors on the date hereof (the "Incumbent Board") cease for any reason to constitute at least a majority thereof, provided that any person becoming a director subsequent to

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the date hereof whose election was approved by a vote of at least three-quarters of the directors comprising the Incumbent Board, or whose nomination for election by the Company's stockholders was approved by the same Nominating Committee serving under an Incumbent Board, shall be, for purposes of this clause (b), considered as though he were a member of the Incumbent Board; or (c) a plan of reorganization, merger, consolidation, sale of all or substantially all the assets of the Bank or the Company or similar transaction in which the Bank or Company is not the surviving institution occurs; or (d) a proxy statement soliciting proxies from stockholders of the Company, by someone other than the current management of the Company, seeking stockholder approval of a plan of reorganization, merger or consolidation of the Company or similar transaction with one or more corporations or financial institutions, and as a result such proxy solicitation a plan of reorganization, merger consolidation or similar transaction involving the Company is approved by the requisite vote of the Company's stockholders; or (e) a tender offer is made for 25% or

more of the voting securities of the Company and the shareholders owning beneficially or of record 25% or more of the outstanding securities of the Company have tendered or offered to sell their shares pursuant to such tender offer and such tendered shares have been accepted by the tender offeror. Notwithstanding anything to the contrary herein, a "Change in Control" of the Bank or the Company shall not be deemed to have occurred in the event of a conversion of Pathfinder Bancorp, MHC to stock holding company form.

- (b) If any of the events described in Section 5(a) hereof constituting a Change in Control have occurred, Executive shall be entitled to the benefits provided in paragraphs (c), (d), (e), (f), (g) and (h) of this Section 5 upon his subsequent termination of employment at any time during the term of this Agreement, regardless of whether such termination results from (i) his resignation or (ii) his dismissal upon the Change in Control.
- (c) Upon the occurrence of a Change in Control followed by the Executive's termination of employment, the Employer shall pay Executive, or in the event of his subsequent death, his beneficiary or beneficiaries, or his estate, as the case may be, as severance pay or liquidated damages, or both, a sum equal to the greater of the payments due for the remaining term of the Agreement or 2.99 times the average of the five preceding years' Base Salary, including bonuses and any other cash compensation paid to the Executive during such years, and the amount of any contributions made to any employee benefit plans, on behalf of the Executive, maintained by the Employer during such years, (hereinafter referred to as "Payment". Such Payment shall be made by the Employer on the Date of Termination. At the election of the Executive, which election shall be made on an annual basis during the month of January, and which election is irrevocable for the year in which made and upon the occurrence of a Change in Control, such Payment may be made in a lump sum or paid in equal monthly installments during the thirty-six (36) months following the Executive's termination. In the event that no election is made, payment of the Payment to the Executive will be made pro-rata on a monthly basis during the remaining term of the Agreement.
- (d) Upon the occurrence of a Change in Control followed by the Executive's termination of employment, the Employer will cause to be continued life, medical, dental and disability coverage substantially identical to the coverage maintained by the Employer for Executive prior to his severance. Such coverage and payments shall cease upon the expiration of thirty-six (36) months.

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- (e) Upon the occurrence of a Change in Control, Executive shall become fully vested in and entitled to all benefits granted to him pursuant to any Stock Option Plan of the Bank or Company.
- (f) Upon the occurrence of a Change in Control, Executive shall become fully vested in and entitled to all benefits granted to him pursuant to Supplemental Executive Retirement Plan of the Bank or Company, applicable to him, if any.
- (g) Upon the occurrence of a Change in Control, the Executive shall become fully vested in and entitled to all benefits awarded to him under the Bank's or the Company's Recognition and Retention Plan or any restricted stock plan in effect.
- (h) Notwithstanding the preceding paragraphs of this Section 5, in the event that:
 - (i) the aggregate payments or benefits to be made or afforded to Executive under said paragraphs (the "Termination Benefits") would be deemed to include an "excess parachute payment" under Section 280G of the Internal Revenue Code or any successor thereto, and
 - (ii) if such Termination Benefits were reduced to an amount (the "Non-Trigging Amount"), the value of which is one dollar (\$1.00) less than an amount equal to the total amount of payments permissible under Section 280G of the Internal Revenue Code or any successor thereto, then the Termination Benefits to be paid to Executive shall be so reduced so as to be a Non-Trigging Amount.
- (i) Notwithstanding the foregoing, there will be no reduction in the Payment otherwise payable to Executive during any period during which Executive is incapable of performing his duties hereunder by reason of temporary disability.
- (j) Any Payment made to Executive pursuant to this Agreement or otherwise, are subject to and conditioned upon their compliance with 12 U.S.C. 1818(k) and any applicable regulations promulgated thereunder.
- (k) The Executive shall not be entitled to immediately receive Payment pursuant to this Section 5 if the Employer is not in compliance with its minimum capital requirements or if such Payment would cause the Employer's capital to be reduced below its minimum capital requirements. In such event, Payment shall be deferred until such times as the Employer is in capital compliance and provided further, that in such event the Payment shall not exceed three times the Executive's Base Salary for the immediately preceding year.

6. TERMINATION UPON RETIREMENT OR DISABILITY

Termination by the Employer of the Executive based on "Retirement" shall mean termination in accordance with the Employer's retirement policy or in accordance with any retirement arrangement established with Executive's consent with respect to him. Upon termination of Executive upon Retirement, Executive shall be entitled to all benefits under any retirement plan of the Employer and other plans to which Executive is a party.

In the event Executive is unable to perform his duties under this Agreement on a full-time basis for a period of six (6) consecutive months by reason of

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illness or other physical or mental disability, the Employer may terminate this Agreement, provided that the Employer shall continue to be obligated to pay the Executive his Base Salary for one year, and provided further that any amounts actually paid to Executive pursuant to any disability insurance or other similar such program which the Employer has provided or may provide on behalf of its employees or pursuant to any workman's or social security disability program shall not reduce the compensation to be paid to the Executive pursuant to this paragraph.

In the event of Executive's death during the term of the Agreement, his estate, legal representatives or named beneficiaries (as directed by Executive in writing) shall be paid Executive's Base Salary as defined in Paragraph 3(a) at the rate in effect at the time Executive's death for the remaining term of the Agreement.

7. TERMINATION FOR CAUSE

The term "Termination for Cause" shall mean termination because of the Executive's personal dishonesty, incompetence, willful misconduct, any breach of fiduciary duty involving personal profit, intentional failure to perform stated

duties, willful violation of any law, rule, or regulation (other than traffic violations or similar offenses) or final cease-and-desist order, or material breach of any provision of this Agreement. In determining incompetence, the acts or omissions shall be measured against standards generally prevailing in the financial services industry. For purposes of this paragraph, no act or failure to act on the part of Executive shall be considered "willful" unless done, or omitted to be done, by the Executive not in good faith and without reasonable belief that the Executive's action or omission was in the best interest of the Employer. Notwithstanding the foregoing, Executive shall not be deemed to have been Terminated for Cause unless and until there shall have been delivered to him a copy of a resolution duly adopted by the affirmative vote of not less than three-fourths of the members of the Boards of Directors of the Company and the Bank at a meeting of said Boards called and held for that purpose (after reasonable notice to Executive and an opportunity for him, together with counsel, to be heard before the Boards), finding that in the good faith opinion of the Boards, Executive was guilty of conduct justifying Termination for Cause and specifying the particulars thereof in detail. The Executive shall not have the right to receive compensation or other benefits for any period after Termination for Cause. Any unexercised stock options granted to Executive under any stock option plan of the Bank, the Company or any subsidiary or affiliate thereof, shall become null and void effective upon Executive's receipt of Notice of Termination for Cause pursuant to Section 8 hereof, and shall not be exercisable by Executive at any time subsequent to such Termination for Cause.

8. NOTICE

- (a) Any purported termination by the Employer or by Executive shall be communicated by Notice of Termination to the other party hereto. For purposes of this Agreement, a "Notice of Termination" shall mean a written notice which shall indicate the specific termination provision in this Agreement relied upon and shall set forth in reasonable detail the facts and circumstances claimed to provide a basis for termination of Executive's employment under the provision so indicated.
- (b) "Date of Termination" shall mean the date specified in the Notice of Termination (which, in the case of a Termination for Cause, shall not be less than thirty (30) days from the date such Notice of Termination is given).

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- (c) If, within thirty (30) days after any Notice of Termination is given, the party receiving such Notice of Termination notifies the other party that a dispute exists concerning the termination, except upon the occurrence of a Change in Control and voluntary termination by the Executive in which case the Date of Termination shall be the date specified in the Notice, the Date of Termination shall be the date on which the dispute is finally determined, either by mutual written agreement of the parties, by a binding arbitration award, or by a final judgment, order or decree of a court of competent jurisdiction (the time for appeal having expired and no appeal having been perfected) and provided further that the Date of Termination shall be extended by a notice of dispute only if such notice is given in good faith and the party giving such notice pursues the resolution of such dispute with reasonable diligence. Notwithstanding the pendency of any such dispute, the Employer will continue to pay Executive his full compensation in effect when the notice giving rise to the dispute was given (including, but not limited to, Base Salary) and continue Executive as a participant in all compensation, benefit and insurance plans in which he was participating when the notice of dispute was given, until the dispute is finally resolved in accordance with this Agreement, provided such dispute is resolved within nine months after the Date of Termination specified in the Notice of Termination; notwithstanding the foregoing no compensation or benefits shall be paid to Executive in the event the Executive is Terminated for Cause. In the event that such Termination for Cause is found to have been wrongful or such dispute is otherwise decided in Executive's favor, the Executive shall be entitled to receive all compensation and benefits which accrued for up to a period of nine months after the Termination for Cause. If such dispute is not resolved within such nine-month period, the Employer shall not be obligated, upon final resolution of such dispute, to pay Executive compensation and other payments accruing more than nine months from the Date of the Termination specified in the Notice of Termination. Amounts paid under this Section are in addition to all other amounts due under this Agreement and shall not be offset against or reduce any other amounts due under this Agreement.

9. POST-TERMINATION OBLIGATIONS

- (a) All payments and benefits to Executive under this Agreement shall be subject to Executive's compliance with paragraph (b) of this Section 9 during the term of this Agreement and for one (1) full year after the expiration or termination hereof.
- (b) Executive shall, upon reasonable notice, furnish such information and assistance to the Bank as may reasonably be required by the Bank in connection with any litigation in which it or any of its subsidiaries or affiliates is, or may become, a party.

10. NON-COMPETITION

- (a) Upon any termination of Executive's employment hereunder pursuant to Section 4(c) hereof, Executive agrees not to compete with the Bank and/or the Company for a period of one (1) year following such termination in any city, town or county in which the Bank and/or the Company has an office or has filed an application for regulatory approval to establish an office, determined as of the effective date of such termination, except as agreed to pursuant to a resolution duly adopted by the Board. Executive agrees that during such period and within said cities, towns and counties, Executive shall not work for or advise, consult or otherwise serve with, directly or indirectly,

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any entity whose business materially competes with the depository, lending or other business activities of the Bank and/or the Company. The parties hereto, recognizing that irreparable injury will result to the Bank and/or the Company, its business and property in the event of Executive's breach of this Subsection 10(a) agree that in the event of any such breach by Executive, the Bank and/or the Company will be entitled, in addition to any other remedies and damages available, to an injunction to restrain the violation hereof by Executive, Executive's partners, agents, servants, employers, employees and all persons acting for or with Executive. Nothing herein will be construed as prohibiting the Bank and/or the Company from pursuing any other remedies available to the Bank and/or the Company for such breach or threatened breach, including the recovery of damages from Executive.

- (b) Executive recognizes and acknowledges that the knowledge of the business activities and plans for business activities of the Employer and affiliates thereof, as it may exist from time to time, is a valuable, special and unique asset of the business of the Employer. Executive will not, during or after the term of his employment, disclose any knowledge of the past, present, planned or considered business activities of the Employer or affiliates thereof to any person, firm, corporation, or other entity for any reason or purpose whatsoever. Notwithstanding the foregoing, Executive may disclose any knowledge of banking, financial and/or economic principles, concepts or ideas which are not solely and exclusively derived from the business plans and activities of the Employer, and Executive may disclose any information regarding the Bank or the Company which is otherwise publicly available. In the event of a breach or threatened breach by the Executive of the Provisions of this Section 10, the Employer will be entitled to an injunction restraining Executive from disclosing, in whole or in part, the knowledge of the past, present, planned or considered business activities of the Employer or affiliates thereof, or from rendering any services to any person, firm, corporation, other entity to whom such knowledge, in whole or in part, has been disclosed or is threatened to be disclosed. Nothing herein will be construed as prohibiting the Employer from pursuing any other remedies available to the Bank for such breach or threatened breach, including the recovery of damages from Executive.

11. SOURCE OF PAYMENTS

All payments provided in this Agreement shall be timely paid in cash or check from the general funds of the Bank. The Company, however, guarantees payment and provision of all amounts and benefits due hereunder to Executive and, if such amounts and benefits due from the Bank are not timely paid or provided by the Bank, such amounts and benefits shall be paid or provided by the Company.

12. EFFECT ON PRIOR AGREEMENTS AND EXISTING BENEFITS PLANS

- (a) This Agreement contains the entire understanding between the parties hereto and supersedes any prior employment agreement between the Employer or any predecessor of the Employer and Executive, except that this Agreement shall not affect or operate to reduce any benefit or compensation inuring to the Executive of a kind elsewhere provided. No provision of this Agreement shall be interpreted to mean that Executive is subject to receiving fewer benefits than those available to him without reference to this Agreement.
- (b) In the event that the provisions of this Agreement are in conflict with the provisions of the Bank's or the Company's Stock Option Plan,

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Supplemental Executive Retirement Plan, or Recognition and Retention Plan (or any such restricted stock plan in effect) in which Executive participates, this Agreement shall govern; provided further, however, that this Agreement shall not supercede provisions that specifically received prior approval by vote of shareholders of the Company.

13. NO ATTACHMENT

- (a) Except as required by law, no right to receive payments under this Agreement shall be subject to anticipation, commutation, alienation, sale, assignment, encumbrance, charge, pledge, or hypothecation, or to execution, attachment, levy, or similar process or assignment by operation of law, and any attempt, voluntary or involuntary, to affect any such action shall be null, void, and of no effect.
- (b) This Agreement shall be binding upon, and inure to the benefit of, Executive and the Employer and their respective successors and assigns.

14. MODIFICATION AND WAIVER

- (a) This Agreement may not be modified or amended except by an instrument in writing signed by the parties hereto.
- (b) No term or condition of this Agreement shall be deemed to have been waived, nor shall there be any estoppel against the enforcement of any provision of this Agreement, except by written instrument of the party charged with such waiver or estoppel. No such written waiver shall be deemed a continuing waiver unless specifically stated therein, and each such waiver shall operate only as to the specific term or condition waived and shall not constitute a waiver of such term or condition for the future as to any act other than that specifically waived.

15. REQUIRED PROVISIONS

- (a) The Employer may terminate the Executive's employment at any time, but any termination by the Employer, other than Termination for Cause, shall not prejudice Executive's right to compensation or other benefits under this Agreement. Executive shall not have the right to receive compensation or other benefits for any period after Termination for Cause as defined in Section 7 hereinabove.
- (b) If the Executive is suspended from office and/or temporarily prohibited from participating in the conduct of the Employer's affairs by a notice served under Section 8(e)(3) (12 U.S.C. 1818(e)(3)) or 8(g) (12 U.S.C. 1818(g)) of the Federal Deposit Insurance Act, as amended by the Financial Institutions Reform, Recovery and Enforcement Act of 1989, or if the Executive is suspended from the practice of law the Employer's obligations under this Agreement shall be suspended as of the date of service, unless stayed by appropriate proceedings. If the charges in the notice are dismissed, or if the Executive's suspension to practice is reversed, the Employer may in its discretion (i) pay the Executive all or part of the compensation withheld while their Agreement obligations were suspended and (ii) reinstate (in whole or in part) any of the obligations which were suspended.
- (c) If the Executive is removed and/or permanently prohibited from participating in the conduct of the Employer's affairs by an order issued under Section 8(e) (12 U.S.C. 1818(e)) or 8(g) (12 U.S.C.

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1818(g)) of the Federal Deposit Insurance Act, as amended by the Financial Institutions Reform, Recovery and Enforcement Act of 1989, or if the Executive is disbarred from the practice of law, all obligations of the Employer under this Agreement shall terminate as of the effective date of the order, but vested rights of the contracting parties shall not be affected.

- (d) If the Employer is in default as defined in Section 3(x) (12 U.S.C. 1813(x)(1)) of the Federal Deposit Insurance Act, as amended by the Financial Institutions Reform, Recovery and Enforcement Act of 1989, all obligations of the Employer under this Agreement shall terminate as of the date of default, but this paragraph shall not affect any vested rights of the contracting parties.
- (e) All obligations of the Employer under this Agreement shall be terminated, except to the extent determined that continuation of the Agreement is necessary for the continued operation of the institution, (i) by the Federal Deposit Insurance Corporation ("FDIC"), at the time FDIC enters into an agreement to provide assistance to or on behalf of the Employer under the authority contained in Section 13(c) (12 U.S.C. 1823(c)) of the Federal Deposit Insurance Act, as amended by the Financial Institutions Reform, Recovery and Enforcement Act of 1989; or (ii) when the Employer is determined by the FDIC to be in an unsafe or unsound condition. Any rights of the parties that have already vested, however, shall not be affected by such action.

16. SEVERABILITY

If, for any reason, any provision of this Agreement, or any part of any provision, is held invalid, such invalidity shall not affect any other provision of this Agreement or any part of such provision not held so invalid, and each such other provision and part thereof shall to the full extent consistent with law continue in full force and effect.

17. HEADINGS FOR REFERENCE ONLY

The headings of sections and paragraphs herein are included solely for convenience of reference and shall not control the meaning or interpretation of any of the provisions of this Agreement.

18. GOVERNING LAW

This Agreement shall be governed by the laws of the State of New York, but only to the extent not superseded by federal law.

19. ARBITRATION

Any dispute or controversy arising under or in connection with this Agreement shall be settled exclusively by arbitration in accordance with the rules of the American Arbitration Association then in effect. Judgment may be entered on the arbitrator's award in any court having jurisdiction; provided, however, that Executive shall be entitled to seek specific performance of his right to be paid until the Date of Termination during the pendency of any dispute or controversy arising under or in connection with this Agreement.

20. PAYMENT OF LEGAL FEES

All reasonable legal fees paid or incurred by Executive pursuant to any dispute or question of interpretation relating to this Agreement shall be paid or reimbursed by the Employer, provided that the dispute or interpretation has been settled by Executive and the Employer or resolved in the Executive's favor.

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21. INDEMNIFICATION

The Employer shall provide Executive (including his heirs, executors and administrators) with coverage under a standard directors' and officers' liability insurance policy at its expense, or in lieu thereof, shall indemnify Executive (and his heirs, executors and administrators) to the fullest extent permitted under federal law against all expenses and liabilities reasonably incurred by him in connection with or arising out of any action, suit or proceeding in which he may be involved by reason of his having been an officer of the Employer (whether or not he continues to be an officer at the time of incurring such expenses or liabilities), such expenses and liabilities to include, but not be limited to, judgments, court costs and attorneys' fees and the cost of reasonable settlements (such settlements must be approved by the Boards of Directors of the Employer). If such action, suit or proceeding is brought against Executive in his capacity as an officer of the Employer, however, such indemnification shall not extend to matters as to which Executive is finally adjudged to be liable for willful misconduct in the performance of his duties. No Indemnification shall be paid that would violate 12 U.S.C. 1828(K) or any regulations promulgated thereunder.

22. SUCCESSOR TO THE EMPLOYER

The Employer shall require any successor or assignee, whether direct or indirect, by purchase, merger, consolidation or otherwise, to all or substantially all the business or assets of the Bank or the Company, expressly and unconditionally to assume and agree to perform the Employer's obligations under this Agreement, in the same manner and to the same extent that the Employer would be required to perform if no such succession or assignment had taken place.

SIGNATURES

IN WITNESS WHEREOF, the Employer has caused this Agreement to be executed and its seal to be affixed hereunto by its duly authorized officer, and Executive has signed this Agreement, on the day and date first above written.

ATTEST: PATHFINDER BANK

/s/ Melissa A. Miller
Secretary

By: /s/ Thomas W. Schneider
Thomas W. Schneider
President and Chief Executive Officer

ATTEST: PATHFINDER BANCORP, INC.

/s/ Melissa A. Miller
Secretary

By: /s/ Thomas W. Schneider
Thomas W. Schneider
President and Chief Executive Officer

WITNESS: EXECUTIVE

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Karen Moskal

By: /s/ Edward A. Mervine

Edward A.Mervine

EXHIBIT 31.1

Rule 13a-14(a) / 15d-14(a) Certification of the Chief Executive Officer

Certification of Chief Executive Officer
Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Thomas W. Schneider, President and Chief Executive Officer, certify that:

1. I have reviewed the June 30, 2004 quarterly report on Form 10-Q of Pathfinder Bancorp, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:

a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors:

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

August 16, 2004

/s/ Thomas W. Schneider

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Date

Thomas W. Schneider
President and Chief Executive Officer

EXHIBIT 31.2

Rule 13a-14(a) / 15d-14(a) Certification of the Chief Financial Officer

Certification of Chief Financial Officer
Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, James A. Dowd, Vice President and Chief Financial Officer, certify that:

1. I have reviewed the June 30, 2004 quarterly report on Form 10-Q of Pathfinder Bancorp, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:

a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors:

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

August 16, 2004

/s/ James A. Dowd

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Date James A. Dowd
Vice President and Chief Financial Officer

EXHIBIT 32.1

Section 1350 Certification of the Chief Executive and Chief Financial Officer

Certification pursuant to
18 U.S.C. Section 1350,
as adopted pursuant to
Section 906 of the Sarbanes-Oxley Act of 2002

Thomas W. Schneider, President and Chief Executive Officer, and James A. Dowd, Vice President and Chief Financial Officer of Pathfinder Bancorp, Inc. (the "Company"), each certify in his capacity as an officer of the Company that he has reviewed the Quarterly Report of the Company on Form 10-Q for the quarter ended June 30, 2004 and that to the best of his knowledge:

1. the report fully complies with the requirements of Sections 13(a) of the Securities Exchange Act of 1934; and

2. the information contained in the report fairly presents, in all material respects, the financial condition and results of operations of the Company.

The purpose of this statement is solely to comply with Title 18, Chapter 63, Section 1350 of the United States Code, as amended by Section 906 of the Sarbanes-Oxley Act of 2002.

August 16, 2004

/s/ Thomas W. Schneider

Date

Thomas W. Schneider
President and Chief Executive Officer

August 16, 2004

/s/ James A. Dowd

Date

James A. Dowd
Vice President and Chief Financial Officer