

PATHFINDER BANCORP INC  
Form 10-Q  
November 14, 2008

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

FORM 10-Q

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

For the quarterly period ending September 30, 2008

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: 000-23601

PATHFINDER BANCORP, INC.  
(Exact Name of Company as Specified in its Charter)

FEDERAL  
(State or Other Jurisdiction of  
Incorporation or Organization)

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

214 West First Street, Oswego, NY 13126  
(Address of Principal Executive Office) (Zip Code)

(315) 343-0057  
(Issuer's Telephone Number including area code)

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES  
T NO \*

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

filer\*                      Large accelerated filer\*                      Accelerated filer\*                      Non-accelerated  
Smaller reporting company T

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). YES \* NO  
T

As of November 13, 2008, there were 2,972,119 shares issued and 2,484,832 shares outstanding of the Registrant's Common Stock.

PATHFINDER BANCORP, INC.  
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PART I - FINANCIAL INFORMATION  
Item 1 – Consolidated Financial Statements

PATHFINDER BANCORP, INC.  
CONSOLIDATED STATEMENTS OF CONDITION  
September 30, 2008 and December 31, 2007  
(Unaudited)

| (In thousands, except share data)   | September<br>30,<br>2008 | December<br>31,<br>2007 |
|---|--------------------------|-------------------------|
| <b>ASSETS:</b>  |                          |                         |
| Cash and due from banks   | \$ 11,365                | \$ 9,908                |
| Interest earning deposits   | 312                      | 305                     |
| Total cash and cash equivalents   | 11,677                   | 10,213                  |
| Investment securities, at fair value  | 75,080                   | 65,010                  |
| Federal Home Loan Bank stock, at cost   | 2,782                    | 2,128                   |
| Loans   | 243,223                  | 222,749                 |
| Less: Allowance for loan losses   | 2,241                    | 1,703                   |
| Loans receivable, net   | 240,982                  | 221,046                 |
| Premises and equipment, net   | 7,484                    | 7,807                   |
| Accrued interest receivable   | 1,637                    | 1,673                   |
| Foreclosed real estate  | 253                      | 865                     |
| Goodwill  | 3,840                    | 3,840                   |
| Bank owned life insurance   | 6,617                    | 6,437                   |
| Other assets  | 2,436                    | 1,672                   |
| Total assets  | \$ 352,788               | \$ 320,691              |
| <b>LIABILITIES AND SHAREHOLDERS' EQUITY:</b>                                  |                          |                         |
| Deposits:   |                          |                         |
| Interest-bearing  | \$ 238,040               | \$ 228,319              |
| Noninterest-bearing   | 26,713                   | 22,766                  |
| Total deposits  | 264,753                  | 251,085                 |
| Short-term borrowings   | 21,755                   | 18,400                  |
| Long-term borrowings  | 35,400                   | 20,010                  |
| Junior subordinated debentures  | 5,155                    | 5,155                   |
| Other liabilities   | 5,134                    | 4,337                   |
| Total liabilities   | 332,197                  | 298,987                 |
| Shareholders' equity:   |                          |                         |
| Preferred stock, authorized shares 1,000,000; no shares issued or outstanding |                          |                         |
| Common stock, par value \$0.01; authorized 10,000,000 shares;                 |                          |                         |

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2,972,119 and 2,971,019 share issued and 2,484,832 and 2,483,732 shares

|  |            |            |
|--|------------|------------|
| outstanding, respectively                  | 30         | 30         |
| Additional paid in capital                 | 7,909      | 7,899      |
| Retained earnings                          | 20,878     | 21,734     |
| Accumulated other comprehensive loss       | (1,724)    | (1,457)    |
| Treasury stock, at cost; 487,287 shares    | (6,502)    | (6,502)    |
| Total shareholders' equity                 | 20,591     | 21,704     |
| Total liabilities and shareholders' equity | \$ 352,788 | \$ 320,691 |

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  
September 30, 2008

For the three  
months ended  
September 30, 2007

(In thousands, except per share data)

## Interest and dividend income:

|  |          |          |
|--|----------|----------|
| Loans, including fees                            | \$ 3,755 | \$ 3,546 |
| Debt securities:                                 |          |          |
| Taxable  | 764      | 623      |
| Tax-exempt                                       | 44       | 42       |
| Dividends  | 91       | 83       |
| Federal funds sold and interest earning deposits | 5        | 6        |
| Total interest income                            | 4,659    | 4,300    |

## Interest expense:

|                                   |       |       |
|-----------------------------------|-------|-------|
| Interest on deposits              | 1,320 | 1,734 |
| Interest on short-term borrowings | 103   | 99    |
| Interest on long-term borrowings  | 455   | 314   |
| Total interest expense            | 1,878 | 2,147 |

|   |       |       |
|---|-------|-------|
| Net interest income                                 | 2,781 | 2,153 |
| Provision for loan losses                           | 270   | 155   |
| Net interest income after provision for loan losses | 2,511 | 1,998 |

## Noninterest (loss) income:

|   |         |     |
|---|---------|-----|
| Service charges on deposit accounts                                 | 397     | 366 |
| Earnings on bank owned life insurance                               | 56      | 56  |
| Loan servicing fees   | 67      | 72  |
| Net (losses) gains on sales and impairment of investment securities | (1,808) | 111 |
| Net (losses) gains on sales of loans and foreclosed real estate     | (85)    | 11  |
| Debit card interchange fees   | 71      | 62  |
| Other charges, commissions & fees                                   | 127     | 114 |
| Total noninterest (loss) income                                     | (1,175) | 792 |

## Noninterest expense:

|                                  |       |       |
|----------------------------------|-------|-------|
| Salaries and employee benefits   | 1,284 | 1,263 |
| Building occupancy               | 331   | 305   |
| Data processing expenses         | 335   | 339   |
| Professional and other services  | 158   | 130   |
| Amortization of intangible asset | -     | 55    |
| Other expenses                   | 354   | 320   |
| Total noninterest expense        | 2,462 | 2,412 |

|                                      |         |     |
|--------------------------------------|---------|-----|
| (Loss) income before income taxes    | (1,126) | 378 |
| (Benefit) provision for income taxes | (288)   | 72  |

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|                                       |    |        |    |        |
|---------------------------------------|----|--------|----|--------|
| Net (loss) income                     | \$ | (838)  | \$ | 306    |
| Net (loss) income per share - basic   | \$ | (0.34) | \$ | 0.12   |
| Net (loss) income per share - diluted | \$ | (0.34) | \$ | 0.12   |
| Dividends per share                   | \$ | 0.1025 | \$ | 0.1025 |

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

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

|   | For the nine<br>months<br>ended<br>September<br>30, 2008 | For the nine<br>months<br>ended<br>September<br>30, 2007 |
|---|--|--|
| (In thousands, except per share data)                               |  |  |
| Interest and dividend income:                                       |  |  |
| Loans, including fees   | \$ 10,943  | \$ 10,393  |
| Debt securities:  |  |  |
| Taxable   | 2,219  | 1,937  |
| Tax-exempt  | 126  | 128  |
| Dividends   | 318  | 249  |
| Federal funds sold and interest earning deposits                    | 59   | 199  |
| Total interest income   | 13,665   | 12,906   |
| Interest expense:   |  |  |
| Interest on deposits  | 4,332  | 5,215  |
| Interest on short-term borrowings                                   | 329  | 111  |
| Interest on long-term borrowings                                    | 1,174  | 1,178  |
| Total interest expense  | 5,835  | 6,504  |
|   | -  |  |
| Net interest income   | 7,830  | 6,402  |
| Provision for loan losses   | 550  | 280  |
| Net interest income after provision for loan losses                 | 7,280  | 6,122  |
| Noninterest income:   |  |  |
| Service charges on deposit accounts                                 | 1,131  | 1,060  |
| Earnings on bank owned life insurance                               | 179  | 169  |
| Loan servicing fees   | 218  | 186  |
| Net (losses) gains on sales and impairment of investment securities | (2,150)  | 108  |
| Net (losses) gains on sales of loans and foreclosed real estate     | (79)   | 42   |
| Debit card interchange fees   | 207  | 178  |
| Other charges, commissions & fees                                   | 334  | 317  |
| Total noninterest (loss) income                                     | (160)  | 2,060  |
| Noninterest expense:  |  |  |
| Salaries and employee benefits                                      | 3,863  | 3,764  |
| Building occupancy  | 1,009  | 935  |
| Data processing expenses  | 974  | 1,033  |
| Professional and other services                                     | 580  | 593  |
| Amortization of intangible asset                                    | -  | 166  |
| Other expenses  | 982  | 906  |
| Total noninterest expense   | 7,408  | 7,397  |

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|                                       |  |           |    |        |
|---------------------------------------|--|-----------|----|--------|
| (Loss) income before income taxes     |  | (288)     |    | 785    |
| (Benefit) provision for income taxes  |  | (82)      |    | 148    |
| Net (loss) income                     |  | \$ (206)  | \$ | 637    |
| <hr/>                                 |  |           |    |        |
| Net (loss) income per share - basic   |  | \$ (0.08) | \$ | 0.26   |
| Net (loss) income per share - diluted |  | \$ (0.08) | \$ | 0.26   |
| Dividends per share                   |  | \$ 0.3075 | \$ | 0.3075 |

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



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PATHFINDER BANCORP, INC.  
 CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY  
 NINE MONTHS ENDED SEPTEMBER 30, 2008 AND SEPTEMBER 30, 2007  
 (Unaudited)

| (In thousands, except<br>share data)<br><S>  | Common          | Common          | Additional         | Retained  | Accumulated<br>Other<br>Com- | Treasury   | Total     |
|--|-----------------|-----------------|--------------------|-----------|------------------------------|------------|-----------|
|  | Stock<br>Shares | Stock<br>Amount | Paid in<br>Capital | Earnings  | prehensive<br>Loss           | Stock      |           |
| Balance, January 1,<br>2008  | 2,971,019       | \$ 30           | \$ 7,900           | \$ 21,734 | \$ (1,458)                   | \$ (6,502) | \$ 21,704 |
| Cumulative effect of a<br>change in accounting<br>principle upon the<br>change in defined<br>employee benefit plans'<br>measurement date<br>under SFAS 158 (net of<br>\$8 tax expense) |                 |                 |                    | (48)      | 13                           |            | (35)      |
| Comprehensive loss:  |                 |                 |                    |           |                              |            |           |
| Net loss   |                 |                 |                    | (206)     |                              |            | (206)     |
| Other comprehensive<br>(loss) income, net of<br>tax:   |                 |                 |                    |           |                              |            |           |
| Unrealized holding<br>losses on securities<br>available for sale (net of<br>\$175 tax benefit)   |                 |                 |                    |           | (317)                        |            | (317)     |
| Retirement plan gains<br>and losses and past<br>service liability not<br>recognized in plan<br>expenses (net of \$26 tax<br>expense)   |                 |                 |                    |           | 38                           |            | 38        |
| Total Comprehensive<br>loss  |                 |                 |                    |           |                              |            | (485)     |
| Stock options exercised  | 1,100           |                 | 9                  |           |                              |            | 9         |
| Dividends declared<br>(\$0.3075 per share)   |                 |                 |                    | (602)     |                              |            | (602)     |
| Balance, September 30,<br>2008   | 2,972,119       | \$ 30           | \$ 7,909           | \$ 20,878 | \$ (1,724)                   | \$ (6,502) | \$ 20,591 |

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|  |           |       |          |           |            |            |           |
|--|-----------|-------|----------|-----------|------------|------------|-----------|
| Balance, January 1, 2007   | 2,953,619 | \$ 29 | \$ 7,786 | \$ 21,307 | \$ (1,770) | \$ (6,502) | \$ 20,850 |
| Comprehensive income:  |           |       |          |           |            |            |           |
| Net income   |           |       |          | 637       |            |            | 637       |
| Other comprehensive income, net of tax:  |           |       |          |           |            |            |           |
| Unrealized holding losses on securities available for sale (net of \$39 tax expense) |           |       |          |           |            |            |           |
|  |           |       |          |           | 59         |            | 59        |
| Total Comprehensive income   |           |       |          |           |            |            | 696       |
| Stock options exercised  | 17,200    | 1     | 113      |           |            |            | 114       |
| Dividends declared (\$0.3075 per share)  |           |       |          | (604)     |            |            | (604)     |
| Balance, September 30, 2007  | 2,970,819 | \$ 30 | \$ 7,899 | \$ 21,340 | \$ (1,711) | \$ (6,502) | \$ 21,056 |

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

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

|   | For the nine<br>months<br>ended<br>September<br>30,<br>2008 | For the nine<br>months<br>ended<br>September<br>30,<br>2007 |
|---|---|---|
| (In thousands)  |   |   |
| <b>OPERATING ACTIVITIES</b>   |   |   |
| Net (loss) income   | \$ (206)  | \$ 637  |
| Adjustments to reconcile net (loss) income to net cash<br>provided by operating activities:   |   |   |
| Provision for loan losses   | 550   | 280   |
| Proceeds from sales of loans  | -   | 3,000   |
| Originations of loans held-for-sale   | -   | (2,973)   |
| Realized losses (gains) on sales of:  |   |   |
| Foreclosed real estate  | 79  | (15)  |
| Loans   | -   | (27)  |
| Available-for-sale investment securities  | (26)  | (108)   |
| Impairment write-down on available-for-sale securities  | 2,176   | -   |
| Depreciation  | 529   | 559   |
| Amortization of intangible asset  | -   | 166   |
| Amortization of deferred financing costs  | -   | 15  |
| Amortization of mortgage servicing rights   | 24  | 37  |
| Earnings on bank owned life insurance   | (180)   | (169)   |
| Net amortization of premiums and discounts on investment securities   | 85  | 78  |
| Decrease in accrued interest receivable   | 36  | 69  |
| Net change in other assets and liabilities  | 64  | (18)  |
| Net cash provided by operating activities   | 3,131   | 1,531   |
| <b>INVESTING ACTIVITIES</b>   |   |   |
| Purchase of investment securities available-for-sale  | (31,730)  | (17,352)  |
| Net purchases of Federal Home Loan Bank stock   | (654)   | (81)  |
| Proceeds from maturities and principal reductions of<br>investment securities available-for-sale  | 15,402  | 14,150  |
| Proceeds from sale of:  |   |   |
| Available-for-sale investment securities  | 3,494   | 359   |
| Real estate acquired through foreclosure  | 773   | 276   |
| Premises and equipment  | -   | 33  |
| Net increase in loans   | (20,729)  | (12,886)  |
| Purchase of premises and equipment  | (206)   | (602)   |
| Net cash used in investing activities   | (33,650)  | (16,103)  |
| <b>FINANCING ACTIVITIES</b>   |   |   |
| Net increase in demand deposits, NOW accounts,<br>savings accounts, money market deposit accounts, MMDA<br>accounts and escrow deposits | 12,832  | 7,351   |
| Net increase in time deposits   | 837   | 2,983   |
| Net proceeds from short-term borrowings   | 3,355   | 9,000   |

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|  |           |           |
|--|-----------|-----------|
| Payments on long-term borrowings                 | (8,610)   | (11,350)  |
| Proceeds from long-term borrowings               | 24,000    | 4,000     |
| Proceeds from trust preferred obligation         | -         | 5,000     |
| Payments on trust preferred obligation           | -         | (5,000)   |
| Proceeds from exercise of stock options          | 9         | 114       |
| Cash dividends paid                              | (440)     | (440)     |
| Net cash provided by financing activities        | 31,983    | 11,658    |
| Increase (decrease) in cash and cash equivalents | 1,464     | (2,914)   |
| Cash and cash equivalents at beginning of period | 10,213    | 13,723    |
| Cash and cash equivalents at end of period       | \$ 11,677 | \$ 10,809 |

NON-CASH INVESTING ACTIVITY

|   |        |        |
|---|--------|--------|
| Transfer of loans to foreclosed real estate | \$ 243 | \$ 109 |
|---|--------|--------|

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

PATHFINDER BANCORP, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(Unaudited)

(1) Basis of Presentation

The accompanying unaudited consolidated financial statements of Pathfinder Bancorp, Inc. and its wholly owned subsidiaries have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information, the instructions for Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes necessary for a complete presentation of consolidated financial position, results of operations, and cash flows in conformity with generally accepted accounting principles. In the opinion of management, all adjustments, consisting of normal recurring accruals, considered necessary for a fair presentation have been included.

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, 2007 and for the two 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 nine months ended September 30, 2008, are not necessarily indicative of the results that may be expected for the year ending December 31, 2008.

(2) Earnings (Loss) per Share

Basic earnings per share have been computed by dividing net income (loss) by the weighted average number of common shares outstanding throughout the three months and nine months ended September 30, 2008 and 2007, using 2,484,364 and 2,483,532 weighted average common shares outstanding for the three month period and 2,483,944 and 2,482,886 for the nine months ended, respectively. Diluted earnings per share for the three months and nine months ended September 30, 2008 and 2007 have been computed using 2,484,364 and 2,487,732 for the three month period and 2,483,944 and 2,489,292 for the nine months ended, respectively. Diluted 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. There was no dilutive effect during the three and nine months ended September 30, 2008 since the Company was in a loss position. The number of dilutive options excluded from the diluted earnings per share calculations were 1,062 and 2,892 for the three and nine months ended September 30, 2008.

(3) Pension and Postretirement Benefits

On January 1, 2008, the Company recorded a \$48,000 charge to retained earnings, representing the cumulative effect adjustment upon adopting the measurement date transition rule for the Company's pension plan and postretirement benefit plan. In accordance with SFAS 158, Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans, measurement date provisions, plan assets and obligations are to be measured as of the employer's balance sheet date. The Company previously measured its pension and postretirement plans as of October 1 of each year. As a result of the measurement date provisions, the Company decreased its retirement plan assets with a corresponding charge to retained earnings, representing the net periodic benefit cost for the period between the October 1, 2007 measurement date and January 1, 2008.



The composition of net periodic pension plan costs for the three months and nine months ended September 30, is as follows:

| (In thousands)                 | For the<br>three months<br>ended<br>September 30, |       | For<br>the nine months<br>ended<br>September 30, |        |
|--------------------------------|---|-------|--|--------|
|                                | 2008  | 2007  | 2008   | 2007   |
| Service cost                   | \$ 54   | \$ 49 | \$ 162   | \$ 147 |
| Interest cost                  | 79  | 68    | 237  | 204    |
| Expected return on plan assets | (112)   | (98)  | (335)  | (294)  |
| Amortization of net losses     | 16  | 22    | 49   | 66     |
| Net periodic benefit cost      | \$ 37   | \$ 41 | \$ 113   | \$ 123 |

The composition of net periodic postretirement plan costs for the three months and nine months ended September 30, is as follows:

| (In thousands)                        | For<br>the three months<br>ended<br>September 30, |       | For the<br>nine months<br>ended<br>September 30, |       |
|---------------------------------------|---|-------|--|-------|
|                                       | 2008  | 2007  | 2008   | 2007  |
| Service cost                          | \$ 1  | \$ 1  | \$ 2   | \$ 2  |
| Interest cost                         | 5   | 5     | 16   | 16    |
| Amortization of transition obligation | 5   | 5     | 14   | 14    |
| Net periodic benefit cost             | \$ 11   | \$ 11 | \$ 32  | \$ 32 |

The Company previously disclosed in its consolidated financial statements for the year ended December 31, 2007, that it expects to contribute \$233,000 to its plans in 2008. As of September 30, 2008, \$135,000 has been contributed to the plans.

#### (4) Comprehensive Income (Loss)

Accounting principles generally accepted in the United States of America, require that recognized revenue, expenses, gains and losses be included in net income. Although certain changes in assets and liabilities, such as unrealized gains and losses on available-for-sale securities, and gains and losses, prior service costs and transition assets or obligations for defined benefit pension and postretirement plans are reported as a separate component of the shareholders' equity section of the consolidated statements of condition, such items, along with net income, are components of comprehensive income.

The components of other comprehensive income (loss) and related tax effects for the three and nine months ended September 30, are as follows:

| (In thousands)  | For the three months<br>ended September 30, |      | For the nine months<br>ended September 30, |      |
|---|---|------|--|------|
|   | 2008  | 2007 | 2008                                       | 2007 |
| Unrealized holding gains (losses) on securities available for sale: |   |      |  |      |

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|   |          |        |            |        |
|---|----------|--------|------------|--------|
| Unrealized holding (losses) gains arising during the period             | \$ (952) | \$ 516 | \$ (2,678) | \$ 206 |
| Reclassification adjustment for losses (gains) included in net income   | 1,808    | (111)  | 2,150      | (108)  |
| Net unrealized gains (losses) on securities available for sale          | 856      | 405    | (528)      | 98     |
| Defined benefit pension and postretirement plans:                       |          |        |            |        |
| Reclassification adjustment for amortization of benefit plans'          |          |        |            |        |
| net loss and prior service liability recognized in net periodic expense | 21       | -      | 63         | -      |
| Other comprehensive gain (loss) before tax                              | 877      | 405    | (465)      | 98     |
| Tax effect  | (350)    | (162)  | 186        | (39)   |
| Other comprehensive income (loss)                                       | \$ 527   | \$ 243 | \$ (279)   | \$ 59  |

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The components of other comprehensive income, net of related tax effects, at September 30, 2008 and December 31, 2007 are as follows:

| (In thousands)  | September<br>30,<br>2008 | December<br>31,<br>2007 |
|---|--------------------------|-------------------------|
| Unrealized losses on securities available for sale (net of tax<br>benefit 2008 - \$653; 2007 - \$441) | \$ (978)                 | \$ (662)                |
| Net pension losses and past service liability (net of tax<br>benefit 2008 - \$468; 2007 - \$495)      | (703)                    |                         |